

	Quarter	FYTD	1 year	3 years	5 years	Since Inception <sup>^</sup>
	%	%	%	% p.a.	% p.a.	% p.a.
Perennial Value Wealth Defender Australian Shares Trust*	-6.1	-6.1	1.0	-	-	0.2
S&P/ASX 300 Accumulation Index	-6.5	-6.5	-0.7	-	-	-2.0
<b>Value Added (Detracted)</b>	<b>0.4</b>	<b>0.4</b>	<b>1.7</b>	<b>-</b>	<b>-</b>	<b>2.2</b>
<b>Net Performance</b>	<b>-6.3</b>	<b>-6.3</b>	<b>0.3</b>	<b>-</b>	<b>-</b>	<b>-0.5</b>

\*Gross Performance. ^Since inception: 31 May 2014. Past performance is not a reliable indicator of future performance.

## Perennial Value Wealth Defender Australian Shares Trust

The Trust aims to outperform the S&P/ASX 300 Accumulation Index by investing in a diversified portfolio of Australian shares and using protection strategies to dynamically protect the portfolio through market cycles, thereby reducing the magnitude of significant negative returns in falling equity markets.

### Trust manager:

Dan Bosscher

### Risk profile:

High

### Trust FUM\* (as at 30/09/15):

AUD 59 million

### Income distribution frequency:

Half yearly

### Strategy FUM (as at 30/09/15):

AUD 766 million

### Team FUM (as at 30/09/15):

AUD 7.3 billion

### Trust redemption price (as at 30/09/15):

\$0.9489

### Any material changes to risk profile, strategy, key service providers or portfolio managers during the period:

Nil

### Minimum initial investment:

\$25,000

### Trust inception date:

31 May 2014

### APIR code:

IOF0228AU

\*Trust FUM is equivalent to the net asset value of the Trust. It is the value of the assets less the liabilities of the Trust, as calculated in accordance with the terms of the Trust's constitution.

- ▶ **Since inception, with the market down 2.0%, the Trust is up 0.2%, outperforming the Index by 2.2%.**
- ▶ **The S&P/ASX300 Accumulation Index (the Index) finished the quarter down 6.5%.**
- ▶ **Globally, the quarter was dominated by extreme gloominess about the prospects for growth in China.**

The market sold off in the September quarter, with the ASX300 Accumulation Index (the Index) ending the quarter down 6.5% and the Trust outperforming the Index by 0.4%. The sell-off, in our view, has been very much led by global macro funds taking a very bearish view on the outlook for China and therefore Australia. The resultant downward move in share prices has also been magnified by unusually low stock turnover levels during the quarter, particularly in September, where the market fell 2.9%. Investors should note that while the market has fallen 13.9% from its peak in April, it has delivered a largely flat return of -0.7% for the last 12 months.

Fortunately for investors, over the last few months, periods of poor returns have often been followed by rallies where a considerable portion of the value lost is subsequently restored. With this higher level of volatility it is more expensive to carry protection, but it is certainly good to know it is there if situations turn for the worse. As it happened whilst the markets have been lower, and we have had a couple of big moves, such as the 12% move down up to the 24th August, the fall in the markets has been quite slow. Had the fall been quicker we would have expected the protection to have had an even more positive impact as the protection strategy works more effectively in sharper market falls.

Wealth Defender is designed to really kick in as markets capitulate, as in August, and other times to act as a traditional long only equity style investment. At the Index lows of 11.7% in August, the Trust was only down 6.8%, 4.9% higher than the Index. This represents an approximately 42% saving, consistent with our objective to cushion the impact of significant market falls.

Whilst September was a difficult month, with our stocks underperforming, we feel the protection overlay since inception continues to perform well. As at the end of September, and since inception, with the market down 2.0%, the Trust is up 0.2%, outperforming by 2.2%. For the quarter the Trust is down 6.1% against the Index which was down 6.5%, thereby outperforming by 0.4%.

For our investors we want to provide a way to access the long term benefits of Australian shares whilst providing comfort that if we do get a sudden significant fall in the market their fund comes with an in built mechanism to mitigate part of that fall. At the same time, we want to provide that without having to invest too much in the protection overlay. Most importantly over time we feel this will provide better long term returns and avoid investors selling at the bottom.

