Perennial Value Shares for Income Trust

Monthly Report May 2022

	Month (%)	Quarter (%)	FYTD (%)	1 Year (%)	3 Years (% p.a.)	5 Years (% p.a.)	Since Inception^ (% p.a.)
Income Distribution	0.5	1.4	5.2	5.8	8.0	7.6	6.2
Capital Growth	-3.1	2.2	-0.6	1.0	-1.9	-1.8	0.0
Total Return	-2.6	3.6	4.6	6.8	6.1	5.8	6.2
Franking Credits#	0.3	0.7	2.4	2.7	3.5	3.1	2.3
Income Distribution including Franking Credits	**0.8**	**2.1**	**7.6**	**8.5**	**11.5**	**10.7**	**8.5**
Benchmark Yield including Franking Credits*	0.5	1.2	5.3	5.6	5.0	5.5	5.9
Excess Income to Benchmark#	**0.3**	**0.9**	**2.3**	**2.9**	**6.5**	**5.2**	**2.6**

^Since inception: December 2005. Past performance is not a reliable indicator of future performance. #Franking credits are an estimate as tax components will only be known with certainty at the end of the financial year. *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.

Overview

Markets stabilised in May, with the S&P500 finishing flat, while the FTSE100 rose +0.8% and the Nikkei 225 rallied +2.5%. However, the NASDAQ continued to decline, falling -2.1%, as loss-making tech stocks continued to be de-rated. By contrast, the Shanghai Composite was up strongly, rallying +4.6%, as it appeared the COVID outbreaks were being brought under control.

The Australian market lagged offshore markets in May, with the ASX300 Accumulation Index declining -2.8% over the month.

Looking to the current financial year, the Trust is currently targeting a 30% increase in FY22 net monthly distributions to 5.5 CPU. Based on the unit price at the start of the year, this equates to a cash distribution yield of around 5.5% and 7.5%, including franking credits. We also expect a significant distribution of surplus income from participation in buy-backs to be paid with the June distribution.

Fund Characteristics

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
Stephen Bruce

Trust FUM
AUD $21 million

Distribution Frequency
Monthly

Minimum Initial Investment
$25,000

Trust Inception Date
December 2005

Fees
0.92%

APIR Code
IOF0078AU

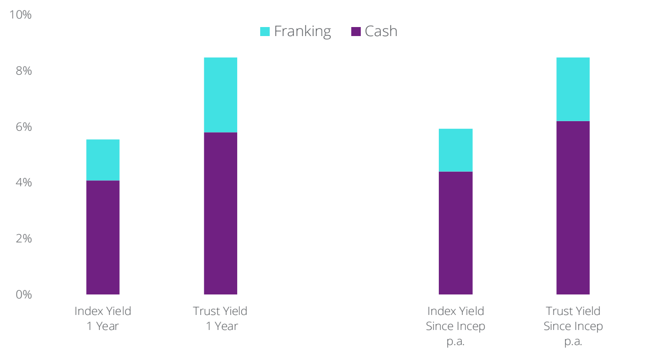
Portfolio Characteristics – FY23	Trust	Market
Price to Earnings (x)	13.1	15.8
Price to Free Cash Flow (x)	10.1	13.9
Gross Yield (%)	7.3	5.4
Price to NTA (x)	2.5	2.7

Source: Perennial Value Management. As at 31 May 2022

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.

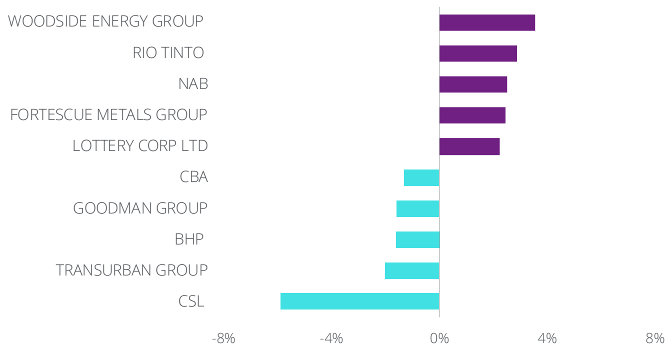
Franking Levels (%)			
FY21	90.3	FY18	99.2
FY20	94.4	FY17	65.6
FY19	95.1	FY16	55.9

Distribution Yield

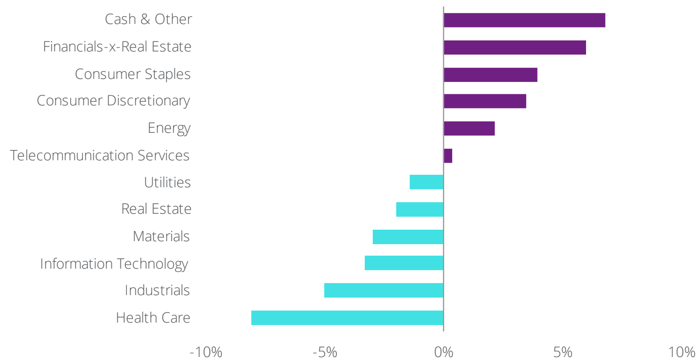


Performance shown net of fees with distributions reinvested. Does not take into account any taxes payable by an investor. Past performance is not a reliable indication of future performance.

