Perpetual Investment Funds

# PERPETUAL DYNAMIC FIXED INCOME FUND

May 2023

## FUND FACTS

**Investment objective:** Aims to provide capital stability and regular income by investing in a diversified range of income generating assets, and a positive return (before fees and taxes) irrespective of market conditions over a rolling three-year period.

**Benchmark:** 50% Bloomberg AusBond Composite Index/50% Bloomberg AusBond Bank Bill Index
**Inception date:** November 2010
**Size of fund:** $35.8 million as at 31 March 2023
**APIR:** PER0557AU
**Mgmt Fee:** 0.45% pa*
**Suggested minimum investment period:** Three years or longer

## FUND BENEFITS

The fund is designed to provide investors with a diversified fixed income solution that manages both credit risk (credit worthiness) and duration risk (sensitivity to changes in interest rates) in different economic conditions.

## 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 May 2023

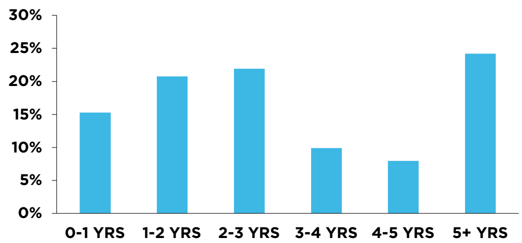
| | 1 MTH | 3 MTHS | 6 MTHS | 1 YR | 2 YRS PA | 3 YRS PA | 5 YRS PA | 7 YRS PA | INCEPT PA |
|---|---|---|---|---|---|---|---|---|---|
| Perpetual Dynamic Fixed Income Fund | -0.27 | 0.88 | 2.08 | 2.15 | -0.94 | 0.86 | 1.76 | 2.33 | 3.91 |
| Bloomberg AusBond Composite/Bank Bill Blend | -0.46 | 1.51 | 1.56 | 2.24 | -1.08 | -0.90 | 1.10 | 1.34 | 2.95 |

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

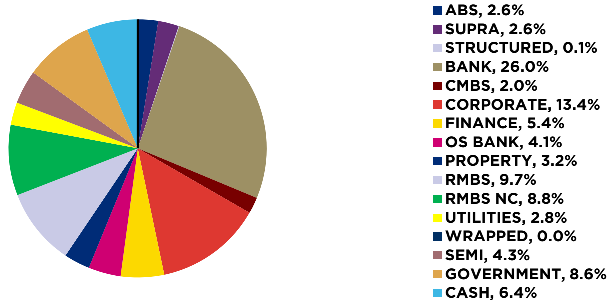
## POINTS OF INTEREST

•Markets price further tightening;
•Domestic yields rise, curve steepens;
•Credit spreads rangebound; credit curve steepens;
•Corporate issuance rebounds; securitisation remains robust;
•The outlook for credit remains marginally negative;

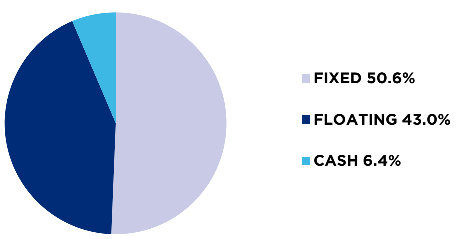
## MATURITY PROFILE




## PORTFOLIO SECTORS




## FIXED AND FLOATING RATE BREAKDOWN




## PORTFOLIO COMPOSITION

| | BREAKDOWN |
|---|---|
| Senior Debt | 64.84% |
| Subordinated Debt | 31.63% |
| Hybrid Debt | 3.53% |
| Running Yield# | 4.47% |
| Portfolio Weighted Average Life (yrs) | 3.67 |
| No. Securities | 260 |
| Modified Duration | 0.63 |

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

## MARKET COMMENTARY

Financial markets saw mixed fortunes during May as equity and bond markets continue to price in starkly different outlooks for global growth. The fight over the US debt ceiling and the looming threat of a US default had an impact with US short end yields spiking during the month. Elsewhere, markets tried to anticipate the path of monetary policy tightening as central banks continue to grapple with stubbornly high core inflation and resilient labour data.

