Perpetual Investments

PERPETUAL INSIGHTS

July 2015

Our team of investment specialists share their views on the past 12 months – how markets have performed and what it means for your investments with Perpetual.

It has been an interesting year for global sharemarkets. On the one hand, we've seen record low interest rates around the world and a much lower growth environment. On the other, there has been continued strong demand for high yielding investments and overall, the MSCI World Total Return Index was up 24.6%.

At Perpetual, we understand that a challenging macroeconomic climate and the prospect of increased volatility can be disconcerting for investors. But it can also provide opportunities to purchase quality assets at prices below their true value. Perpetual has a long history of this type of prudent investing.

GLOBAL OPPORTUNITIES FROM AN AUSTRALIAN PERSPECTIVE

During the past financial year, we launched the Perpetual Global Share Fund – a focused portfolio of fewer than 40 high-quality companies, hand-picked for their long-term investment potential. We believe that when it comes to value investing, we not only have an active and proven approach, we also have the conviction to stick to it.

In December we debuted our first listed investment company – the Perpetual Equity Investment Company (ASX: PIC). PIC was designed to provide investors with direct access to Perpetual's expert investment team and proven, value-oriented investment philosophy. It's also structured to allow access to global opportunities, together with all the transparency and liquidity that comes from a listed investment.

Finally, earlier this year we announced the retirement of Matt Williams as Head of Equities, after more than 22 years with Perpetual, and the promotion of Paul Skamvougeras to the role. I was delighted for Matt to be able to pass the baton of leadership over to such an experienced investment professional within the team.

Thank you for continuing to invest with Perpetual.

Michael Gordon
Group Executive –
Perpetual Investments

CONTINUING TO DELIVER FOR YOU

Over the past year we have been honoured to be recognised as:

Australian Equities
Provider of the Year

Winner
SMA Portfolio Award

Gold Winner
Perpetual Concentrated Equity and SHARE-PLUS Long-Short Funds

PERPETUAL GLOBAL SHARE FUND KEY FACTS

32.6%
Return per annum
Net performance over three years to 31 May 2015*

20-40
Handpicked portfolio of securities

1,000
Company meetings worldwide over the past year

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* To give a longer term view of our performance in the Fund, the returns for Class W, which has been operating since January 2011 (and is not publicly available for investment), are shown. Class W has identical investments to Class A which is publicly available. We have adjusted the return of Class W to reflect the fees applicable to Class A. For updated performance to 30 June 2015, please visit www.perpetual.com.au. Past performance is not indicative of future performance.

FINANCIAL YEAR 2014/15 AT A GLANCE

5.7%

Return from the Australian sharemarket over the financial year

S&P/ASX 200 Accumulation Index, Source: FactSet

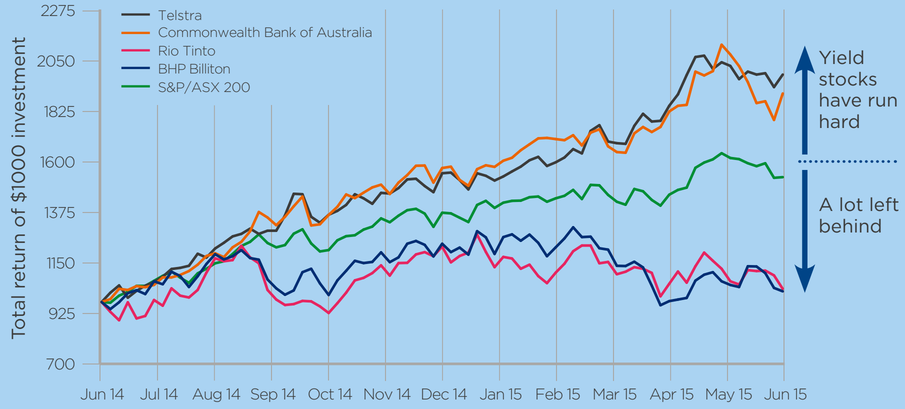
AUSTRALIAN SHAREMARKET

With global interest rates remaining at historic lows and a steady decline in bond yields, investors continued to look to the Australian equity market for greater investment return opportunities. However, the S&P/ASX 200 Accumulation Index rose just 5.7% for the financial year ending 30 June 2015 – significantly lower than growth experienced in recent years.

Valuations have become stretched, especially in sectors where investors have chased dividend yields. Whilst the big bank stocks corrected somewhat towards the end of the year, the 'yield trade' remains very much in vogue, as evidenced by the continued strong performance of Telstra and infrastructure companies.

On the economic front, *growth remained subdued* as the economy continues to slowly transition from a declining mining investment boom to more domestic driven activity. Employment and housing construction activity were solid, however this has yet to translate into higher consumer sentiment or stronger non-mining business investment.