With markets exhibiting a higher level of volatility and given the fall in markets to date, we have chosen to remain cautious which means we are not trying to second guess the markets and continue to carry levels of protection that will meaningfully cushion the impact should we get a serious market capitulation. We believe we are not out of the woods yet.

Globally, the quarter was dominated by extreme gloominess about the prospects for growth in China. Key data disappointed, including the latest monthly production and investment prints, alongside the manufacturing Purchasing Managers Index (PMI) and many investors seem to be losing faith that China can maintain growth of close to the 7.0% target. This is despite even more stimulus being announced and further exchange rate depreciation. The weakness in China is reverberating through the region, with Taiwan, Singapore and now Japan in technical recession. Outside Asia, however, the news was better, with European growth seemingly tracking close to 2.0%, although inflation across the region has dropped back close to zero. Similarly, the US economy is doing well, although employment growth was unexpectedly weak early in the month. The Federal Reserve (the Fed), however, balked at raising interest rates, citing offshore “wobbles” as a key reason for caution. Equity markets had a very tough quarter, with most indexes losing further ground, as many investors reassessed the prospects of a world without the same momentum in China’s growth engine.

In Australia, the biggest development was not in economics, but in politics, with Malcolm Turnbull successfully challenging incumbent Tony Abbott to become Australia’s fifth Prime Minister (PM) in as many years. There has been no significant policy change yet, but consumer and business confidence likely will lift on hopes of a fresh start, particularly around economic reform. The domestic data was a mixed bag. Retail sales growth was weak and consumer and business confidence fell, but the August employment report was much better than expected and the jobless rate fell slightly to 6.2%. The Q2 Gross Domestic Product (GDP) report was also underwhelming, showing that growth was barely positive, albeit after a decent Q1. The Australian Dollar (AUD) weakened further over the quarter, in line with Reserve Bank of Australia (RBA) expectations, dropping below 70 US cents, and the RBA left the cash rate steady.

The other main focus of the quarter was reporting season. Results were generally in line with expectations, with industrials delivering modest Earnings per Share (EPS) growth while resource company earnings fell sharply due to lower commodity prices. Low top-line growth was again a feature of results, with a significant proportion of earnings improvement being driven by cost-out and internal improvement programs. Currency was also a major driver, with many companies beginning to see benefits from the lower AUD. This particularly favoured companies with significant offshore earnings. Outlook statements were again cautious given the uncertain economic environment and weak demand conditions both domestically and globally.

In this risk-off environment with concerns over Chinese growth, industrial and defensive sectors tended to outperform, with industrials (up 3.6%), utilities (up 1.8%), consumer staples (up 1.5%), Real Estate Investment Trust (REITs) (up 1.1%) and consumer discretionary (up 1.1%) while resources (up 16.4%) fell sharply, with energy (down 24.1%) and metals and mining (down 12.8%) and financials (down 9.6%) with the major banks falling an average of 11.3%.

#### Share portfolio news

The best performing stock in the Trust for the quarter was Asciano (up 26.3%) following a takeover offer from Brookfield. Other strong performers included BlueScope Steel (up 21.0%), Aristocrat Leisure (up 12.5%), Brickworks (up 12.5%), Orora (up 12.4%), Fairfax (up 11.0%), CIMIC Group (up 10.2%),

Flight Centre (up 8.7%), Graincorp (up 6.9%), Henderson Group (up 5.6%) and Amalgamated Holdings (up 5.2%).

In terms of stocks which detracted from performance, the sell-off in housing-related companies held in the Trust has been significant and, we believe, often indiscriminate, including Boral (down 23% off August highs), Harvey Norman and Lend Lease (both fell 20%) and Stockland (down 11%). Perennial Value does not subscribe to this sudden and negative change in sentiment, which appears to be driven by an overheated apartment building sector. Each of the building-related companies has diversified earnings streams. Boral’s domestic housing exposure represents 21% of total profits, Lend Lease around 10% and Stockland 30% to 35%. Stocks held also generally have a far greater reliance on detached housing and renovations, where the cyclical upturn to date has been more muted.

