

## Wholesale Funds

# PERPETUAL WHOLESAL DIVERSIFIED GROWTH FUND

March 2022

### FUND FACTS

**Investment objective:** Aims to: provide long-term capital growth and regular income through investment in a diversified portfolio of growth and income assets; and outperform a composite benchmark (before fees and taxes) reflecting its allocation to the various asset types over rolling three-year periods.

### FUND BENEFITS

Provides investors with an equal mix of growth and income assets, for long-term capital growth, but with a significant exposure to defensive assets to reduce volatility. Strategic and tactical asset allocation techniques are employed in order to further enhance the fund's returns and manage risk.

### FUND RISKS

All investments carry risk and different strategies may carry different levels of risk. The relevant product disclosure statement or offer document for a fund should be considered before deciding whether to acquire or hold units in that fund. Your financial adviser can assist you in determining whether a fund is suited to your financial needs.

**Benchmark:** Moderate Growth Index (Internally generated composite)

**Inception Date:** October 2001

**APIR:** PER0114AU

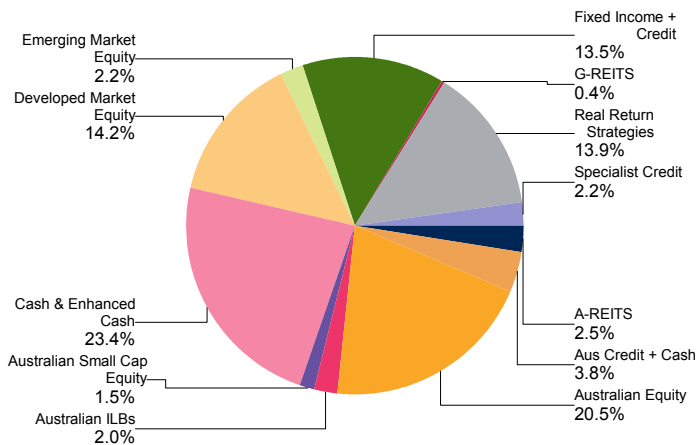
**Management Fee:** 0.96% p.a.

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

**Investment style:** Active, fundamental, disciplined, value

**Suggested minimum investment period:** Three years or longer

### PORTFOLIO SECTORS



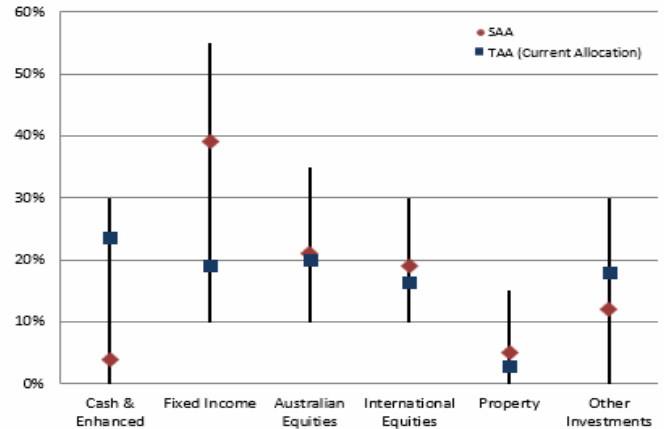
### NET PERFORMANCE- periods ending 31 March 2022

	Fund	Benchmark	Excess
1 month	0.1	0.2	-0.1
3 months	-0.6	-3.7	3.1
FYTD	1.9	-0.8	2.7
1 year	5.7	4.1	1.6
2 year p.a.	10.8	9.4	1.4
3 year p.a.	6.4	5.7	0.7
5 year p.a.	6.0	6.3	-0.3
10 year p.a.	7.1	7.3	-0.2
Since incep.	6.2	6.1	0.2

Past performance is not indicative of future performance. Returns may differ due to different tax treatments.

