Perennial Value Shares Wholesale Trust

Perennial Partners

Monthly Report January 2024

	Month (%)	Quarter (%)	FYTD (%)	1 Year (%)	2 Years (% p.a.)	3 Years (% p.a.)	5 Years (% p.a.)	7 Years (% p.a.)	10 Years (% p.a.)	Since Inception ^(% p.a.)
Perennial Value Shares Wholesale Trust (Net)	0.5	11.3	5.3	4.1	7.3	10.0	9.2	7.1	7.1	8.2
S&P/ASX 300 Accumulation Index	1.1	13.9	8.6	6.7	9.1	9.3	9.7	8.8	8.4	7.9
Value Added	**-0.6**	**-2.3**	**-3.3**	**-2.6**	**-1.8**	**0.7**	**-0.5**	**-1.7**	**-1.3**	**0.3**

^Since inception: June 2001. Past performance is not a reliable indicator of future performance.

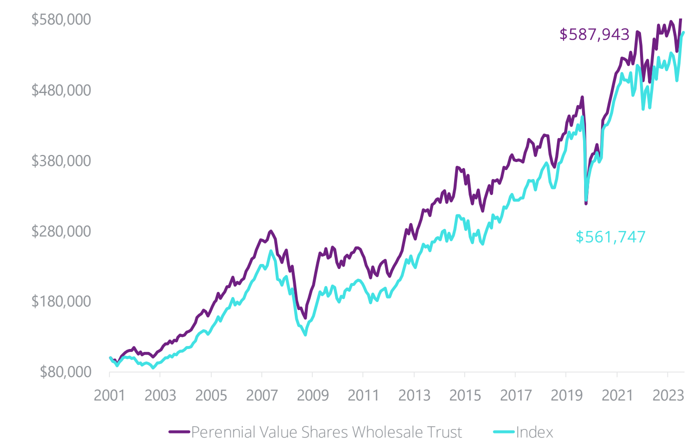
Overview

After a wobbly start, markets regained their upwards momentum in January, as inflation readings continued to head lower. While expectations regarding the extent and timing of future interest rate cuts have been tempered, this has been more than offset by positivity around ongoing economic strength, particularly in the US. Despite the increase in bond yields that have accompanied this, optimism around a "Goldilocks" soft landing continues to grow, and the market has adopted a "good news is good news" stance.

This saw the S&P500 up another +1.6% to a record high, and the NASDAQ lifting another +1.0%, to be up +18.9% and +30.9% respectively over the last 12 months. It should be noted, however, that the vast bulk of these gains have been driven by the "Magnificent 7" tech stocks, with the bulk of the market contributing little to the index. The Nikkei 225 surged a further +8.4% to be up +32.8% for the last 12 months, while the FTSE 100 eased -1.3%. Increasing concerns over the Chinese economic outlook saw the Shanghai Composite down another -6.3%, leaving it down -14.3% for the last 12 months.

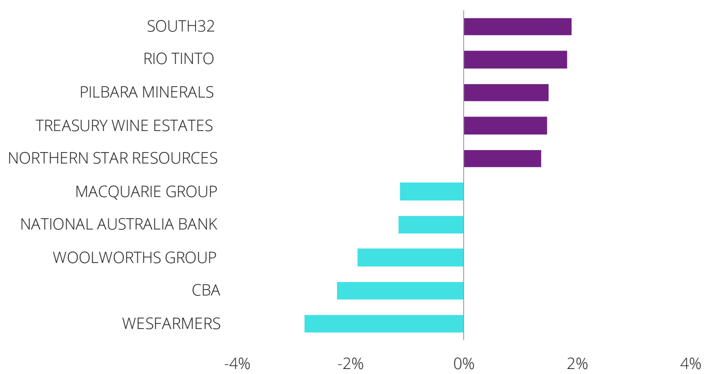
The Australian market was also positive, with the ASX300 Accumulation Index rising +1.1%. Better than expected inflation data buoyed hopes of interest rate cuts, driving a rotation into domestic cyclicals. This boosted sectors such as the Banks (average +5.5%) and Consumer Discretionary (+2.5%). Energy (+5.2%) was the best performing sector, as Middle East tensions saw a recovery in the oil price. By contrast, intensifying China concerns, saw Metals and Mining (-5.7%) the worst performing sector over the month.

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 Trust aims to grow the value of your investment over the long term via a combination of capital growth and 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.

Portfolio Managers
Stephen Bruce,
Andrew King

Trust FUM
AUD $457 million

Distribution Frequency
Half yearly

Minimum Initial Investment
$25,000

Trust Inception Date
June 2001

Fees
0.92% p.a.

