

## Wholesale Funds

# PERPETUAL WHOLESAL DIVERSIFIED GROWTH FUND

June 2021

### 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

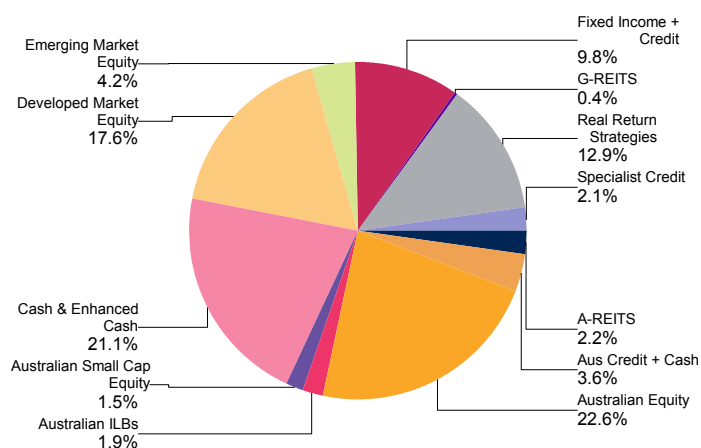
**Management Fee:** 0.96% p.a.

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



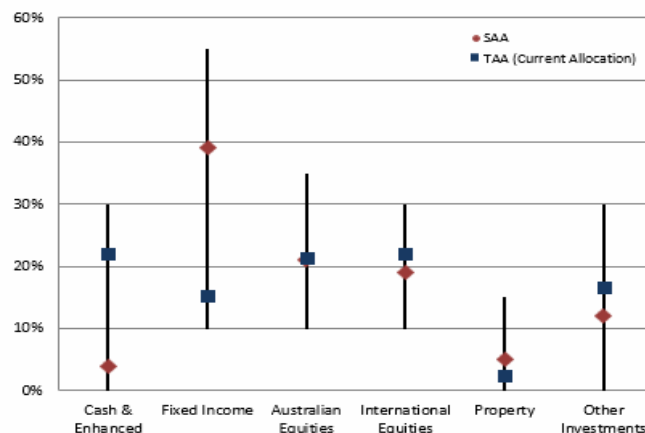
### NET PERFORMANCE- periods ending 30 June 2021

	Fund	Benchmark	Excess
1 month	0.9	1.8	-0.8
3 months	3.7	4.8	-1.1
FYTD	15.1	13.4	1.7
1 year	15.1	13.4	1.7
2 year p.a.	6.9	6.9	0.0
3 year p.a.	7.2	7.8	-0.6
5 year p.a.	6.8	7.8	-1.0
10 year p.a.	7.4	7.8	-0.3
Since incep.	6.4	6.4	0.0

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

### ASSET ALLOCATIONS AND INVESTIBLE RANGES

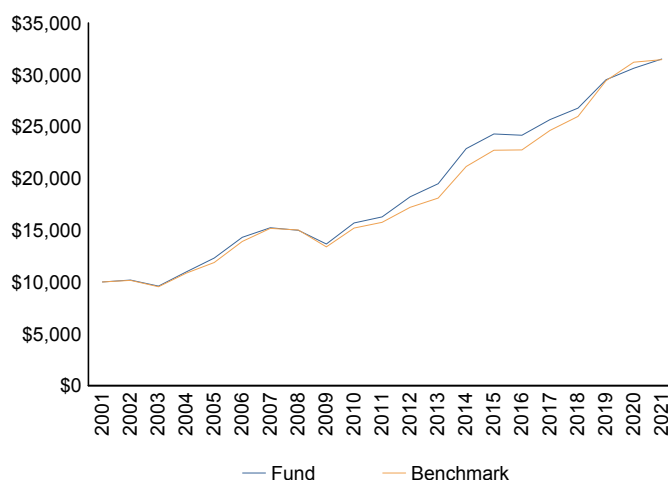
FUND TACTICAL AND STRATEGIC ALLOCATIONS INCLUDING ALLOWABLE MAXIMUM AND MINIMUM RANGES



### 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

As expected, the global economy is rebounding very strongly in 2021, led by the US in the first half of this year to be followed by Europe and emerging market economies (excluding China) in the second half as lockdowns and other social mobility restrictions ease.

Global growth was very strong in the first half and is expected to accelerate in the second half of 2021 as the vaccination roll-out continues apace releasing pent up demand in reopening economies in the developed world. Growth is expected to slow in 2022 as fiscal policy becomes a drag and pent up demand is satisfied.

As a result, profit estimates for this year and next continue to be revised up, so much so that 2022 earnings per share in the US are expected to be almost a third higher than in 2019.

There are, however, some more problematic developments for the market outlook:

- Inflation in the US has been much higher than expected in recent months. These misses have been attributed to 'transitory factors' caused by supply side bottlenecks, most notably in used cars (as a spill-over from excess demand for new cars) as well as sporting goods, furniture and appliances. A lot hinges on this assessment as monetary policy settings are so extreme – our own view is that core inflation will subside from recent levels back towards 2% next year as some of these 'one-offs' reverse. With growth estimates expected to be well above potential growth however, average core inflation will likely be somewhat higher than we previously estimated.
- The emergence of the highly contagious delta variant has wreaked havoc in India and has now become the dominant strain in the UK and is growing rapidly elsewhere. The growth in cases in the UK has happened despite a population with a high level of natural immunity and vaccinations. On the more encouraging side, there are some indications that the vaccine is working to significantly reduce the risk of severe disease.
- The outlook for Australia is especially delicately poised given the combination of a highly contagious variant and very low levels of vaccination and natural immunity. The economy has recovered very well but the second half of 2021 is going to be difficult to navigate if the virus becomes established in the most populous states.

