Perpetual Investments

PERPETUAL WHOLESALE DYNAMIC FIXED INCOME FUND

November 2018

FUND FACTS

Investment objective: To provide capital stability and regular income by investing in a diversified range of income generating assets. Aims to provide a positive return (before fees and taxes) irrespective of market conditions over a rolling three-year period.

FUND BENEFITS

The fund is designed to provide investors with a diversified fixed income solution that manages both credit risk (credit worthiness) and duration risk (sensitivity to changes in interest rates) in different economic conditions.

Benchmark: 50% Bloomberg AusBond Composite Index/50% Bloomberg AusBond Bank Bill Index
Inception date: November 2010
Size of fund: $15.7 million as at 30 September 2018
APIR: PER0557AU
Mgmt Fee: 0.55% pa*
Suggested minimum investment period: Three years or longer

TOTAL RETURNS % (AFTER FEES) AS AT 30 November 2018

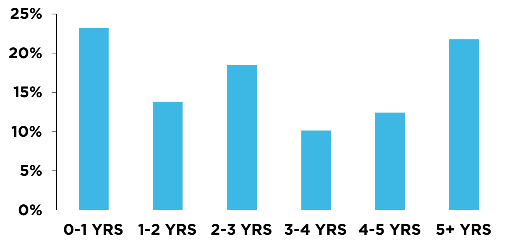
	1 MTH	3 MTHS	6 MTHS	1 YR	2 YRS PA	3 YRS PA	5 YRS PA	7 YRS PA	INCEPT PA
Perpetual Wholesale Dynamic Fixed Income Fund	-0.19	-0.04	0.81	1.61	3.02	3.42	3.87	4.65	5.13
Bloomberg AusBond Composite/Bank Bill Blend	0.20	0.39	1.38	2.19	2.53	2.62	3.32	3.58	4.11

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.

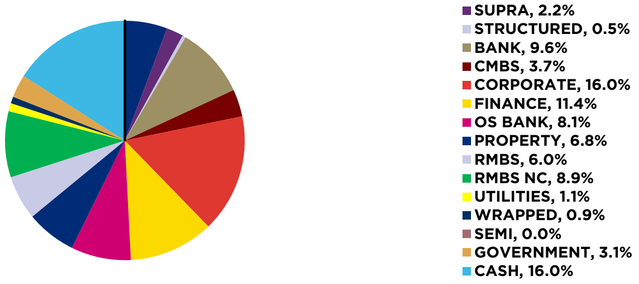
POINTS OF INTEREST

•Credit spreads widen sharply, particularly pronounced in offshore banks and financials
•RBA remain on hold, bank bills rally higher, ACGB curve flattens; Swap spreads widen
•Elevated A$13.8 of domestic issuance; 7 new securitisation deals price in November
•The outlook for credit has turned negative

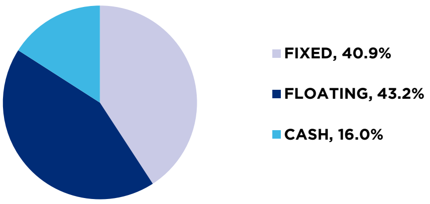
MATURITY PROFILE



PORTFOLIO SECTORS



FIXED AND FLOATING BREAKDOWN



PORTFOLIO COMPOSITION

	BREAKDOWN
Senior Debt	84.59%
Subordinated Debt	11.22%
Hybrid Debt	4.20%
Running Yield	3.28%
Portfolio Weighted Average Life (yrs)	3.31
No. Securities	267
Modified Duration	0.60

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

MARKET COMMENTARY

November was a volatile month for risk assets. Fears of potential policy error by the US Federal Reserve, geopolitical uncertainties and negatively biased idiosyncratic events underpinned fragile investor sentiment. Although having appeared resilient early in the month, spreads of domestic cash bonds pushed wider as time progressed, following the trend observed in offshore equivalents earlier in the period.