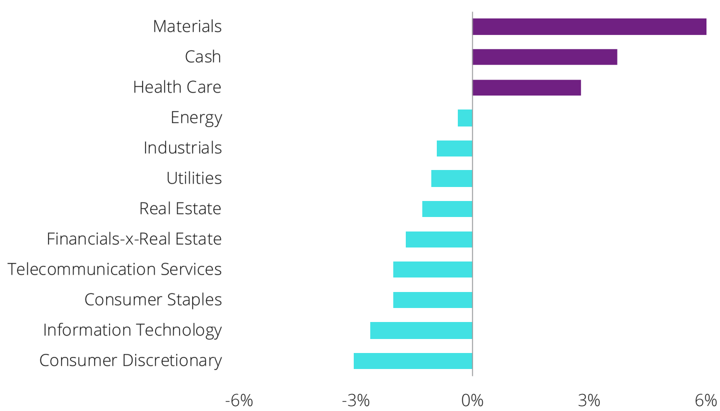
APIR Code
IOF0206AU

Portfolio Characteristics – FY25	Trust	Market
Price to Earnings (x)	14.6	16.2
Price to Free Cash Flow (x)	13.3	14.6
Gross Yield (%)	5.0	5.0
Price to NTA (x)	2.0	2.6

Source: Perennial Value Management. As at 31 January 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 +0.5%, after-fees in January, underperforming the benchmark by -0.6%.

Key contributors to performance over the month included Healthcare stocks, Resmed (+14.8%) and CSL (+5.3%). We moved to overweight positions in these stocks in the second half of last year, after both had been sold off aggressively, in what we believed to be overreactions to negative news.

In the case of Resmed, investors were concerned that the adoption of GLP-1 weight loss drugs would materially reduce the incidence and severity of sleep apnea, thereby reducing demand for Resmed's products. Evidence to date, however, is that this is not the case as, while people's sleep apnea may improve with weight loss, it is not eliminated, and continued use of CPAP machines is warranted. Further, the regulatory woes of Philips, Resmed's main global competitor, continue to go from bad to worse, with their return to the key US market being pushed further out. All of this is positive for Resmed from a market share point of view. CSL was sold off for several reasons, a key one of which being the slow pace of margin recovery post the impacts of COVID on their plasma business. While the pace of margin recovery has definitely been slower than some had anticipated, demand has been very strong, and the overall business is performing well.

These selloffs presented us with the opportunity to invest in very high-quality stocks at valuations well below their normal levels. Both of these stocks have subsequently rallied strongly from their lows, being up around +30% over the last quarter. As a result, we have recently been taking profits, as their valuation discounts have narrowed.

The rally in bond yields from their November lows, benefitted insurers, with holdings in QBE (+7.0%) and IAG (+6.7%) both outperforming. Insurers are positively leveraged to rising interest rates as this increases the earnings on their reserves, which are generally invested in fixed income securities. In addition, industry data suggests that the premium pricing cycle remains strong.

Packaging company, Orora (+7.7%) has begun to recover some of the ground it lost after announcing the acquisition of a French bottle-maker, serving the high-end spirits market. The market is sceptical of this acquisition, and time will tell if this is concern is warranted, however with the company trading on a FY25 P/E of only around 12x, there is not a lot of optimism baked into the share price. Further, the pick-up in Australian wine export volumes is positive for its domestic glass bottle business and the ongoing strength in the US economy bodes well for its US packaging operations. This is in addition to the baked-in earnings growth from pre-contracted capacity expansions in its Australian aluminium can manufacturing business.

The prospect of the RBA cutting rates boosted optimism around the local economy and saw a rotation into domestic cyclicals. The Banks were a key beneficiary of this, up an average of +5.5%, and retail stocks were also strong. While the banks continue to report very low bad debts and retailers continue to report strong sales, we remain cautious on these sectors. While the employment market has remained very strong to date, anecdotally, layoffs seem to be increasing across the economy. In addition, we believe that the impact of higher interest rates and general cost of living pressures are still to be fully felt.

As a result, we remain underweight these sectors, as we do not consider that the current share prices are reflective of the potential risks. For example, CBA is trading at a record high share price, with an FY25 P/E of around 20x. CBA is probably the best bank in the world, however, everything has a price!

The main detractors to performance over the month were our Resource holdings, which were weaker on the back of ongoing negative Chinese economic data. In contrast, to sentiment around the soft-landing and cyclicals, which is at near euphoric levels, sentiment towards China and Resources is extremely negative. This is reflected in relative valuations, for example with CBA trading on the valuation mentioned above, while the bulk miners are trading on single-digit cash flow multiples based on spot commodity prices (and being virtually debt-free). As a result, we continue to see a good opportunity in the Resources sector.

Trust Activity

During the month, we took profits and reduced our holdings in stocks which had outperformed including Resmed, CSL, James Hardie and CBA. At month end, stock numbers were 59 and cash was 3.7%.

Outlook

Despite higher interest rates, economic data continues to be robust in most key developed markets, while inflation continues to ease back towards the Central Banks' target levels. While there is some evidence of softening, the consensus view has become that rate cuts are in the offing 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.

The Australian economy continues to look reasonably healthy, however, GDP growth is weakening. While activity is receiving a strong boost from record immigration, per capita GDP growth is negative. On the positive, the prospect of RBA interest rate cuts is positive for sentiment and the upcoming tax cuts will also boost disposable income. Further, despite the Chinese economic woes, to date the Resources sector continues to be strong and the Agricultural sector is also experiencing positive conditions.

Given this backdrop, we are taking a neutral stance towards interest rates and balancing our cyclical exposures with solid defensives.

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.

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