These companies have their largest presence in the eastern seaboard, especially New South Wales where the detached housing cycle most likely has at least two years to run. Queensland is only starting to improve while Victoria is likely to slow from a high level. During the quarter, Brickworks (up 12.5%) delivered a record FY15 profit result and highlighted strong momentum in building approvals on the east coast, with an “extremely strong order book in most east coast divisions”. Further, this group of companies offers significant value at current levels. Harvey Norman, for example, is currently trading on a prospective FY16 gross yield of 8.0%, Lend Lease on a FY16 P/E of 11.2x and Stockland on a FY16 price to NTA of 1.0x. Thus, we continue to retain these stocks in the Trust.

Stocks which detracted from performance included BlueScope Steel (down 28.2%) and Sims Metal (down 15.8%) after their Q3 trading update showed that constrained scrap generation and a weak export market resulted in lower scrap volumes. Coca-Cola Amatil (down 15.1%), Fairfax (down 14.7%) and Ansell (down 12.6%) also underperformed on no particular news. Flight Centre (down 14.7%) fell after indicating that its profit would come in at the lower end of its previous guidance range.

With regards to our materials and resources exposure, the Trust has held a range of companies providing select, diversified industry exposure. From a portfolio construction perspective, given global macro uncertainties, we have ensured in recent times that the Trust was not overly exposed to any one stock. Notwithstanding, this sector took the brunt of the global macro sell-off. Stock holdings which were hardest hit included AWE (down 48.8%), Origin Energy (down 47.0%), Orica (down 29.3%), Downer (down 27.6%), South32 (down 23.7%), Iluka Resources (down 18.4%) and BHP (down 14.6%).

In terms of portfolio movements, we locked in profits and reduced holdings in some of the stocks which have performed strongly in recent times including Ansell, Aristocrat Leisure, Boral, Fairfax, Harvey Norman, Orora, Macquarie Group and Sandfire Resources. Funds were reinvested into a number of stocks including AGL, CIMIC Group, Flight Centre, Orica, NAB and NewsCorp.

We also increased our holdings in ANZ and CBA, with the Trust participating in their capital raisings as well as Westpac. In mid-September, we reduced the Trust’s exposure to Origin at an average price of \$7.13 and it closed the month at \$6.10. On 30 September, Origin announced \$4.7 billion of capital initiatives, including a \$2.5 billion capital raising, to strengthen

\*\*This is an expected outcome of an overnight move based on risk modelling. While we expect this to be accurate, it relies on a number of assumptions and is used as a guide only. The actual outcome may be affected by inaccurate assumptions or by known or unknown risks and uncertainties and may differ materially from the expected outcome shown above.

its balance sheet. This comes on top of recently announced \$2.2 billion in capital initiatives, including capex reductions, reduced cost of doing business and asset sales.

### Outlook

Perennial Value Management remains alert to Environmental, Social and Corporate Governance (ES&G) issues in the Trust. During the quarter, Harvey Norman announced an investment in a dairy farming operation. In our view these types of non-core investments are not in the interests of shareholders and we expressed this to management and the board and will take the issue up again ahead of the AGM.

Top 10 Holdings		
Stock name	Trust weight %	Index weight %
Westpac Banking Corporation	7.4%	7.1%
Commonwealth Bank	7.1%	9.3%
National Australian Bank	6.9%	5.9%
BHP Billiton Limited	6.0%	5.4%
ANZ Banking Group Ltd	5.4%	5.9%
Telstra Corporation	4.9%	5.2%
Woolworths Limited	3.2%	2.4%
Macquarie Group Ltd	3.1%	1.9%
QBE Insurance Group	2.5%	1.3%
AMP Limited	2.4%	1.2%

Asset Allocation		
Sector	Trust weight %	Index weight %
Energy	4.2%	4.0%
Materials	17.9%	13.9%
Industrials	3.8%	8.0%
Consumer Discretionary	11.3%	4.7%
Consumer Staples	6.6%	7.1%
Health Care	0.3%	6.4%
Financials-x-Real Estate	36.0%	38.4%
Real Estate	3.7%	8.4%
Information Technology	0.3%	1.1%
Telecommunication Services	5.0%	5.7%
Utilities	2.4%	2.3%
Other	8.5%	-

Rounding accounts for small +/- from 100%.

Signatory of:



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