Broadly positive employment and economic data announcements early in the month were tempered by a variety of headwinds. Continued US-Sino trade tensions remained in focus, while political uncertainty associated with the midterm elections in the US occupied investors minds. Markets grappled with ongoing concerns over the global economic growth outlook, Italy's budget clash with the European Commission and Brexit related risk. Concerns around the volume of lower quality corporate bonds outstanding (primarily in the US) also served to compound nervousness.

While offshore cash bonds succumbed to widening pressures early in the month, domestic spreads were initially relatively resilient. This was in part attributable to diminished volumes of local market new issuance holding spreads firm. However, as primary market activity increased, lacklustre demand for the significant volumes of supply resulted in significant new issuance concessions relative to where comparable secondary market equivalents were pricing.

Although domestic employment data was robust and Australia's terms of trade higher, evidence of less favourable dynamics in the housing market served to temper sentiment regarding domestic economic conditions. This prompted the Reserve Bank of Australia (RBA) to maintain 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. 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.

Credit spread widening detracted from performance. Offshore spreads pushed wider throughout the month with dynamics driven by a myriad of concerns including geopolitical uncertainties, US-Sino trade tensions and fears associated with potential policy error in the US. Although diminished new issue volumes in the Australian market early in the period provided support for domestic spreads, as primary market activity increased, spreads pushed wider. The proposed change by the Australian Prudential Regulation Authority (APRA) for tier two debt to form a substantial part of the major banks Total Loss Absorbing Capacity (TLAC) resulted in spreads of domestic bank sub-debt to push significantly wider following the proposal.

Portfolio duration was actively managed over the period in line with signalling from our proprietary tactical asset allocation model. This is used to determine valuation, economic cycle and technical indicators and appropriate duration positioning is based on the cumulative result of each of these signals. While valuations and cycle have remained negative and neutral respectively, technical indicators diminished to become negatively biased early in the month as a result of the volatility observed in markets. As such portfolio exposure to duration was reduced early in the month.

OUTLOOK

The credit outlook has turned negative. Despite the prevalence of a supportive macroeconomic environment, deteriorating market driven metrics alongside unbalanced supply and demand dynamics underpin the negative bias observed.

Valuation indicators are modestly negative. From a relative valuation perspective, spread differentials between domestic and offshore paper remain mostly tight. Despite recent spread widening, 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, a slight divergence in spreads relative to US equivalents have been observed.

Support from market metrics continues to deteriorate on the back of recent increased volatility in both equity and bond markets. This has caused some credit buyers to pull back and raise cash in anticipation of buying at better technical levels. In addition, intermediary appetite for credit appears to have waned recently. Supply and demand dynamics have also become less supportive. A combination of elevated volumes of primary issuance in the past month and reduced upcoming maturities has put a floor under any meaningful near-term tightening expectations. Recent demand for primary issuance has become somewhat lacklustre, where new issue concessions relative to secondary market equivalents have been present. Somewhat tempering the negative biases observed is strength in the macroeconomic outlook. This is driven by strength in economic indicators, including the recent US manufacturing ISM survey print alongside PMI prints and the recent decline in the crude oil price in US dollar. Credit fundamentals in both the investment grade and high yield spaces remain robust.

Although the fundamentally strong economic environment remains positive for credit, we remain vigilant regarding the fragility of the geopolitical landscape. Trade friction is appearing to dampen the outlook for global economic growth. Uncertainty around potential policy error in the United States, Brexit related volatility 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.

Total return shown for the fund(s) have been calculated using exit prices after taking into account all of Perpetual's ongoing fees and assuming reinvestment of distributions. No allowance has been made for entry or exit fees or taxation (except in the case of superannuation funds).

Past performance is not indicative of future performance.

*** The benchmark for the Fund was previously reported as both the Bloomberg AusBond Bank Bill Index and the Bloomberg AusBond Composite Index. As at 29 April 2015, the benchmark for reporting was updated to a composite benchmark comprising 50% Bloomberg AusBond Bank Bill Index & 50% Bloomberg AusBond Composite Index. The change in benchmark was to better reflect the investment strategy. The performance table above reflects the change in benchmark applied across all periods.

MORE INFORMATION

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