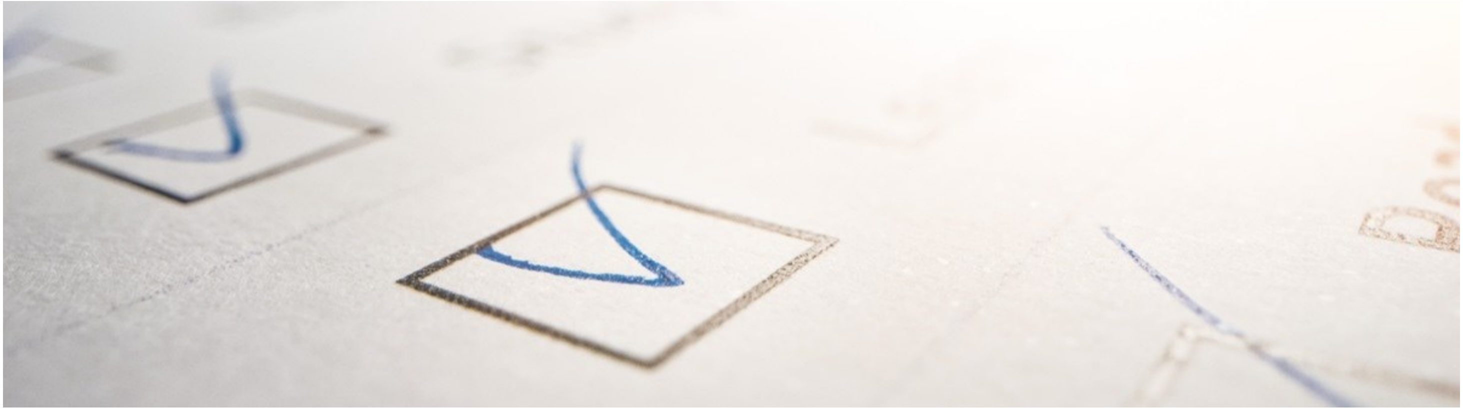
STOCK PICKS IN A VOLATILE MARKET



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Although it's possibly the most overused word in the past four months, it's true that the current situation is unprecedented. Yes, parts of the world have experienced outbreaks of illness, and there have been several financial crises in living memory. For the two events to take the world by storm, hand-in-hand is, thankfully, not our usual experience.

Markets have been see-sawing, providing opportunities to top up core holdings, invest in new but previously overvalued stocks and sell down others that have fared surprisingly well in this unusual environment.

As such, we'd like to share two core holdings we believe are well placed to deliver value to investors.

Ferguson

Ferguson is a leading distributor of pump, plumbing and heating products. It is very similar to Australia's successful Reece business, a business we know well at Perpetual.

Predominantly a US-focused business, Ferguson also has a small business in Canada and a residual UK business, which accounts for less than 10 percent of earnings. The UK business is due to be demerged later this year, leaving Ferguson solely exposed to North America.

There are several reasons we like the company's medium-term prospects. Ferguson today compared to the Ferguson of many years ago shows an increasing focus on residential repair and remodel and less exposure to new build. This means the company is incrementally more resilient than in past cycles.

Importantly, Ferguson ended 2020 with a conservative net debt-to-EBITDA of around one times earnings. The company has ample liquidity and undrawn facilities; for these reasons, we believe its well-placed to ride out the next six to 12 months.

While enjoying strong market positions in each of its business lines, there remains significant room for Ferguson to grow share, particularly given the fragmented nature of the markets in which it competes.

Ferguson has been doing this successfully over time. The strongest evidence of this is its organic revenue growth, which has consistently been above market. In short scale and network density means Ferguson is a very competitive offer for customers. We see Ferguson well placed to continue to gain share in what are structurally attractive markets.

Given recent uncertainty the stock has been sold off, and we believe it represents excellent value at these levels.

Asaleo Care

Asaleo Care is a newer position and is more defensive in nature. Where many companies perceived as 'defensive' are quite expensive, this is a stock that's rather cheap.

Asaleo is a hygiene products company that sells feminine hygiene brand, Libra, as well as Tork and TENA products sold under long-term licence from former parent, Essity. That licence has recently been extended to the end of the decade.

Asaleo recently strengthened its balance sheet by divesting their consumer tissue business that, in a commoditised market and heavily promotional product category, struggled to grow its top line. Although it was loss-making when sold, it attracted a good price which repaired the balance sheet.

Post-sale, the remaining brands have better growth prospects, better competitive environments and are less capital-intensive. Accordingly, we expect cashflow generation to improve materially. The biggest priority now is to continue reinvesting in the core brands with the aim of sustaining recent improvements in organic growth rates.

Asaleo also has a B2B business, which services commercial premises such as hospitals, aged care facilities, workplaces, offices and restaurants. It has good market share, a diverse customer base, and is expected to quickly regain volume post a temporary COVID-19 shutdown.

Asaleo trades on 13 times earnings and its prospective free cashflow yield is just shy of 8%. With an improving balance sheet, reinstatement of its dividend and attractive free cash flow yield, in this market environment, there's valuation upside to the stock.

Our focus remains on balance sheet resilience and companies with strong industry positions, looking for those businesses where competitive position is likely to improve. This is how we continue to add value for our investors.

Find out more about the performance, strategy and holdings of the Perpetual Wholesale Ethical SRI Fund.