Top 5 Over / Underweight Positions vs Index



Sector Active Exposure vs Index



Trust Review

The Trust returned –2.3%, including franking credits and after-fees in May, outperforming the Index by +0.2%. For the last 12 months, the Trust has delivered a return of +9.5%, outperforming the Index by +3.3%. This demonstrates the Trust's leverage to the value rotation which has been taking place as global growth has improved and interest rates have begun to rise from their historically low levels.

While the current uncertainties may cause a short-term pause, we expect that this rotation still has a long way to run, given the macro backdrop and the high level of valuation dispersion which exists in the market. As such we continue to position the portfolio to benefit from this trend.

Better performing stocks during the month included our Resources holdings, with BHP (+4.4%) and Rio Tinto (+1.4%) both outperforming. At the beginning of the year, the Chinese government had adopted a number stimulus measures to achieve their growth target of around 5.5% for 2022. However, the impact of COVID means that far more aggressive measures will be needed if this target is to be met. As a result, many of these measures have been brought forward and it is likely that significant additional measures will be announced early in the second half of the year. As in the past, these measures will likely focus on the infrastructure and property sectors and be positive for resources and commodity prices.

The strong oil price saw energy stocks perform well. However, our holding in Woodside Petroleum, now renamed Woodside Energy Group (-4.5%), lagged the market and sector. However, this was likely due to the overhang of stock that was expected to be sold post the completion of the merger with BHP Petroleum. The merger sees Woodside become a top 10 global oil and gas producer, with an attractive portfolio of low-cost growth options and a strong balance sheet. At current oil prices, the company is generating enormous amounts of cash flow and trading at very low multiples.

Treasury Wine Estates (+5.6%), a recent portfolio addition, outperformed as investors warmed to its premiumisation strategy. This has seen it exit the lower margin commercial wine segment and focus on the higher margin premium end of the market. The company is positioned to benefit as economic reopening continues, driving more on-premise consumption of premium wines. Earnings are set to be boosted further over coming periods as cost of goods will fall due to lower grape costs as production has picked up after a number of constrained seasons.

Aristocrat Leisure (+1.2%) outperformed after delivering a strong first half result. This company continues to perform very strongly in its core gaming machine business, increasing market share and growing its installed base, while at the same time growing its digital business. Importantly, the business has around 1,000 staff in Kharkiv, Ukraine and has been able to relocate the majority of these staff either internationally or to safer locations within Ukraine.

Three of the major banks reported their half-yearly results during the month, which showed improving earnings and increased dividends. The banks are well-capitalised and well-provisioned and should be able to continue to pay attractive dividends. The fund continues to be overweight the sector.

Stocks which detracted from performance included United Malt (-7.9%), Virgin Money UK (-13.8%) and Kathmandu (-12.7%). We remain positive on the outlook for each of these stocks.

Trust Activity

During the month, we took profits and reduced our holding in Ampol. This stock has been a strong outperformer over the last 12 months, as refining margins have surged to very high levels due to global supply chain constraints. During the month, the fund received additional shares in Woodside Energy Group as a result of its merger with BHP Petroleum and received shares in Lotteries Corporation, which was demerged from Tabcorp. We are positive on the outlook for both these businesses. At month end, stock numbers were 33 and cash was 6.6%.

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.

Despite the various uncertainties, many businesses are seeing strong operating conditions. Further, corporate balance sheets are generally in good shape. This has underpinned an attractive level of dividends over the year and seen a number of companies undertake capital returns, such as off-market buy-backs, in which the fund has participated.

As a result, the Trust expects to deliver a 30% increase in total net monthly distribution to 5.5 CPU for FY22. At the opening unit price of $1.02, this represents a net distribution yield of 5.5% or 7.5% including franking. In addition, we expect a significant distribution of surplus income to be paid with the June distribution.

Outlook

While growth is clearly slowing, on balance, we view the outlook as sound, with economies recovering as COVID recedes. Economic data continues to be sound in most regions, with very low unemployment rates. The Australian economy is performing particularly strongly and will continue to be a key beneficiary of the strength in commodity markets. However, there are a number of potentially significant changes in the global economic and political backdrop, from the return of inflation and the change in the interest rate cycle, to rising geopolitical tensions. As a result, the level of uncertainty is elevated, and a degree of caution is warranted.

This view is expressed in the portfolio through holding a combination of stocks with cyclical leverage, as well as stocks with solid defensive characteristics. Importantly, the portfolio is positively leveraged to improving growth, higher inflation, and rising interest rates. Within the cyclical part of the portfolio, this is achieved through overweight positions in the Resources, Energy and Consumer Discretionary sectors. In the defensive part of the portfolio, this is achieved through holdings in the sectors such as Telcos and Consumer Staples.

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

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