Perennial Concentrated Australian Shares Trust

Perennial Partners

Monthly Report May 2024

	Month (%)	Quarter (%)	FYTD (%)	1 Year (%)	2 Years (% p.a.)	3 Years (% p.a.)	5 Years (% p.a.)	Since Inception^ (% p.a.)
Perennial Concentrated Australian Shares Trust (Net)	1.1	4.1	11.1	13.1	9.5	7.0	7.9	7.3
S&P/ASX 300 Accumulation Index	0.9	1.1	10.9	12.8	7.5	6.5	7.8	8.4
Value Added	**0.2**	**3.0**	**0.2**	**0.3**	**2.0**	**0.5**	**0.1**	**-1.1**

^Since inception: May 2017. Past performance is not a reliable indicator of future performance.

Overview

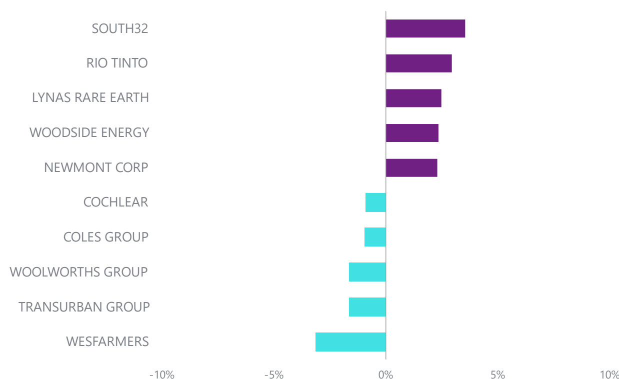
Markets rallied in May, recovering from last month's sell-off. The US market was particularly strong, with an "in line" CPI figure easing inflation fears and propelling the S&P500 (+4.8%) and NASDAQ (+6.9%) to new highs. As usual, NVIDIA had an outsized impact on markets, continuing its phenomenal upwards move. Other markets were also positive, with the FTSE100 (+1.6%) and Nikkei 225 (+0.2%) both rising. The exception was the Chinese market, with the Shanghai Composite (-0.6%) for the month and being the only major market to post a negative return for the last 12 months. While a range of steps have been taken by the Chinese authorities to support the housing market, a new round of tariffs has caused concerns about exports, which have been key to supporting their economy recently.

The Australian market also posted a gain, with the ASX300 Accumulation Index rising +0.9%, to have delivered a healthy return of +12.8% over the last 12 months. During the month, the Government delivered its budget, which while stimulatory, was accompanied by a benign inflation forecast (albeit at odds with the views of the RBA). The market took this forecast, combined further evidence that the economy is slowing, as suggesting that rate cuts may be coming. This boosted the rate-sensitive sectors of the market, with IT (+4.5%), Utilities (+3.4%) and REITs (+1.9%) all outperforming. The banks also outperformed modestly (average +3.5%). By contrast, consumer facing sectors such as Staples (-1.0%) and Discretionary (-0.9%) underperformed.

Growth of $100,000 Since Inception

Performance shown net of fees with distributions reinvested. Does not take into account any taxes payable by an investor. Past performance is not a reliable indication of future performance.

Top 5 Over / Underweight Positions vs Index



Fund Characteristics

The aim of the Trust is to grow the value of your investment over the long term by investing in a concentrated portfolio of Australian companies and to provide a total return that exceeds the S&P/ASX300 Accumulation Index measured on a rolling three-year basis.

Portfolio Manager
Stephen Bruce

Trust FUM
AUD $25 million

Distribution Frequency
Half yearly

Minimum Initial Investment[1]
$50,000

Trust Inception Date
May 2017

Fees
0.70% p.a. + Performance fee

APIR Code
WPC6780AU

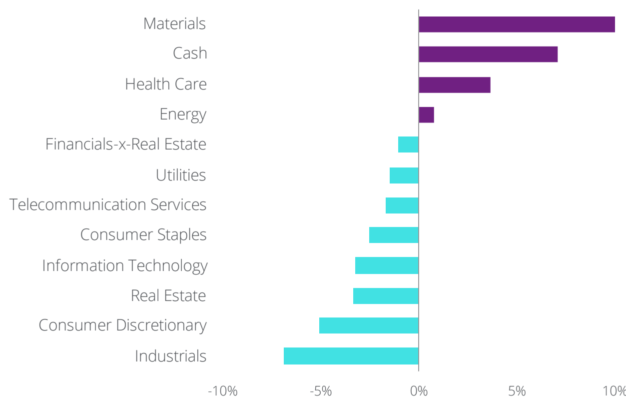
[1] Perennial Concentrated Australian Shares Trust is open to wholesale investors only.

Portfolio Characteristics – FY25	Trust	Market
Price to Earnings (x)	14.9	16.2
Price to Free Cash Flow (x)	11.6	13.7
Gross Yield (%)	5.1	5.1
Price to NTA (x)	2.2	2.6

Source: Perennial Value Management. As at 31 May 2024

The above figures are forecasts only. While due care has been used in the preparation of forecast information, actual outcomes may vary in a materially positive or negative manner.

Sector Active Exposure vs Index



Trust Review

The Trust returned +1.1%, after-fees in May, outperforming the benchmark by +0.2%.