### ASSET ALLOCATIONS AND INVESTIBLE RANGES

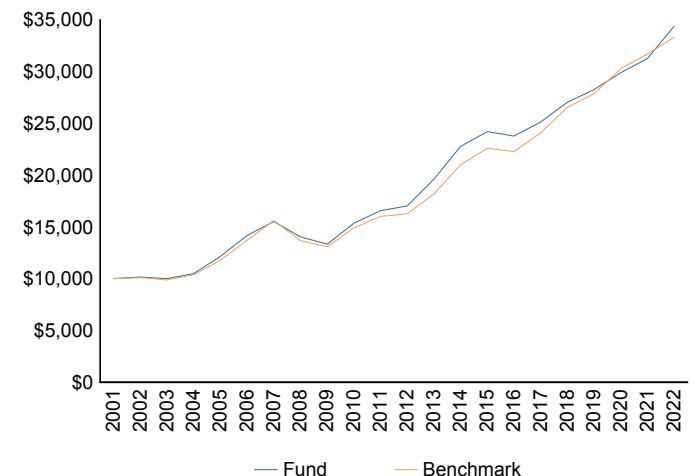
FUND TACTICAL AND STRATEGIC ALLOCATIONS INCLUDING ALLOWABLE MAXIMUM AND MINIMUM RANGES



### STRATEGIC AND TACTICAL ASSET ALLOCATIONS

The Strategic Asset Allocation (SAA) is the neutral allocation acting as an anchor for active positioning, while the Tactical Asset Allocation (TAA) process adjusts the asset allocation according to market opportunities and risks.

### GROWTH OF \$10,000 SINCE INCEPTION



## MARKET COMMENTARY

There have been a number of bearish developments over the past quarter that have weakened the growth outlook to the point where recession risks in the next two years are coming back into focus. In particular, inflation in the US has increased to levels not seen for four decades. Combined with surging wage growth and very tight labour markets this is forcing a complete recalibration of monetary policy expectations. The Russian invasion of Ukraine has just exacerbated the worsening trade off between growth and inflation, as oil and other commodity prices surge, adding to inflationary pressures.

- US equities (-4.6%) fell through January and February before rebounding in March. Persistent inflationary pressure and the US Federal Reserve's (the Fed's) expected policy response saw growth stocks in particular sell off significantly.
- UK equities (+2.9%) led major markets proving resilient to tighter monetary policy and geopolitical risks. By contrast, continental markets including France (-6.7%) and Germany (-9.3%), were significantly impacted by the invasion of Ukraine.
- Australian equities (+2.2%) outperformed the broader global market. Australian equities were bolstered by rising commodity prices and led all developed markets over February and March.
- Bond markets sold off aggressively over the quarter on persistent inflation concerns. US 10-year yields increased 81 bps while Australian yields were up 116 bps (the latter represents the biggest sell-off since 1994). Bond yields rose despite investors reducing risk as a result of the war in Ukraine.
- Commodity markets were significantly impacted by the invasion of Ukraine with oil moving above US\$100. Gold performed well, rising sharply in February as the Russian invasion began before retreating somewhat during March.

In March, the Fed elected to increase the Fed Funds rate to the 0.25%-0.5% range. More importantly, the Fed foreshadowed a much more aggressive monetary policy tightening path over the next year leading to a substantial repricing of fixed income markets. Quantitative tightening (or selling down the Fed's balance sheet) is also being touted as another tool to curb inflation by members of the Federal Open Market Committee. This would likely be a catalyst for further increases in bond yields and volatility in financial markets.

The challenge facing the Fed is clear with core inflation almost triple their 2% target rate and the economy already slowing. It will be extremely difficult for the Fed to engineer a soft landing given the prolonged delay in the process of unwinding their extreme policy settings. During the last week of March, the US yield curve became briefly inverted with the 2-year yield rising above the 10-year yield. Yield curve inversion has been a consistent harbinger of recession within the following 12-24 months. The signal has not yet been generated (as the curve needs to stay inverted for three months). Nonetheless, the brief inversion has certainly added to the perception of increased recession risk in the US in the next two years. The combination of slowing economic growth, higher interest rates, tightening liquidity and margin pressure is problematic for the equity market outlook.

