

## Perpetual Investments

# PERPETUAL ETHICAL SRI CREDIT FUND

August 2021



### FUND FACTS

**Investment objective:** To provide investors with regular income and consistency of return by investing in a diversified range of income generating, ethical and socially responsible assets. To outperform the stated benchmark over rolling three year periods before fees and taxes.

**Benchmark:** Bloomberg AusBond Bank Bill Index  
**Inception date:** June 2018  
**Size of fund:** \$54.8 million as at 30 June 2021  
**APIR:** PER1744AU  
**Mgmt cost:** 0.59%pa\*  
**Benchmark Yield:** 0.03% as at 31 August 2021  
**Suggested minimum investment period:** Three years or longer

### FUND BENEFITS

Provides investors access to an actively managed fund that more closely matches their personal social and ethical beliefs or preferences, without compromising investment returns over the long term.

### 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.

### TOTAL RETURNS % (AFTER FEES) AS AT 31 August 2021

	1 MTH	3 MTHS	6 MTHS	1 YR	2 YRS PA	3 YRS PA	5 YRS PA	7 YRS PA	INCEPT PA
Perpetual Ethical SRI Credit Fund	0.17	0.53	1.43	4.35	2.83	2.96	-	-	2.86
Bloomberg AusBond Bank Bill Index	0.00	0.01	0.02	0.04	0.35	0.84	-	-	0.93

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

### POINTS OF INTEREST

- Domestic spreads tighten marginally.
- Financials outperform corporates.
- Primary market issuance robust.
- Credit outlook remains strongly positive.

### ETHICAL EXCLUSIONS AND SRI SCREENING

There are two main steps to the process, namely ethical exclusions and socially responsible investments (SRI) screening.

#### ETHICAL EXCLUSIONS

We don't invest in issuers or counterparties that derive a material proportion (5% or more) of their revenue from:

- the manufacture or sale of alcohol or tobacco<sup>^</sup>
- the operation of gambling facilities or the manufacture of gambling equipment
- fossil fuels (upstream)
- uranium and nuclear
- animal cruelty (cosmetic testing)
- genetic engineering
- pornography
- armaments (including weapons)<sup>^</sup>

<sup>^</sup>For involvement in the production of tobacco, tobacco based products and the development and production of controversial weapons, a 0% revenue threshold is applied.

#### SRI SCREENING

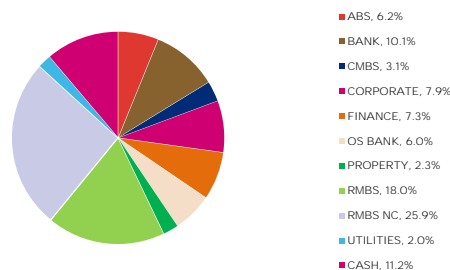
Issuers or counterparties remaining after the ethical exclusions are then subject to an SRI screening to evaluate how their business practices impact society and the environment, while other companies become allowable investments.

#### SOVEREIGN ISSUERS

Governments will be analysed on ESG factors, based on a scoring system utilising research from external specialists. This may include, but is not limited to, considering any unethical practices such as corruption, rule of law and political instability of the sovereign.

For further details on the Ethical Exclusions or SRI screening please refer to the PDS.

### PORTFOLIO SECTORS



### PORTFOLIO COMPOSITION

	BREAKDOWN
Senior Debt	46.07%
Subordinated Debt	46.21%
Hybrid Debt	7.73%
Running Yield <sup>^</sup>	1.41%
Portfolio Weighted Average Life	3.31 yrs
No. Securities	120
Modified Duration	-0.17

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

<sup>^</sup>The methodology used to calculate Running Yield is derived from FactSet, and calculated as follows: The coupon rate of the security / the capital price of the security. Note that the exception is discounted securities, where a Yield to Maturity calculation is used.

## MARKET COMMENTARY

Financial markets were mixed during August. Global equities continued to march higher, rallying throughout the month. Economic growth expectations however continued to be revised down as a result of the spread of the delta variant and continued supply chain disruption. A slew of leading indicators turned over during August with global service and manufacturing PMIs falling, most notably in China.