FIRST CRACKS IN THE YIELD TRADE
YIELD TRADE VS RESOURCES MARKET



Source: FactSet as at 30 June 2015

0.5%

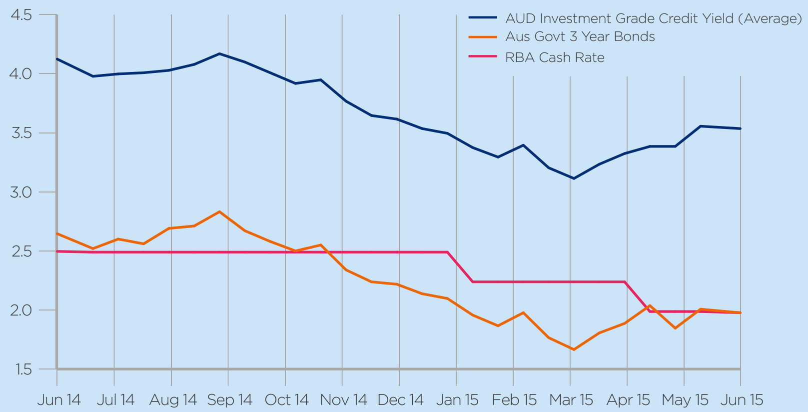
Fall in the Australian cash rate (from 2.5% to 2.0% this financial year)

Source: Reserve Bank of Australia, as at 30 June 2015

INTEREST RATES

With economic growth persisting at subdued levels and the slow pace of a transition from mining investment to domestic activity, the Reserve Bank of Australia (RBA) embarked on a new round of interest rate cuts in 2015, reducing the official cash rate in February and May by 0.5% in total. Whilst the cuts raised concerns that it might fuel large increases in house prices in certain housing markets, the Reserve Bank felt that this was warranted – given the significantly lower commodity prices and an expectation that a return to trend growth might take longer than expected.

The cuts saw Australia with *the lowest official cash rates on record,* although they still continued to be above other countries such as the near-zero rates of the US, Japan and Europe. As a result, over the financial year, inflation has remained within the RBA's target band of between 2 and 4%.



Source: BofA Merrill Lynch, FactSet, RBA, Perpetual, as at 30 June 2015

High
94.58c
Low
75.90c

Australian Dollar from 1 July 2014 to 30 June 2015

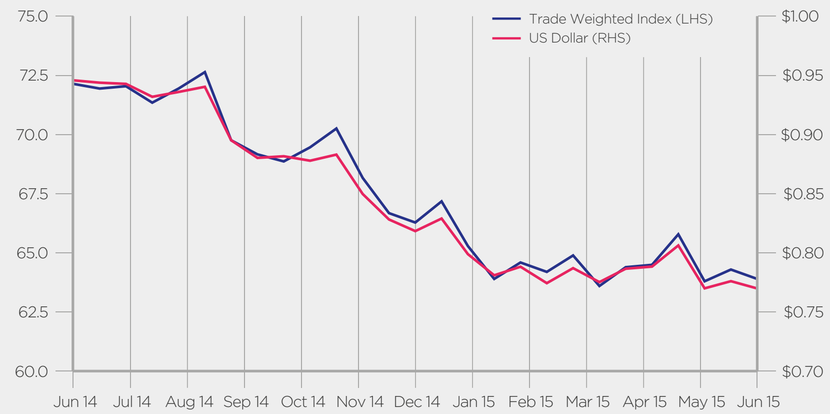
Source: Reserve Bank of Australia, as at 30 June 2015

THE AUSTRALIAN DOLLAR

The extended period of strength for the Australian dollar finally came to an end during the financial year. The Australian dollar had long benefited from its status as a AAA-rated currency, as well as the ongoing central bank policies of close to zero official policy rates and money printing programs in the major global economies.

However, the slowing Chinese economy, sharply lower commodity prices and the shift to an easing bias by the Reserve Bank of Australia combined to finally drive the Australian dollar lower this year. Despite this, the RBA noted that the Australian dollar *still remains overvalued on a trade weighted basis* given the size of the decline in commodity prices and that further depreciation seemed 'likely and necessary'.

AUSTRALIAN DOLLAR VS US DOLLAR AND TWI (INDEX, $)



Source: Reserve Bank of Australia, as at 30 June 2015

PERPETUAL VIEWPOINT

At the beginning of the new financial year, we ask Perpetual's experts what's in store for the coming year. Where are they seeing challenges and opportunities for investors in 2016?

Paul Skamvougeras
Head of Australian Equities

Whilst the yield trade remains very resilient in parts of the market and the overall market trades at elevated levels, there continue to be pockets that we believe represent good value investment opportunities. In particular, we continue to look for high quality companies with solid earnings growth that are not reliant on the domestic business cycle, companies where management are initiating turnarounds in company performance or deep value companies that are in industries currently out of favour. Perpetual's focus on quality as well as value, including owning companies with lower levels of debt, will be of particular importance as the US Federal Reserve contemplates its first rate rises in nearly a decade.

