Perpetual Investments

PERPETUAL WHOLESALE DIVERSIFIED INCOME FUND

October 2018

FUND FACTS

Investment objective: To provide regular income and consistency of return by investing in a diversified range of income generating assets.

Benchmark:	Bloomberg AusBond Bank Bill Index**
Inception date:	October 2005
Size of fund:	$1,260.1 million as at 30 September 2018
APIR:	PER0260AU
Mgmt Fee:	0.70% pa*
Benchmark Yield:	1.817% as at 31 October 2018

Suggested minimum investment period: Three years or longer

FUND BENEFITS

Provides investors with the potential for regular income, above cash returns and lower volatility than other income strategies through an actively managed, highly diversified and liquid investment.

TOTAL RETURNS % (AFTER FEES) AS AT 31 October 2018

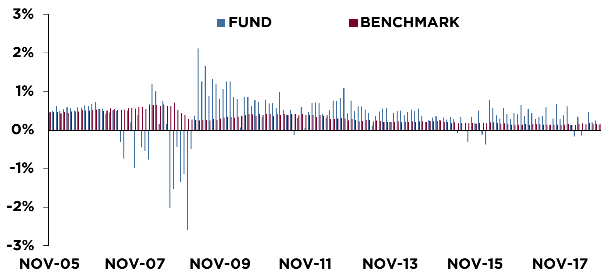
	1 MTH	3 MTHS	6 MTHS	1 YR	2 YRS PA	3 YRS PA	5 YRS PA	7 YRS PA	INCEPT PA
Perpetual Wholesale Diversified Income Fund	0.14	0.60	0.97	2.59	3.90	3.95	3.87	4.72	4.67
Bloomberg AusBond Bank Bill Index**	0.17	0.49	1.01	1.89	1.83	1.93	2.18	2.58	3.97

Please note: Performance for Perpetual's complete list of investment funds is available on www.perpetual.com.au. Past performance is not indicative of future performance.

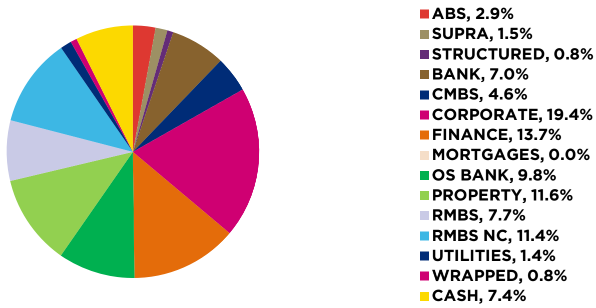
POINTS OF INTEREST

- •Domestic cash bond spreads outperform offshore equivalents
- •RBA remain on hold, bank bills rally modestly but remain elevated
- •ACGB curve shifts lower on market uncertainty; Swap spreads widen across maturities
- •Modest volumes of domestic issuance; three new securitisation deals price in October
- •The outlook for credit is neutral

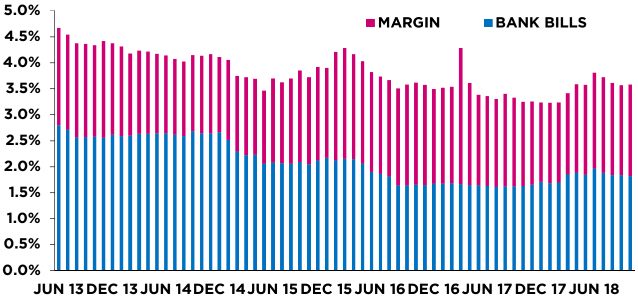
MONTHLY PERFORMANCE SINCE INCEPTION



PORTFOLIO SECTORS



RUNNING YIELD



PORTFOLIO COMPOSITION

	BREAKDOWN
Senior Debt	78.60%
Subordinated Debt	13.99%
Hybrid Debt	7.41%
Core Component	87.54%
Plus Component	12.46%
% Geared	0.00%
Running Yield	3.63%
Portfolio Weighted Average Life	3.68 yrs
No. Securities	161

* Information on Management Costs (including estimated indirect costs) is set out in the Fund's PDS.

MARKET COMMENTARY

October was a challenging month for risk assets. Spreads of offshore cash bonds succumbed to widening pressures driven by increased global equity market volatility. The culmination of potential geopolitical woes, escalating trade tensions and receding global monetary policy stimulus caused investors to question valuations, underpinning a wide reaching sell off across broader risk assets. Domestic credit spreads were mostly resilient to these events, outperforming their offshore equivalents. A diminished level of local primary issuance during the period helped to assuage potential spread widening. A healthy bid for domestic credit remained in the secondary market, with longer dated domestic corporates performing well. Strength in appetite for primary market issuance was lacklustre. Fundamentals remained robust, confirmed by positively biased data prints and a theme of solid sales and earnings growth momentum coming from US report season results.