Financial markets are continuing to run hard with the upbeat growth and profits story, while largely ignoring the risks created by recent higher inflation prints and the emergence of the delta variant. In fact, there are very few signs of distress in financial markets as equity, credit and commodity markets all continue an amazing run of performance which began in the depths of despair at the onset of the covid-19 crisis in March last year:

- Global equity markets continue to perform very strongly, at first led by growth stocks in 2020 (particularly the technology sector) as the US 10-year rate fell under 1%. Value stocks have taken over so far this year, but the technology behemoths (Amazon, Google, Apple, Microsoft and Facebook) are still trading at or close to record highs.
- Commodity markets are very buoyant – iron ore prices are at record highs; copper prices are around the record highs of 10 years ago; and oil prices have recovered strongly after trading at negative prices in April last year.
- Credit spreads are very tight. For example, the spread on US high yield (or 'junk') debt is less than 3%. Moreover, benchmark government bond yields subsided somewhat in the June quarter, notwithstanding the spike in US inflation. As a result, government bond yields are still remarkably low with 10-year bonds in the major markets ranging from -0.17% in Germany to 0.05% in Japan and 1.5% in the US and Australia. And the value of negative yielding debt in the Barclays Global Aggregate Index (an index of global government and corporate investment grade debt) is still

USD14trillion or 20% of the index.

- Currency markets have been marked by a weaker USD in 2020, but volatility in these markets is near 20-year lows.

Perhaps one sign of distress in markets is a major correction in bitcoin in the June quarter (of 41%). Even after this correction, however, bitcoin is still up nearly 280% from a year ago!

How do we make sense of these ebullient markets for risky assets like equities and commodities at the same time as the increase in bond yields has been quite limited? In our view, the answer is liquidity. Central banks went to 'tilt' monetary policy settings when the coronavirus hit early last year with zero (or negative) policy rates in all major economies supported by massive quantitative easing (QE) programs. While the global economic recovery is now well established, there has been very little change so far in the guidance for monetary policy from the key central banks (the US Federal Reserve, the European Central Bank and the Bank of Japan). The strongest year of economic growth in many decades and a series of upside inflation surprises sits awkwardly with current policy settings.

In our judgement, this is why the bond market has been able to stabilise and the secular bull market in bonds over the past four decades remains very much intact. Indeed, interest rates are not far above their lowest levels ever (reached last year) underpinning eye-watering valuations in many key markets (like US equities). As the stimulus is inevitably wound back, we expect a more difficult backdrop for markets and particularly for those investments where the valuation is most sensitive to the level of interest rates.

It is difficult to be precise about the timing of such a major change. As usual one central bank, the US Federal Reserve (the Fed), will dominate the narrative. For now, we are in a holding pattern awaiting more inflation data, developments on the delta variant and central bank policy decisions.

Once again, the main contributor to absolute performance was the Fund's global and Australian equity allocations. The Fund is slightly overweight Australian equities and overweight global equities which added to relative performance during the quarter. The June quarter, however, saw the rotation from growth to value stocks cool. Following very strong performance in the March quarter, style positioning and stock selection in global equities detracted somewhat from performance.

Equity exposures retain their long-standing quality and value bias which significantly contributes to the defensive attributes of the Fund. Moreover, after an extended period of under-performance, we expect a period of sustained out-performance from 'value' relative to 'growth' in the next 3 to 5 years.

With the strong performance of equity markets, the portfolios cash allocation detracted from performance. However, this was more than offset by the positive contribution from an underweight allocation to fixed income and credit.

We continue to prefer cash to government bonds in the defensive part of the portfolio. The stretched valuations of government bonds limit their upside potential while their defensive utility is compromised. A key feature of portfolio construction for the past four decades has been the diversification benefit of owning bonds (with bonds rallying when equities are in bear markets). This time, bonds appear vulnerable and could continue to be the cause of a significant rotation within equity markets. Given the low compensation for the risk of default, the Fund also has very low exposure to credit.

The fund has substantial foreign exchange exposure diversified across a number of developed and emerging market currencies.

Finally, 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

The global economy is currently positioned for a significant recovery in 2021. The extraordinary monetary and fiscal policy response to the COVID-19 crisis has been very successful in minimising the damage of a massive shock to the global economy. The policy response has also had a pervasive impact on the valuation and outlook for many key markets. The massive monetary expansion led by the US Federal Reserve has limited the attractiveness of defensive assets including government bonds and the US dollar (which has fallen significantly over the past year). In addition, credit markets are distorted with spreads much tighter than would be indicated by the state of the economy and the risk of default. Finally, extraordinarily low interest rates are intensifying the hunt for yield and contributing to very expensive equity valuations. In this climate the fund remains well positioned to benefit from the improving macro outlook, while maintaining a defensive profile through its value and quality biases in equity exposures and allocation to sources of uncorrelated returns.

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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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