Key contributors to performance over the month included Telix Pharmaceuticals (+20.6%), which rallied after announcing positive clinical trial data regarding their prostate cancer therapeutic. This comes on top of continuing strong sales of their prostate imaging agent which is gaining significant market share due to its logistical benefits versus existing products. In addition to their prostate imaging and therapeutic products, the company has a strong pipeline of other potential imaging agents and therapies. Should any of these prove to be successful, there is significant upside to the current share price. However, the stock has risen significantly, returning over +100% from our purchase price, and we have been taking profits and progressively trimming our position.

Gaming machine manufacturer, Aristocrat Leisure (+13.5%), outperformed after delivering a solid half-year result. Despite overall market softness, the company continues to gain market share. Importantly, they continue to build their number of participation machines. This is where, rather than making an outright sale, Aristocrat provides the machine in exchange for a share of the revenue it generates. While more capital intensive, this creates a higher-quality, annuity-style revenue stream. The company also announced a review of certain non-core assets, which if sold, would further bolster the company's already debt-free balance sheet.

Resources holding had mixed fortunes in May. Strength in aluminium and manganese saw South32 (+10.6%) rally strongly. Ironically, the strength in the manganese price was largely driven by a ship crashing into the loading dock of South32's Groote Eylandt manganese operation, which will prevent any exports for the remainder of 2024. The copper price stabilised after its spectacular recent run and saw some profit taking in copper names, including Sandfire Resources (-3.1%). The iron ore price continued to be strong, rising +6% to US$118/t. However, more negative China sentiment on the back of new tariffs, saw Rio Tinto (-1.2%) and Fortescue Metals (-5.0%) both underperform. By contrast, BHP (+3.4) outperformed after walking away from their bid for Anglo American. While the bid made strategic sense, as with any takeover, price matters, and it was good to see BHP being disciplined with use of shareholders' capital.

ANZ, NAB and Westpac reported their half-year results during the month. Overall, the results were in-line with, to marginally positive vs expectations, seeing the sector rise an average of +3.5%. However, there was nothing in it to change our view that the sector will struggle to generate any meaningful earnings growth in the near term. Credit growth is modest, and margins remain under pressure, limiting revenue growth. Costs and productivity continue to be a focus, but like all other businesses, the banks are facing high cost inflation. EBAs are locking in higher wage growth and external software vendors a jacking up prices. While regulatory-related spending is rolling off, new areas like cyber spend are taking its place. All this adds up to a pretty flat pre-provision profit growth outlook. While the commentary suggested that some competitive pressures on margins are easing slightly, if the RBA cuts rates, then that will hurt margins. While a rate cut cycle does give the banks the opportunity to reprice, it would be a courageous CEO who doesn't pass on the first few cuts in full! Credit quality is deteriorating slightly, but still remains strong, with the bad debt expense at very low levels by historical standards. Obviously, how this plays out will depend on the direction of the economy.

On the positive, the banks all remain well-provisioned, and in strong balance sheet positions, with CET1 capital at the top of their target ranges and high levels of liquidity. This has allowed them to increase dividends and buy-backs. However, in terms of valuation, while the sector is trading around its long-term average relative to the broader Industrials market, in absolute terms, the sector is as expensive as it has ever been. With soft landing being most people's base case assumption, the risk to earnings is skewed to the downside. Putting this all together, we are running a slight underweight in the sector.

The main detractors over the month were Nufarm (-12.9%), which reported a poor result, impacted by global de-stocking in the ag-chem supply chain. Looking forward, this will normalise over the coming season and, importantly, the seeds business continued to grow strongly. Other detractors included, Iluka Resources (-6.9%) and Orora (-6.4%). We continue to be positive on the longer term outlooks for each of these stocks.

Trust Activity

During the month, we locked in profits and trimmed our holding in Telix, following its strong performance, as well as reducing our overweight in Pilbara Resources. Proceeds were used to increase our holding in Telstra which was looking very attractive following some recent share price weakness. At month end, stock numbers were 30 and cash was 6.9%.

Outlook

Globally, inflation continues to moderate, albeit at a slowing pace, as while goods inflation has fallen sharply, services inflation is proving more persistent. While the expected timing of interest rate cuts has been pushed out, the consensus view is that rate cuts are coming, and a soft landing will be achieved. This would be an excellent outcome. However, history suggests that soft landings are few and far between, so a degree of caution is warranted. Should inflation prove resurgent, then the sentiment could change quickly. Given that much of the market – particularly the Tech sector – is very fully-valued, there is not much margin for error here.

While corporate earnings have generally proven resilient to date, outside of the US, there is clear evidence that growth is slowing. In Australia, economic growth has stalled, and the economy has been in a pre-capita recession for some time now. While the upcoming tax cuts will boost disposable income, there are signs the labour market is beginning to soften, leaving us cautious on the consumer. Further, immigration – a key plank of our growth – has become a political issue and is set to be reduced. In terms of Resources, demand for most commodities remains healthy and supply is generally constrained. However, while the Chinese Government has taken steps towards stabilising the property market, renewed trade tensions and the prospect of new tariffs puts a question over the outlook for growth in their manufacturing sector.

While there is a high level of economic uncertainty, our focus remains on investing in quality companies with proven business models and strong balance sheets, which are offering attractive valuations and have the ability to deliver high levels of franked dividend income to investors.

Invest Online Now

Contact us

Level 27, 88 Phillip Street
Sydney NSW 2000

1300 730 032

invest@perennial.net.au

www.perennial.net.au

Signatory of:

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