

## Perpetual Investments

# PERPETUAL ETHICAL SRI CREDIT FUND

April 2022



### 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:** \$51.7 million as at 31 March 2022  
**APIR:** PER1744AU  
**Mgmt cost:** 0.59%pa\*  
**Benchmark Yield:** 0.05% as at 30 April 2022  
**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 30 April 2022

	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	-0.30	-1.11	-1.05	-0.32	3.35	1.90	-	-	2.09
Bloomberg AusBond Bank Bill Index	-0.02	-0.01	0.01	0.02	0.04	0.40	-	-	0.77

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

- Financial markets sell off on accelerated monetary tightening.
- Credit spreads mixed; financials underperform corporates.
- Short end yields sell off; US AU spread widens.
- Financial issuance robust; corporate issuance subdued.
- The credit outlook remains marginally 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

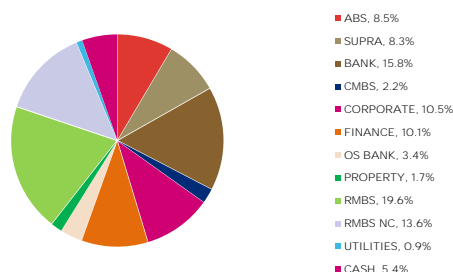
Issuers or counterparties remaining after the ethical exclusions are then subject to an SRI screening to evaluate how their business practices impact society and the environment, while other companies become allowable investments.

#### 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	42.14%
Subordinated Debt	48.25%
Hybrid Debt	9.62%
Running Yield <sup>^</sup>	2.02%
Portfolio Weighted Average Life	3.68 yrs
No. Securities	117
Modified Duration	0.65

\* 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 roiled in January with bonds and equities selling off. Global equity fell sharply as the expectation of accelerated monetary policy tightening weighed on valuations. Further contributing to reduced investor sentiment was increasing geopolitical tensions, mixed early company earnings results, persistent high inflation and the continued disruption caused by the Omicron variant.

Domestic spreads were broadly resilient to the increased volatility in rates markets. Corporate spreads remained rangebound while financials – led by regional and offshore banks – widened slightly. Persistent high inflation, acceleration of The Fed's tapering and tightening schedule and elevated credit issuance saw US spreads widen more sharply. Earnings results for US banks showed increasing expense and margin pressure which impacted financial spreads. Despite some slowing indicators, domestic credit spreads remain supported by robust economic and earnings growth.

Australian Dollar yields rose in January and the curve flattened as the short end sold off. Notably, the AU 10-year yield traded briefly above 2% for the second time since March 2019. The rise in Australian dollar yields reflected both the surge in December CPI and the broader global rise in yields precipitated by the acceleration of Fed policy. US yields rose more dramatically, and the Australian dollar fell against the greenback as the US AU 10-year spread narrowed. The domestic rates market continues to anticipate rate increases in 2022 despite the RBA maintaining that rate rises would remain on hold until at least 2023. At month end, the futures curve priced in a March rate rise and a swift rise in the target cash rate.

Primary issuance was elevated through the first three weeks of January leading to the highest aggregate January volume since 2011. The increased volume was led by financial issuers while the corporate primary market was more subdued. The securitisation market was quiet, in line with seasonal expectations.

## PORTFOLIO COMMENTARY

Income return was the key contributor to relative performance 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 2.02% with the spread measured at 1.87%.

Widening credit spreads detracted from performance during January. Credit spread dynamics were mixed with financials widening somewhat while corporates traded in a tight range. Financials – led by regional and offshore banks were the most significant detractors from credit spreads return during the month. The Fund's allocation to securitised sectors including RMBS contributed to credit spread return while exposure to non-financial corporate detracted marginally. While widening credit spreads in some sectors contributed to the negative return, month to month volatility continues to be substantially offset by the portfolio's robust running yield.

Sector and risk allocations were broadly maintained over the month. The Manager was selective in purchases made despite strong primary issuance volumes in the financial sector. The Fund's weighted average life was selectively lengthened and exposure to domestic banks was increased via a regional bank senior bond purchased in primary.

The outlook for credit remains marginally positive, supported by robust credit quality. The fund's elevated cash holdings are reflective of seasonal positioning over the holiday period and a defensive posture given historically low credit premiums.

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 remains marginally positive.

Valuation indicators are benign. Concerns surrounding the Omicron variant and a more hawkish stance from the Fed have contributed to widening spreads across US investment grade, high yield and AU investment grade. The basis swap has normalised and is no longer detracting from the overall credit outlook.

The growth outlook has moderated while remaining slightly positive. PMIs – while remaining robust – have fallen from their 2021 highs. The recent spike in the oil price is expected to weigh on the outlook. Credit quality – expressed by the ratio of upgrades to downgrades – continues to strongly contribute to the overall outlook.

Demand and supply indicators have further cooled and are now neutral. Market demand has been more selective than recent months, with a number of new deals trading wider than issue by month end.

Technical indicators are marginally negative for the overall credit outlook. Investor and intermediary cash balances are very low relative to historical levels, weighing on the outlook for credit spreads. The team will continue to monitor technical and supply demand indicators to identify inflection points in investor risk sentiment.

The credit outlook has tempered recently as credit markets face risks in the form of central bank tapering and the Omicron variant. At the end of a long rally in spreads, the credit outlook remains supported by positive macroeconomic indicators while valuation, technical, and supply and demand indicators have moderated. The portfolios are well positioned to continue to deliver income and defend capital in these conditions.

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## MORE INFORMATION

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