The Russian invasion of Ukraine and subsequent sanctions have already seen the oil price increase to well over US\$100 a barrel, putting further pressure on headline inflation. Recession risks in Europe have also increased due to the heavy reliance on Russian oil and natural gas. Furthermore, the impact on input prices, supply chains and consumer sentiment have wide ranging implications for the global economy which is still affected by a profound supply and labour shock that began two years ago.

The growth outlook in Asia is also being revised down as China unveiled its lowest growth target in 30 years. The path of the COVID-19 pandemic remains a crucial consideration as China remains more sensitive to the spread of the disease. China's zero-COVID lockdown policy was tested towards the end of the quarter with cases reaching their highest level since the start of the pandemic. The surge in cases comes while the property sector

remains under enormous pressure as the 'three red lines' policy continues to restrict the flow of credit to a heavily levered sector.

The Reserve Bank of Australia (RBA) is presiding over a more favourable growth/inflation trade off with less inflationary pressure and economic resilience supported by very high commodity prices. The RBA started the process of normalising policy late last year when they abandoned the yield curve control policy. We expect the cash rate to increase from 0.1% this year, but at a much slower pace than the Fed.

Tightening monetary policy, slowing growth, disrupted supply chains and increasing geopolitical tension all contribute to a very challenging outlook for financial markets. Equity valuations are at extremes on just about all metrics -- except relative to interest rates. Meanwhile, bond yields -- while rising -- are very low relative to historical levels and could go significantly higher. Against this backdrop, the most exposed part of the market would be growth stocks, while value and quality could be expected to be much more resilient.

The Fund's significant underweight allocation to fixed income and credit was a significant contributor to outperformance during the quarter. Much higher inflation and very tight labour markets led to a complete recalibration of monetary policy expectations which was the key driver of much weaker fixed income markets. For some time, the Fund has retained a substantial underweight allocation to fixed income (including credit) due to valuation concerns and a corresponding overweight cash position. The Fund remains substantially underweight, notwithstanding a marginal increase in its allocation to domestic fixed income late in the quarter.

Stock selection within global equities was a substantial contributing factor to outperformance over the March quarter. The Fund's quality and value biases in global equities performed well as growth stocks are more exposed to rising interest rates. The Fund's emerging market equity stock selection also performed well during the quarter as a result of its underweight exposure to China. Australian equity stock selection was close to flat, outperforming through the first two months of the year before moderating in March. The Fund is marginally underweight across domestic and global equities. All equity exposures retain their long-standing quality and value bias which are expected to continue to outperform against a backdrop of rising interest rates.

The Fund's strategic allocation to foreign currency detracted from performance as the Australian dollar strengthened, supported by much higher commodity prices. The Fund maintains a significant foreign exchange exposure, diversified across a number of developed and emerging market currencies.

The Fund's allocation to uncorrelated sources of return were constructive for performance during a turbulent quarter. The fund maintains its position in the Diversified Real Return Fund which continues to deliver low volatility absolute returns while retaining a relatively low correlation to equity markets.

## OUTLOOK

Following a dramatic repricing of monetary policy expectations over the past six months, the remainder of 2022 will likely be dominated by the impact of central banks, led by the Fed, unwinding their extreme policy settings. Slowing economic growth, geopolitical risks and the path of the pandemic will also be critical considerations for investors. There are few places for conservative investors to hide.

The massive monetary expansion led by the US Federal Reserve has limited the attractiveness of defensive assets including government bonds. The subsequent economic recovery and increasing inflation risk has put significant upward pressure on interest rates. The tightening of monetary policy presents a major challenge to financial markets as liquidity is reduced and discount rates increase. Of course, geopolitical developments and the pandemic remain key risks that could also destabilise markets. In this climate the fund remains well positioned to navigate the tightening cycle and retains the capacity to add risk as valuations become more attractive.

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The Diversified Growth Fund gains its exposure to Australian Shares by investing in an underlying Australian Share Fund/s which primarily invests in Australian listed or soon to be listed shares but may have up to 20% exposure to stocks outside Australia. The investment guidelines showing the Fund's maximum investment in international shares do not include this potential additional exposure. Short positions may be part of the underlying Australian Share Fund's strategy. Currency hedges may be used from time to time.

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## MORE INFORMATION

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