Domestic yields were steady through August in spite of the continued impact of the delta variant. Longer term yields outperformed and the yield curve flattened slightly. The RBA maintained their tapering schedule in spite of the continued lockdown in New South Wales. Semi-government spreads widened in August reflecting the elevated issuance schedule over the prior months.

Domestic credit spreads tightened slightly while remaining rangebound over the month. Financial spreads outperformed corporates during August. The credit curve flattened somewhat with longer dated credit outperforming. Credit volatility remains subdued with supportive conditions and low yields contributing to the stability in credit spreads. Reporting season results were mixed for credit markets. While corporate earnings were unquestionably strong, there was increased uncertainty with regards to forward guidance as a result of the spread of the delta variant and the impact of ongoing lockdowns in Australia.

Corporate and financial issuance was elevated in August, in line with seasonal trends following reporting season. Pacific National Finance came to market for \$400M following the release of their earnings. The deal was met with demand more than twice the deal size and priced 10bps tighter than initial guidance. NBN Co continued to tap the Australian credit market raising \$825M in a 3-year deal as they seek to replace their expiring government funding. The securitisation market remained active with a number of deals priced across ABS and RMBS. In spite of the active issuance schedule, securitised spreads ground tighter over the month, notably in subordinated tranches.

## PORTFOLIO COMMENTARY

Income return was the key contributing factor to outperformance over the month. The portfolio collected running income in excess of the benchmark across all corporate and collateralised sectors. Contributions to income return were broad based, led by RMBS, non-financial corporate, domestic and offshore banks. The portfolio running yield at month end was 1.4% with the spread measured at 1.2%.

Credit spread tightening contributed to outperformance. Financial spreads outperformed corporates and the Fund's exposure to domestic and offshore banks performed well. Most notably, the Fund's exposure to subordinated and hybrid Bank debt contributed to credit spread performance. The Fund's allocation to securitised sectors also contributed to credit spread return, subordinated spreads in the ABS and RMBS sectors ground tighter over the month in spite of an active issuance schedule.

The manager was selective with purchases made during the month. Over the past months, the Fund's risk profile has been adjusted to reduce credit risk. Allocation to AAA rated RMBS and ABS has been increased while profits were taken on a number of strong performing corporate positions. The manager continued to build the fund's exposure to short dated AAA subordinated RMBS which offer competitive compensation for low risk. The Fund also took part in the new subordinated deal from Commonwealth Bank.

While the credit outlook remains positive, the fund remains fully invested, albeit returning to a more defensive posture given historically low credit premiums. During the month the manager added to the bought protection (short) position in an index credit default swap in order to hedge tail risks. With many credit spreads tighter than their pre-COVID levels, active management is crucial in managing downside risk and identifying the remaining pockets of compelling relative value in the credit market.

The fund applies both ethical and socially responsible investment (SRI) screens relating to what the company is in the business of and the way business operations are conducted respectively. Upon application of the ethical and SRI screens, several bond issuers have been screened out - including for example, companies involved in the extraction of fossil fuels or companies whose revenues are significantly associated with socially questionable products or services.

## OUTLOOK

The credit outlook has remains strongly positive.

Valuation indicators are neutral. Spreads have contracted significantly over the past year reaching below their pre COVID levels.

The growth outlook remains strongly positive. Global PMIs softened during the month as a result of COVID concerns and continued supply chain disruption. Growth expectations continued to be revised down during the month and are now neutral. The ratio of credit rating upgrades to downgrades remains very supportive.

Demand and supply indicators continue to positively contribute to the overall credit outlook. Issuance volume in the primary credit market is below trend relative to long term averages. Reduced primary market activity over the recent months continue to support credit spreads.

Technical indicators remain neutral to the overall credit outlook. US credit spreads continue to marginally detract from the overall credit score while, robust equity valuation and volatility continue to be supportive for domestic spreads.

The credit outlook remains strongly positive, supported by supply and demand factors as well as robust corporate earnings and improved credit ratings. The portfolios remain well positioned to take advantage of relative value opportunities presented by the current market conditions.

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## MORE INFORMATION

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