

Perennial Value Australian Shares Trust

Monthly Report as 30 June 2012

	1 Month %	3 Months %	FYTD %	1 Year %	3 Years % p.a.	5 Years % p.a.	Since Inception [^] % p.a.
Perennial Value Australian Shares Trust*	-2.2	-8.4	-10.4	-10.4	2.9	-3.3	9.9
S&P/ASX 300 Accumulation Index	0.5	-5.0	-7.0	-7.0	5.6	-4.1	6.5
Value Added (Detracted)	-2.7	-3.4	-3.4	-3.4	-2.7	0.8	3.4
Net Performance	-2.2	-8.6	-11.1	-11.1	2.0	-4.1	9.1

*Gross Performance. ^Since inception: March 2000. Past performance is not a reliable indicator of future performance.

- The Australian equities market ended higher in June.
- Financials (up 4.8%), telecommunications (up 3.6%), healthcare (up 2.5%), and staples (up 1.3%) all outperformed.
- During the month, ASX and Crown were added to the Trust.

The Australian equities market ended higher in June, with the S&P/ASX300 Accumulation Index (the Index) up 0.5%. The Perennial Value Australian Shares Trust (the Trust) finished the month down 2.2%, underperforming the Index return by 2.7%.

In what could well be described as a perfect storm this month, a number of the Trust holdings experienced a complete and absolute disconnect between prevailing share prices and true underlying value. The ongoing macro economic dominance surrounding Europe further fuelled the 'risk-off' trade and, in the Australian sharemarket context, this was played out through a major sell-off in a number of cyclical stocks held in the Trust. On top of this, there has been ongoing selling pressure from short-sellers in these same stocks. The negative effect which these factors have had on stocks is magnified in the current environment of low overall volumes being traded in the Australian sharemarket.

International markets performed strongly with the S&P500 up 4.0%, the FTSE100 up 4.7% and the Nikkei 225 up 5.4%. Domestic economic data was broadly positive, with March quarter GDP growth of 1.3% versus the prior quarter, well ahead of market expectations. The unemployment rate moved slightly higher to 5.1%. The Reserve Bank of Australia reduced the cash rate a further 25 basis points to 3.5%. The Australian dollar bounced back above parity with the USD finishing 5.2 cents higher at USD1.024. Globally, however, weakening economic data forced the Chinese central bank to cut interest rates by 25 basis points for the first time since 2008.

While the market registered an overall gain, the divergence in the sectoral performances highlights the extent to which sharemarket investors again shunned

Perennial Value Australian Shares Trust Facts:

The Trust aims to grow the value of your investment over the long term via a combination of capital growth and tax effective income, by investing in a diversified portfolio of Australian shares, and to provide a total return (after fees) that exceeds the S&P/ASX 300 Accumulation Index measured on a rolling three-year basis.

Trust Manager:

John Murray

Trust FUM

(as at 30/06/12):

AUD1.8 billion

Team FUM

(as at 30/06/12):

AUD7.3 billion

Trust Inception date:

March 2000

Risk Profile:

High

Income Distribution

Frequency:

Half yearly

Minimum Initial

Investment:

\$25,000

APIR code: IOF0200AU

cyclicals in favour of defensives. Financials (up 4.8%), telecommunications (up 3.6%), healthcare (up 2.5%), and consumer staples (up 1.3%) all outperformed. Energy (down 6.2%), materials (down 3.5%), and consumer discretionary (down 0.7%) ended the month lower.

We are not at all comfortable with this flight to safety stance taken by investors. For example, infrastructure stocks have been highly prized due to supposedly strong dividend yields. Perennial Value's proprietary research indicates that the free cash flows generated by these businesses are not sufficient to sustain the supposed dividend yields which have led many investors to invest in these stocks. Thus, we do not hold companies such as

Transurban Group, Sydney Airport, Duet Group and Envestra Limited. Further, as a value investor, we cannot justify investing in the healthcare sector on the basis that the stocks are very expensive. For example, CSL Limited trades on a prospective FY13 P/E of 18.7x, a 78% premium to the current market P/E of 10.4x. We do not hold this stock as, while it is a good business, in our view it simply does not represent value.

Other stocks which performed strongly and which we do not hold include News Corporation Limited (up 9.1%), QBE Insurance Group Limited (up 8.1%) and Westfield Group (up 4.5%).

Stocks in which we hold overweight positions which outperformed included ANZ (up 5.4%), NAB (up 4.7%) and Telstra Corporation Limited (Telstra) (up 3.9%). Telstra is not a "default holding" for us as a value manager, however, we have held a large position in this stock during the year and it has delivered significant outperformance. Another positive contributor to the Trust has been GrainCorp Limited (up 1.2%). This stock has been a strong performer, outperforming the market by 29.1% over the past year.

