Perennial Value Shares for Income Trust

MONTHLY REPORT AUGUST 2020

	Month (%)	Quarter (%)	FYTD (%)	1 Year (%)	3 Years (% p.a.)	5 Years (% p.a.)	Since Inception (%p.a.)
Income Distribution	0.4	1.4	0.8	5.1	7.9	8.1	6.3
Capital Growth	1.4	1.9	0.1	-16.2	-7.9	-5.8	-1.3
Total Return	1.8	3.3	0.9	-11.1	-0.1	2.3	5.0
Franking Credits#	0.2	0.6	0.4	2.3	3.5	3.1	2.3
Income Distribution including Franking Credits	**0.6**	**2.0**	**1.2**	**7.4**	**11.4**	**11.2**	**8.6**
Benchmark Yield including Franking Credits*	0.8	1.0	0.8	4.2	5.6	5.9	6.0
Excess Income to Benchmark#	**-0.2**	**1.0**	**0.4**	**3.2**	**5.8**	**5.3**	**2.6**

#Franking credits are an estimate as tax components will only be known with certainty at the end of the financial year. Since inception: December 2005. *Benchmark yield including franking credits is calculated as the difference between the return on S&P/ASX300 Franking Credit Adjusted Daily Total Return Index (Tax Exempt) and the return of the S&P/ASX300 Index. Past performance is not a reliable indicator of future performance.

Overview

- Global markets were strong in August, with all major indices rising, as positive announcements around vaccine trials outweighed concerns around increasing COVID-19 infections in many countries.
- The Australian market also delivered a strong performance, with the ASX300 Accumulation Index logging its fifth consecutive positive month, rising +3.0%. This was achieved despite the impacts of the lockdown in Victoria.
- Looking to FY21, the Trust is targeting a pre-tax distribution yield of around 7%. While market dividends will be lower, the Trust will seek out the best dividend opportunities and may seek to supplement income generation by undertaking limited call-writing.

Perennial Value Shares for Income Trust

The objective of the Trust is to provide investors with an attractive level of tax effective income, paid via monthly distributions. The Trust aims to provide a gross distribution yield, adjusted for applicable franking credits, above that provided by the S&P/ASX300 Franking Credit Adjusted Daily Total Return Index (Tax-Exempt).

Portfolio Manager	Trust FUM	
Stephen Bruce	AUD $20 million	
Distribution Frequency	**Minimum Initial Investment**	
Monthly	$25,000	
Trust Inception Date	**Fees**	**APIR Code**
December 2005	0.92%	IOF0078AU

Portfolio Characteristics – FY22	Trust	Market
Price to Earnings (x)	14.7	17.0
Price to Free Cash Flow (x)	13.4	16.5
Gross Yield (%)	6.5	4.6
Price to NTA (x)	2.0	2.2

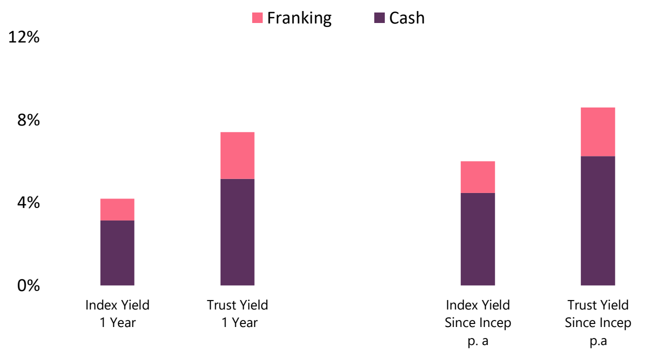
Source: Perennial Value Management. As at 31 August 2020

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.

Franking Levels (%)

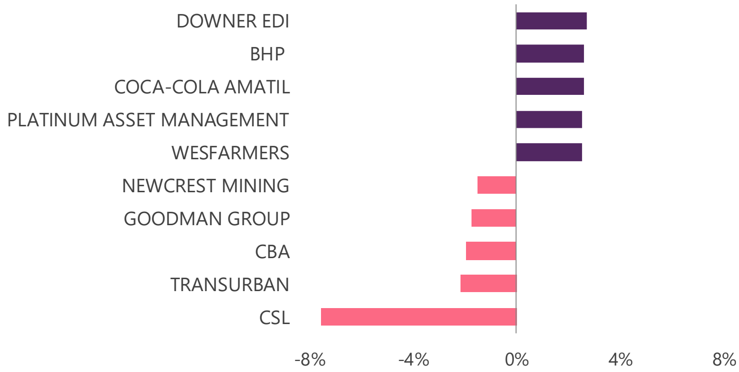
FY20	94.4	FY17	65.6
FY19	95.1	FY16	55.9
FY18	99.2	FY15	88.4

Distribution Yield

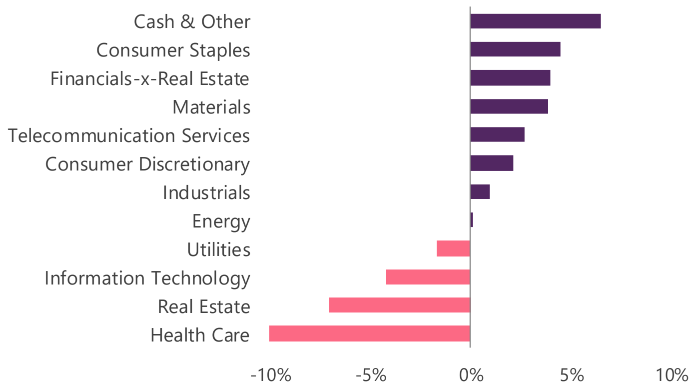


Does not take into account any taxes payable by an investor. Past performance is not a reliable indication of future performance.

