Perennial Value Shares Wholesale Trust

Monthly Report September 2022

	Month (%)	Quarter (%)	FYTD (%)	1 Year (%)	2 Years (% p.a.)	3 Years (% p.a.)	5 Years (% p.a.)	Since Inception (% p.a.)
Perennial Value Shares Wholesale Trust (Net)	-6.0	-0.3	-0.3	-6.3	12.8	3.4	5.4	7.8
S&P/ASX 300 Accumulation Index	-6.3	0.5	0.5	-8.0	9.7	2.7	6.8	7.4
Value Added	**0.3**	**-0.8**	**-0.8**	**1.7**	**3.1**	**0.7**	**-1.4**	**0.4**

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

Overview

Persistently high inflation and ongoing hawkish commentary from the US Fed and other central banks, saw bond yields rise and growth expectations fall, sending global markets sharply lower in September. The S&P500 finished the month down -9.3%, the NASDAQ fell -10.5%, FTSE100 declined -5.4%, the Nikkei 225 shed -7.7% and the Shanghai Composite was off -5.6%.

The Australian market was also weaker in September, with the ASX300 Accumulation Index finishing the month down -6.3%. While all sectors of the market delivered negative returns, the Resources sector again outperformed, with Metals and Mining (-1.9%) and Energy (-3.9%) the best performing sectors over the month. The prospect of higher interest rates saw rate sensitive sectors such as Utilities (-13.8%), REITs (-13.6%) and IT (-10.4%) down sharply, while a darkening economic outlook saw Industrials (-9.5%) and Consumer Discretionary (-9.2%) weaker.

Looking forward, while activity remains strong, markets are increasingly pricing recessions in the US and Europe. Investors are searching for signs of slowing activity and easing inflationary pressures, which could foretell the end of the current rate tightening cycle. In this respect, the coming US quarterly earnings season will be very interesting. Economic activity in Australia also remains very robust, with consumer spending holding up despite interest rate rises and inflationary pressures.

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, Damian Cottier, Andrew King

Trust FUM
AUD $480 million

Distribution Frequency
Half yearly

Minimum Initial Investment
$25,000

Trust Inception Date
June 2001

Fees
0.92% p.a.

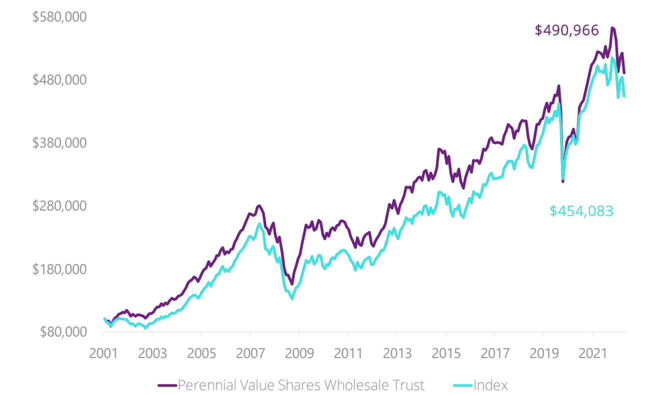
APIR Code
IOF0206AU

Portfolio Characteristics – FY23	Trust	Market
Price to Earnings (x)	12.6	14.4
Price to Free Cash Flow (x)	12.9	13.6
Gross Yield (%)	5.9	5.6
Price to NTA (x)	2.1	2.5

Source: Perennial Value Management. As at 30 September 2022

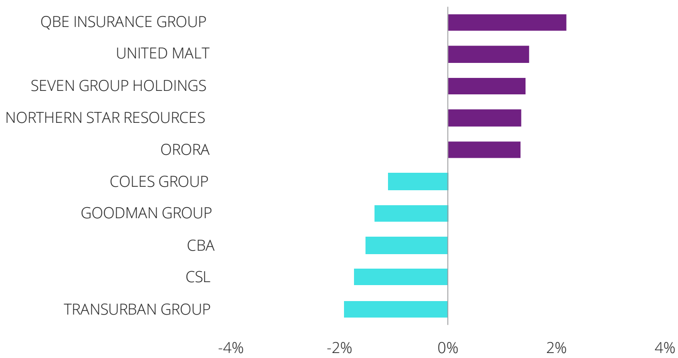
The above figures are forecasts only. While due care has been used in the preparation of forecast information, actual outcomes may vary in a materially positive or negative manner.

Growth of $100,000 Since Inception

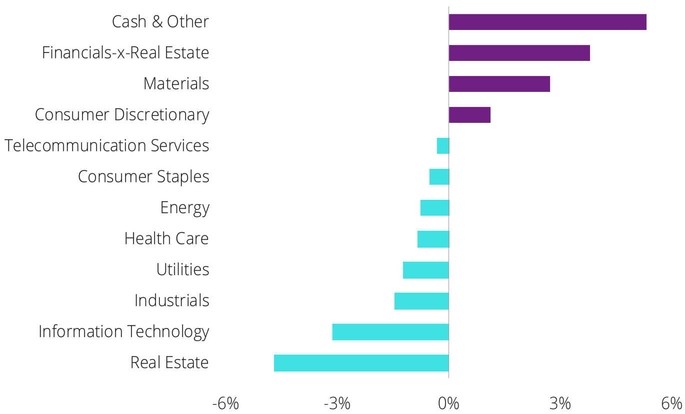


Performance shown net of fees with distributions reinvested. Does not take into account any taxes payable by an investor. Past performance is not a reliable indication of future performance.