However, concerns around the sustainability of growth momentum stemming from the reduction in stimulatory measures weighed on market sentiment. In addition, a cut to the IMF's Global GDP outlook and simmering geopolitical concerns occupied investors minds. Australian bonds rallied across the curve and yields shifted lower in the second half of the month in response to the broader risk off tone observed. Robust domestic employment data was tempered by a weak inflation measure at month end. As such, the Reserve Bank of Australia (RBA) maintained their ongoing dovish tone, leaving interest rates at 1.5% while indicating that current monetary conditions are appropriate for the growth objectives of the domestic economy.

Lighter volumes of domestic primary issuance assisted credit spread stability during the month. A$4.4bn printed across both corporate and SSA issuers. Domestic cash bonds outperformed their synthetic iTraxx equivalents, which were more volatile as a result of dynamics in broader risk assets generally.

PORTFOLIO COMMENTARY

The portfolio continued to collect running income in excess of the benchmark across all corporate and collateralised sectors. This contribution from positive carry was mainly associated with portfolio exposure to corporates alongside banks and financials which served to insulate the fund from instances of spread widening observed in higher yielding offshore related holdings during the period.

Credit spread widening detracted from performance. However, a positive contribution from a short risk (bought protection) position on European high yield (XOver) credit default swaps (CDS) which benefited from a widening in credit spreads during the month served to partially offset the impact of spread widening observed. Although domestic spreads were steady and rangebound during the month, spreads of select offshore holdings, most notably financials, pushed wider given the risk off tone across broader risk assets. Lighter volumes of supply in the domestic primary market supported the resilience of domestic spreads to widening pressures observed.

In terms of positioning, sector allocation was actively managed while maintaining a focus on risk and relative value in opportunities seen. Within the "core" investment grade allocation, exposure to securities higher up both the ratings and capital structure was increased in line with a preference for higher rated, more defensive exposures, while the weighted average life of the portfolio was modestly reduced in line with a softening, though still positive outlook. Portfolio exposure to domestic banks was decreased, while exposure to RMBS was built upon. Primary market participation included a position in Korea Development Bank's FRN alongside higher rated tranches of Peppers 'i-Prime 2018-2 Trust' RMBS. Secondary market purchases included attractive relative value opportunities observed in securitised products. The running yield at month end was approximately 3.63% with the spread measured at 1.77% above the benchmark.

OUTLOOK

The outlook for credit has softened to neutral. A strong macroeconomic outlook is being tempered by less supportive market metrics. Valuations alongside supply and demand dynamics also have a modestly negative bias.

Strength in the macroeconomic outlook remains a key support for the prospect of tighter spreads, with economic indicators continuing to print positively. Credit fundamentals in both the investment grade and high yield spaces remain robust, supported by constructive global economic data. However, support from market metrics has diminished. A spike in volatility alongside an associated weakness in equity markets are both negative for credit spread dynamics. The continued appearance of diminished cash levels across aggregate domestic accounts is also less supportive for market demand.

Supply and demand dynamics are modestly negative. Recent primary market dynamics have resulted in broader spread dynamics being range bound. Elevated volumes of primary issuance in previous months had put a floor under any meaningful near-term tightening expectations, however the prospects of wider spreads has also been dampened given lighter levels of supply to the domestic market in October. More recent demand for primary issuance has become somewhat lacklustre whereas secondary demand remains robust. Upcoming supply expectations and maturities due are at normal levels.

Valuation indicators have a modestly negative bias. From a relative valuation perspective, spread differentials between domestic and offshore paper remain mostly tight. Both domestic and offshore cash bonds continue to trade tight of their long-term averages in investment grade and high yield spaces. However, given an elevated basis swap, instances of slight divergence in spreads relative to US equivalents have been observed.

Although the fundamental backdrop of a robust economic environment remains positive for credit, we remain vigilant regarding the fragility of the geopolitical landscape. Rising trade friction typically threatens to dampen global economic growth. Uncertainty around rising interest rates and the pace of unwind of quantitative easing in place is also apparent. We continually monitor information flows that may influence market sentiment and in such situations retain sufficient flexibility to appropriately and actively manage portfolio risk exposures.

** UBS Australian Bond Index changed to Bloomberg AusBond Bank Bill Index effective 26 September 2014

MORE INFORMATION

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