The worst performing stocks included Aquarius Platinum Limited (Aquarius Platinum) (down 41.7%), Billabong International Limited (Billabong) (down 29.6%), Seven West Media Limited (Seven West Media) (down 29.4%), Qantas Airways Limited (Qantas) (down 27.9%), FKP Property Group (FKP) (down 18.8%), Boral Limited (down 16.4%), and Myer Holdings Limited (Myer) (down 16.1%). Billabong announced an earnings downgrade driven by the extreme weakness in Europe in recent weeks. Additionally, the company announced a discounted capital raising via a six for seven non-renounceable rights issue at \$1.02, proceeds of which will be used to repay debt. We took up our full entitlement at this issue price (versus a month end closing price of \$1.075). While we had factored in weaker earnings from Europe, we were disappointed by the amount of capital raised as it has only been four months since the company announced the 51.5% profitable sale of a portion of its Nixon (mainly watches and accessories) business for a net \$285 million. This transaction, coupled with the bids the company

subsequently received in late February from private equity firm TPG further vindicates the value in Billabong's brands, which is one of the reasons we were attracted to this company initially. The largest shareholder, with a stake of approximately 16%, who is also the founder of the company and remains a Non-Executive Director, rejected TPG's offers and thereafter went so far as to personally purchase \$7.9 million of stock on market at an average price of \$3.13, which we viewed positively. Needless to say we were wrong. We are monitoring our current position closely and are encouraged by the founder now being more amenable to engaging with private equity.

We are cutting our losses in a number of holdings, including Aquarius Platinum, Seven West Media, Seven Group Holdings Limited and Qantas. We have acted decisively in selling down and the common theme here is that their underlying trading environments, and therefore profitability, are continuing to decline. We also reduced our weighting in BHP Billiton Limited. While the company is financially very strong, we believe that the commodity super cycle has peaked and find it difficult to see strong share price appreciation from here.

Myer, in our opinion, remains very cheap at current, depressed levels. Taking a medium-term view on mid-cycle earnings and multiples leads to a share price of around \$2.30 a share, which represents 43% upside from the current very depressed levels of \$1.62. Short selling has compounded the share price in the short-term on supposed balance sheet concerns and we do not share the market's view on this. The value inherent in this company is also highlighted by a very attractive prospective FY12 gross yield of 17.6%.

In a similar vein, FKP remains outstanding value. The share price of 37 cents compares to Perennial Value's calculation of net tangible assets (NTA) of \$1.10, a 66% discount. Given the recent interest rate cuts, we believe earnings in FY13 should begin to pick up for FKP's residential land developments and retirement units and the cash generated will allow further debt reduction. The recently announced proposal for a de-merger of the two businesses is a potential catalyst to move the share price

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closer to NTA given corporate interest in the separate assets.

The current operating environment for Sims Metal Management Limited (Sims) remains challenging and, if margins continue at current low levels, further industry consolidation is inevitable. Sims' strong balance sheet should enable it to participate in any consolidation and therefore increase its market position. Looking beyond the current environment to a mid cycle view could see share price upside to around \$15 a share, some 57% above current levels.

In terms of reinvesting share sale proceeds, the share price falls of a number of higher quality companies has seen their current valuations trading lower than long term averages. This has presented us with the opportunity to introduce both ASX Limited (ASX) and Crown Limited (Crown) into the Trust. This valuation opportunity is highlighted by the fact that the Trust has never previously held either of these stocks.

ASX is a high return on capital, highly cash generative business with a monopoly position in its key divisions. While some competition has entered the equity execution business the impact has been muted to date. ASX has historically traded on a high earnings multiple given its underlying characteristics with a ten year average P/E of 18.9x and P/FCF 16.3x. The stock is currently trading on a P/E of 13.6x and P/FCF of 13.3x, some 28% and 18% below its long term average respectively, in an environment where market turnover, a key driver of earnings, is at cyclical lows.

Crown is Australia's premium casino operator and is currently completing a major capital refurbishment of its two Australian casinos in Melbourne and Perth. They are the key drivers of the company's earnings and this is complemented with a growing Asian presence, most notably to date in Macau. Crown should derive strong cash flows from its revitalised Australian casinos, enough to retire debt over the next three years excluding any further growth plans.

At month end, stock numbers stood at 49 with cash at 2.4%.

Top 10 Holdings as at 30 June 2012

Stock	Trust Weight %	Index Weight %
ANZ Banking Grp Ltd	8.2%	5.9%
Commonwealth Bank.	7.8%	8.5%
National Aust. Bank	7.5%	5.3%
Telstra Corporation.	7.2%	4.6%
BHP Billiton Limited	7.2%	10.1%
Westpac Banking Corp	5.2%	6.5%
Rio Tinto Limited	4.2%	2.5%
Woodside Petroleum	3.6%	1.9%
Brambles Limited	2.9%	1.0%
Macquarie Group Ltd	2.8%	0.9%

Asset Allocation as at 30 June 2012

Asset Class	Trust Weight %	Index Weight %
Energy	4.9%	6.9%
Materials	25.8%	22.2%
Industrials	4.6%	7.1%
Consumer Discretionary	10.8%	3.7%
Consumer Staples	3.5%	8.3%
Health Care	0.0%	4.1%
Financials-x-Real Estate	33.9%	33.1%
Real Estate	5.0%	7.3%
Information Technology	0.0%	0.7%
Telecommunication Services	7.2%	4.9%
Utilities	0.6%	1.9%
Other	3.6%	-

Rounding accounts for small +/- from 100%.

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