

# Perennial Value Shares for Income Trust

Monthly Report as at 31 December 2013

|  | 1 Month %   | 3 Months % | FYTD %      | 1 Year %   | 3 Years % p.a. | 5 Years % p.a. | Since Inception <sup>^</sup> % p.a. |
|--|-------------|------------|-------------|------------|----------------|----------------|-------------------------------------|
| Perennial Value Shares for Income Trust* | 0.4         | 3.5        | 12.7        | 23.0       | 13.3           | 14.4           | 7.6                                 |
| S&P/ASX 300 Accumulation Index           | 0.8         | 3.4        | 14.0        | 19.7       | 8.5            | 12.3           | 5.9                                 |
| <b>Value Added (Detracted)</b>           | <b>-0.4</b> | <b>0.1</b> | <b>-1.3</b> | <b>3.3</b> | <b>4.8</b>     | <b>2.1</b>     | <b>1.7</b>                          |
| Capital Growth                           | -0.6        | 2.3        | 9.8         | 17.3       | 7.2            | 8.7            | 1.3                                 |
| Income Distribution                      | 0.9         | 0.9        | 2.5         | 4.7        | 5.3            | 4.9            | 5.5                                 |
| Net Performance <sup>^^</sup>            | 0.3         | 3.3        | 12.2        | 22.0       | 12.5           | 13.6           | 6.8                                 |

\*Gross Performance. ^Since inception: December 2005. ^^This refers to the Trust's gross performance net of investment management fees. Past performance is not a reliable indicator of future performance.

- During December, the Trust became entitled to dividends from Australand and Stockland.
- Henderson Group (up 9.7%) was the Trust's best performing stock for the month.
- The Trust has delivered a very strong total return of 23.0% for the past 12 months, outperforming the Index return of 19.7% by 3.3%.

## Trust Characteristics

In line with the objective, the Perennial Value Shares for Income Trust (the Trust) continues to invest in a portfolio of financially sound companies which demonstrates superior dividend yield characteristics to the overall stock market.

## Dividend Activity

During December, the Trust became entitled to dividends from Australand and Stockland.

## Trust Activity

December was a quiet month in terms of Trust activity, with no stocks added or removed. During the month, however, three of our portfolio holdings undertook demergers. Amcor spun out its Australian packaging and US distribution business into a new entity named Orora, Brambles spun off its Recall document management business and Macquarie Group distributed its holding in Sydney Airport to its shareholders via an in-specie distribution. We sold out of the holdings we received in each of these stocks as, in the case of Orora and Recall, the gross yields on offer were not compelling, being below market average, particularly given the relatively modest underlying growth outlooks for these businesses. We sold out of Sydney Airport as, while gross yield appeared reasonable at 6.4%, Sydney Airport falls into the category of highly-g geared infrastructure stocks, paying dividends out of debt, which we avoid in favour of companies with true cash yield generated from operating cash flow with conservative balance sheets.

At month end, stock numbers were 35 and cash was 4.8%.

## Perennial Value Shares for Income Trust Facts:

The Trust aims to provide investors with an attractive level of tax effective income, which the Trust aims to pay via quarterly distributions. The Trust aims to provide a dividend yield, adjusted for applicable franking credits and before fees, above that provided by the S&P/ASX 300 Accumulation Index\*.

|   |  |
|---|--|
| <b>Portfolio Manager:</b><br>Stephen Bruce            | <b>Risk Profile:</b><br>High                       |
| <b>Trust FUM (as at 31/12/13):</b><br>AUD73.4 million | <b>Income Distribution Frequency:</b><br>Quarterly |
| <b>Team FUM (as at 31/12/13):</b><br>AUD8.4 billion   | <b>Minimum Initial Investment:</b><br>\$25,000     |
| <b>Trust Inception date:</b><br>December 2005         | <b>APIR code:</b><br>IOF0078AU                     |

\*Gross dividend yield

## Stock and Trust Performance

The Trust has delivered a very strong total return of 23.0% for the past 12 months, outperforming the S&P/ASX 300 Accumulation Index (the Index) return of 19.7% by 3.3%. Notwithstanding the yield focus of the Trust, it is pleasing to have outperformed the market during a period of such strong total returns.

The Australian market resumed its advance in December, with the Index increasing 0.8%. The Trust delivered a return of 0.4% for the month, underperforming the index return by 0.4%.

The better performing sectors during December were telecommunications (up 4.3%), energy (up 3.3%), industrials (up 2.6%), materials (up 2.3%) and consumer discretionary (up 1.9%), while REITs (down 1.3%) and financials (down 1.0%) underperformed.