Top 5 Over / Underweight Positions vs Index



Sector Active Exposure vs Index



Trust Review

The Trust returned -6.0%, after-fees in September, marginally outperforming the index by +0.3%. Key positive contributors to performance included resources holdings, with copper miner 29Metals (+13.9%), Independence Group (+2.3%), BHP (+1.2%), Oz Minerals (+0.2%), Rio Tinto (-1.2%) and Fortescue Metals (-2.1%) all outperforming. The Trust holds a modest overweight position in the miners, seeing positive sector dynamics as demand for minerals is boosted by the post-COVID reopening of China near-term and the energy transition medium-term. Further, in these times of rising geopolitical tensions and ESG focus, Australian producers are particularly well-placed, as customers seek reliable supply from "strategically-aligned" and well-governed jurisdictions.

One feature of the economy, both here and abroad, has been the resilience of consumer spending, with actual behaviour not reflecting the negative sentiment reported in surveys. While it is almost inevitable that consumer spending will fall from its current very elevated levels, there are certain categories which are likely to continue to deliver growth. Travel is a good example, where there is still likely to be considerable pent-up demand. This bodes well for the earnings of Qantas (-5.6%), which is experiencing a rapid recovery in demand. At the same time, industry capacity constraints are allowing strong ticket pricing, which more than offsets higher costs such as fuel.

In a similar vein, outdoor apparel retailer, KMD Brands (-5.7%), owner of brands such as Kathmandu, Oboz and Rip Curl, is another stock which stands to benefit from the recovery in travel. During the month Kathmandu reported its full-year result, which showed a very strong recovery, with sales and margins accelerating through the year. Further, management indicated continuing momentum into FY23, benefitting from the return to travel.

Rising bond yields saw IAG (-1.1%) and QBE (-4.5%) both outperform, with insurance companies being leverage to higher Interest rates. Further, while a spate of extreme weather events means there is currently no shortage of natural perils, the premium pricing environment continues to remain strong for the sector.

The Energy sector outperformed, with Woodside energy (-2.8%) the key driver. Woodside is very well-placed to benefit from the current strong energy prices, with around a quarter of its production uncontracted and able to be sold into the spot market. While the Energy sector is, hopefully, in a long-term decline as fossil fuels are replaced with renewables, this will not be a rapid process and LNG will be a transition fuel along that journey. In the meantime, Woodside is generating enormous cash flows and sitting on an ungeared balance sheet. While the war in Ukraine has dramatically increased gas prices, it is important to remember that, prior to the invasion in February, Brent crude was trading at around US$100 per barrel. This strength reflected tight supply resulting from several years of significantly reduced investment across the sector. This underinvestment has continued and, as a result, energy prices can be expected to remain relatively high for some time.

Telstra (-3.0%) continues to outperform and remains one of our preferred defensive holdings. At the AGM in October, the company will seek shareholder approval to legally restructure the company into four separate entities. This essentially separates the operating business from the infrastructure assets and international operations. This aims to allow for greater focus on operations and strategy of each of these separate businesses. Further, it aims to provide greater transparency and create greater flexibility to realise the value of some of these assets, as they did with the sale of 49% of the mobile towers business. Given the valuations ascribed to infrastructure assets, this may be a source of considerable value in the future. Further, the recent data breach by Optus may well lead to some market share gains by Telstra.

The main detractors over the month included Ramsay Healthcare (-19.4%), which fell after KKR retracted their takeover offer. The small caps part of the market was particularly hard hit in the risk-off environment. This saw many of the Trust's small cap holdings down sharply, with MA Financial (-30.1%), City Chic Collective (-20.4%), Virgin Money UK (-18.7%) and Smartgroup (-13.1%). Each of these stocks continues to have considerable upside in our view.

Trust Activity

During the month we took profits and trimmed our holdings in Treasury Wines and ANZ, both of which have outperformed recently. Proceeds were used to increase our holding in engineering firm, Worley, which stands to benefit in the near-term from catch-up capex in the energy sector and longer-term from the investment in the energy transition. We also topped up our holdings in Reliance Worldwide and Smartgroup, both of which had been sold off in recent times and are offering good long-term value. At month end, stock numbers were 59 and cash was 5.1%.

Outlook

Global growth is clearly slowing as interest rates rise and economies grapple with the impacts of high inflation and energy supply problems. However, we believe that this will be offset to some extent by the benefits to economies as COVID disruptions continue to recede. While economic data is mixed, and varies greatly from region to region, unemployment rates are very low in most major markets. 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 reopening leverage, as well as stocks with solid defensive characteristics. Importantly, the portfolio is positively leveraged to post-COVID reopening, higher inflation, and rising interest rates. Within the cyclical part of the portfolio, this is achieved through overweight positions in the Resources, Energy and select parts of the Consumer Discretionary sectors. In the defensive part of the portfolio, this is achieved through holdings in the sectors such as Telcos, Healthcare and Insurance as well as a modest overweight in gold.

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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Contact us

Level 27, 88 Phillip Street
Sydney NSW 2000

1300 730 032

invest@perennial.net.au

www.perennial.net.au