Top 5 Over / Underweight Positions vs Index



Sector Active Exposure vs Index



Trust Review

Global markets were strong in August, with all major indices rising, as positive announcements around vaccine trials, outweighed concerns around increasing COVID-19 infections in many countries. The Australian market also delivered a strong performance, with the ASX300 Accumulation Index logging its fifth consecutive positive month, rising +3.0% in August and having now risen +35.4% from its March low. This was achieved despite the impacts of the lockdown in Victoria.

In line with offshore markets, the rally in Tech stocks saw IT (+15.2%) the best performing sector during the month. This was led by Afterpay (+33.4%), which currently has market capitalisation of over $20bn. This is very impressive for a business generating no earnings (or dividends) and operating in a sector with no barriers to entry. Time will tell if this is justified, but we would argue its true value is closer to zero. Needless to say, this stock does not look like a good investment proposition to us. The Consumer Discretionary sector (+9.7%) also performed well, as spending remained robust, particularly through online channels, while the REIT sector (+7.9%) also made up some of its lost ground. Defensive sectors generally underperformed, with Utilities (-4.8%), Telcos (-3.8%) and Consumer Staples (-0.3%). Metals & Mining (+0.4%) lagged, having performed strongly in recent months, while Financials (+1.3%) also underperformed.

The highlight of the month was the company reporting season. Never before has the market entered a reporting season in such an information vacuum, with virtually all companies having previously withdrawn guidance due to COVID-19 uncertainty. As a broad statement, while many companies are being significantly impacted, results were less bad than feared. After the initial shock of lockdowns, many companies are seeing a reasonable activity levels as economies progressively reopen. Those most impacted are adapting to the current environment by reducing costs, hunkering down and strengthening their balance sheets.

Holdings which outperformed over the month included mining services company Monadelphous (+26.7%), which delivered a better than expected result and has a strong pipeline of work ahead of it, particularly in the iron ore sector. Seven Group Holdings (+12.0%) also delivered a solid result and is also poised to benefit from the ongoing strength in the iron ore sector which is its Caterpillar equipment business services. Graincorp (+15.3%) rallied on the positive seasonal outlook, with a big east coast grain crop expected to drive large volumes through its grain handling and export operations. Coca-Cola Amatil (+12.3%) and Event Hospitality (+11.8%), with their exposure to the domestic economy, both rose in anticipation of economic reopenings.

The major banks lagged slightly (average +1.1%) in August. During the month CBA reported its full-year result, while the others delivered quarterly trading updates. While the current mortgage and business loan repayment holidays have been extended until March next year, indications are that a significant proportion of borrowers will return to making payments well before this time. Trust holds a significant position in the sector as we see material medium-term valuation upside. Further, the sector is highly leveraged to any improvement in the domestic outlook.

Telstra (-11.3%) detracted from performance, after delivering a slightly soft result and guiding to a lower long-term return target. We continue to see Telstra as offering an attractive dividend yield and standing to benefit from the ongoing growth in mobile and the roll out of 5G.

Trust Activity

During the month, the Trust exited a number of holdings including TPG Telecom, IAG and Janus Henderson and reduced our holding in Rio Tinto. Proceeds were used to increase our holdings in a number of stocks including ANZ, which paid its interim dividend during the month, having previously deferred it due to uncertainty around the outlook. Holdings were also increased in Aurizon, Amcor and Coca-Cola Amatil which offer relatively certain earnings and attractive dividend yields. The Trust also participated in a capital raising by Tabcorp. At month end, stock numbers were 31 and cash was 6.5%.

Distribution

In order to provide a regular income stream, the Trust pays monthly distributions. We aim to pay equal cash distributions each month, based on our estimate of the dividend income to be generated over the year. Franking credits, surplus income and any realised capital gains will then be distributed, as per usual, with the June distribution.

The Trust declared a distribution for August of 0.35cpu, bringing the total income return for the last 12 months to 5.1% or 7.4% including franking credits.

Looking forward, the outlook for dividends for FY21 will become clearer over the next few months. While it is certain that many companies will be reducing their dividends, the market overall should still be expected to generate an attractive level of dividend income in the year ahead, particularly compared to other alternative sources of yield. In addition, we may seek to enhance the income generation of the Trust by undertaking limited call-writing. At this stage, we are targeting a pre-tax distribution yield of approximately 7.0% for the FY21 financial year.

Outlook

The market has rallied strongly from its March lows, however, is still well down from its previous highs. While the sharp slowing of activity means that forecasting near-term earnings for many companies is difficult, the market's fall means a significant amount of bad news is now factored into the share prices of many companies.

Looking forward, while the current situation is unprecedented, so too has been the response of governments, with coordinated policies covering monetary easing, fiscal stimulus and legislative actions. While the renewed lockdown in Victoria is a clear setback, Australia has, so far, fared very well relative to most other countries, meaning it is reasonable to expect that we are well placed to lead others in terms of a recovery in activity.

Finally, the silver lining of a downturn such as this is that it provides the long-term investor with opportunities to buy quality businesses at very attractive prices. Indeed, we have been taking the opportunity to add a number of new stocks to the portfolio which we are confident will deliver strong returns to investors over time.

In the meantime, the Trust continues to offer a higher forecast gross yield than the overall market and, as always, our focus will continue to be on investing in quality companies with strong balance sheets, which are offering attractive valuations and have the ability to deliver high levels of franked dividend income to investors. Further, we believe the current very low interest rates highlight the relative attractiveness of financially-sound, high dividend yielding equities.

Invest Online Now

Level 27, 88 Phillip Street Sydney NSW 2000 | 1300 730 032 | invest@perennial.net.au | www.perennial.net.au