The main issue dominating global markets during the month was the decision of the US Federal Reserve to begin tapering its bond buying program, reducing purchases by USD10 billion to USD75 billion per month from January. Markets took this in their stride, with further positive economic data lifting the S&P500 2.4% in December to a new record high. The FTSE (up 1.5%) and the Nikkei 225 (up 4.0%) both rose, while the Shanghai Composite was down 4.7%. WTI oil rallied 6.2% to close at US\$98/b, copper was stronger, up 5.2% to US\$3.40/lb while iron ore fell 1.6% and gold continued its fall, down 3.9% to US\$1,202.

Domestic data was mixed, with Q3 GDP growing below trend at 2.3% pa, unemployment rising marginally and business confidence slipping, while building approvals and retail sales improved. The Reserve Bank of Australia (RBA) left interest rates on hold at 2.5% and the AUD continued its decline, finishing the month down 2 cents at USD0.89.

The best performing stock in the Trust was Henderson Group (up 9.7%). With its UK earnings, Henderson is leveraged to a lower AUD and to an improvement in the European economic and financial markets outlook. Since we added Henderson to the Trust in July 2013, it has delivered a total return of 64.5%. Other strong performers included Australand (up 5.3%), Premier Investments (up 4.5%), Amcor (up 4.3%) and Woodside Petroleum (up 4.0%). Telstra (up 3.8%) rose on the sale of its Hong Kong mobiles business for \$2.0 billion. The market reacted positively to this announcement as the business is non-core to Telstra and the cash received will further underpin the dividend paying ability of the company. At the month end share price of \$5.25, the stock is offering a very attractive FY14 gross yield of 8.2%, and this is expected to grow over time.

The worst performing stock in the portfolio was QBE (down 26.5%), which significantly reduced profit guidance after a review of its US businesses resulted in a significant strengthening in insurance reserves and a reassessment of the prospects of the lenders placed insurance business. While the magnitude of the downgrade was disappointing, we believe that the company's new management has now set the company on a far more conservative and sustainable footing than their predecessors. While risks remain, in our view these are outweighed by the potential for significant medium-term upside from rebased earnings and market expectations. From a valuation perspective, at

the month-end closing price of \$11.51, QBE appears to offer very good value on a FY14 P/E of 10.4x. This represents a significant 26% discount to the overall market FY14 P/E of 14.0x with greater earnings and dividend upside medium term.

#### Outlook

The current financial year has begun positively, with the Index up 14.0% and positive economic signals in many markets. However, the level of macroeconomic uncertainty remains high and ongoing volatility is likely. Longer-term, however, as economic growth resumes, company profits should grow and dividends paid to shareholders should increase, providing a growing stream of reliable, tax-effective income to investors.

#### Top 10 Holdings as at 31 December 2013

| Stock                | Trust Weight % | Index Weight % |
|----------------------|----------------|----------------|
| BHP Billiton Limited | 9.5            | 9.1            |
| National Aust. Bank  | 7.4            | 6.1            |
| ANZ Banking Grp Ltd  | 7.4            | 6.6            |
| Westpac Banking Corp | 7.2            | 7.5            |
| Telstra Corporation. | 7.1            | 4.9            |
| Commonwealth Bank.   | 6.9            | 9.4            |
| Woodside Petroleum   | 4.0            | 1.8            |
| CASH                 | 3.1            | 0.0            |
| Wesfarmers Limited   | 3.0            | 3.8            |
| Macquarie Group Ltd  | 2.8            | 1.3            |

#### Asset Allocation as at 31 December 2013

| Asset Class                | Trust Weight % | Index Weight % |
|----------------------------|----------------|----------------|
| Energy                     | 6.5            | 5.9            |
| Materials                  | 17.2           | 17.9           |
| Industrials                | 3.5            | 6.7            |
| Consumer Discretionary     | 10.8           | 4.8            |
| Consumer Staples           | 3.9            | 8.2            |
| Health Care                | 0.0            | 4.7            |
| Financials-x-Real Estate   | 39.2           | 37.5           |
| Real Estate                | 6.7            | 6.6            |
| Information Technology     | 0.0            | 0.9            |
| Telecommunication Services | 7.1            | 5.3            |
| Utilities                  | 0.0            | 1.6            |
| Other                      | 5.0            | 0.0            |

Rounding accounts for small +/- from 100%.

Signatory of:



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