Michael O'Dea
Head of Multi Asset

With many festering issues at the heart of the eurozone unresolved, China's growth slowing, and the US Federal Reserve edging closer to increasing interest rates for the first time since before the GFC, 2015 has signalled a more muted return environment. To compound investors' woes, historically "low risk" assets are offering unusually low prospective returns and many growth markets are at unappealing valuation levels. It is understandable that some people are perplexed by the question of how to invest to balance both risk and return. We believe investment success in the year ahead will come from being aware of global themes (opportunities and risks), while maintaining a disciplined approach to invest in attractively priced opportunities resulting from volatility. Avoiding expensive investments and embracing a broader set of investment opportunities is a tried and tested way of improving the likelihood of delivering acceptable returns with less downside risk.

Michael Korber
Head of Credit

Nowhere exemplified the challenging market conditions of 2015 more than the unusual situation of negative yields on selected European government bonds that saw investors actually paying to invest in fixed income. As I write, the situation in Greece remains in focus. With the country struggling to secure necessary funds to repay its creditors, fears of a Greek exit from the eurozone continue to escalate. We are closely monitoring these developments in Europe in a market increasingly driven by sentiment and headlines. This may present attractive investment opportunities in quality securities that get caught in the market disruption. We believe that continuing to be risk aware and vigilant will ultimately reward investors.

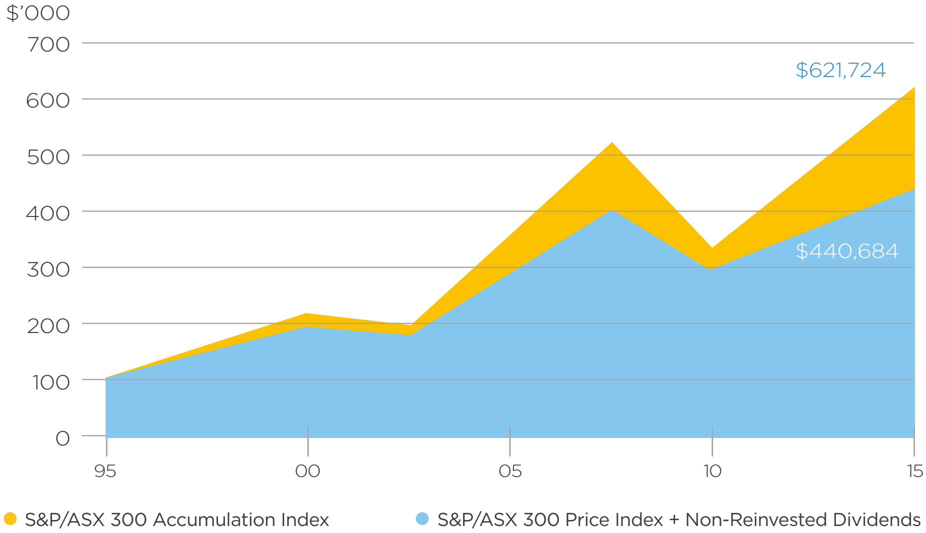
YOUR FUND IS WORKING HARD. NOW WORK IT HARDER.

A CASE FOR COMPOUNDING

For many people, investment decisions revolve around three words: Buy, Sell or Hold. But there's another primary consideration: what to do with the income generated from the investment?

Here's a quick example. The graph to the right compares the performance of $100,000 invested in S&P/ASX 300 over the past 20 years with dividends reinvested (the yellow section) versus the same amount with dividends received, but not reinvested (the blue section). The difference is more than $180,000.

S&P/ASX 300 INDEX COMPARISON
20 years to 30 June 2015



Source: FactSet. Past performance is not indicative of future performance.

TO REINVEST OR NOT?

The decision whether or not to reinvest should be based on your personal circumstances. You may want to use the distribution income to pay for living expenses or other immediate needs. Alternatively, if you don't require the funds in the short term, then harnessing the power of compound growth could be a beneficial long-term strategy for you.

In addition, because reinvestments aren't subject to transaction costs (eg. buy spreads), it means you receive more units than you would have if you had made a new investment at the same time. Like any investment, reinvesting distributions is subject to investment risk, including the chance that the investment will not gain or retain its value. Talking to a financial adviser could help inform your decision.

As billionaire investor Warren Buffet put it,

"My wealth has come from a combination of living in America, some lucky genes – and compound interest."

HOW TO REINVEST YOUR DISTRIBUTIONS

Reinvesting your distributions is easy and can be reversed at any time.
Talk to your financial planner today or call us on 1800 022 033.

We've been renovating Perpetual's website to make it faster and easier to use, particularly on your mobile phone or tablet. The updates will also allow us to share more views and insights from our experts. Look out for major changes in August this year.

MORE INFORMATION

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