Domestic bond yields rose throughout May as markets adjusted to the RBA's surprise rate hike and parsed their increasingly hawkish commentary. The RBA elected to increase rates at their May meeting and their rhetoric was adjusted to include reaching target inflation levels "in a reasonable timeframe" which prompted markets to anticipate further rate hikes in the near term. While headline inflation has eased throughout 2023, this has been primarily attributable to moderating goods prices while services sector inflation remains intransigent. The domestic yield curve steepened as 1 and 2-year yields sold off sharply and the inversion of the short end deepened further.

Credit spreads were relatively benign during May, trading in range of recent levels. Financials marginally outperformed corporates on aggregate as global banking sector concerns continued to ease. The credit curve steepened with shorter dated spreads outperforming while long dated issues saw more widening. Swap to bond spreads narrowed as bond yields rose more rapidly than swap rates.

The domestic primary market welcomed back non-financial corporate issuance during May following an extended lean period. Australian Postal Corporation raised $100M in a fixed rate Sustainability bond deal. Meanwhile, TransGrid ($500M), Ausnet ($700M) and PACCAR financial ($200M) also contributed to the nascent resurgence in corporate issuance. Financial sector issuance remained robust, headlined by NAB's $5.25B deal which priced in early May across 3 and 5-year fixed and floating tranches. The Securitisation market continued to be active with the recent trend of elevated Auto ABS issuance persisting.

## PORTFOLIO COMMENTARY

The Fund's running income was a substantial positive contributor to relative return, partially offsetting the impact of rising bond yields. Domestic and offshore banks alongside RMBS were the key drivers of income return with non-financial corporate exposures also contributing. The income generated by the Fund's floating rate credit exposures continues to benefit from rising interest rates. The portfolio running yield at month end was 4.5%.

Rising bond yields were the most significant determinant of return during the month. Domestic yield moved higher over the month following the RBA's decision to increase rates at their May meeting in anticipation of further tightening. Facing persistently elevated core inflation and a backdrop of slowing global growth, the path of monetary policy tightening is uncertain, and risk of policy errors remains elevated. In such conditions, the Fund's relatively short target duration continues to limit downside risks and mitigate the impact of month-to-month yield volatility. During the month, the manager elected to reduce the Fund's duration in line with the worsening Tactical Asset Allocation Bond Score. At month end, the Fund's modified duration was 0.6 years.

Credit spread dynamics were marginally negative for performance during May as spreads traded in range of recent levels. The Fund's semi-government and securitised exposures contributed to credit spread return while longer dated domestic bank paper and real estate investment trusts detracted slightly. Following a substantial de-risking of the portfolio over recent months credit risk was marginally increased during the month as the outlook improved.

In line with the challenging outlook for credit, the Manager remains cognisant of risks and selective in purchases made. Fund remains defensively positioned while retaining the capacity to take advantage of relative value opportunities presented by recent volatility.

## OUTLOOK

The Credit outlook improved towards the end of May, remaining slightly negative.

Valuation indicators have improved to neutral. Spreads remain in range of historical averages across Australian investment grade, US investment grade and high yield. The relative attractiveness of Australian Dollar credit has improved somewhat on the back of narrowing spreads vs offshore comparable as well as the tightening of USD AUD basis swaps.

Macro indicators continue to detract from the overall credit outlook. Tightened financial conditions as described in the Fed's Senior Loan Officer survey remain a significant headwind. The ratio of credit rating upgrades to downgrades has improved to neutral with a number of investment grade issuers upgraded following a US reporting season.

Supply and demand indicators remain marginally negative. Robust aggregate issuance volumes continue to weigh on the outlook for spreads.

Technical indicators are constructive. While cash levels across real money accounts have moderated, demand from intermediaries remains healthy. US credit, equity and equity volatility indicators are supportive for the credit outlook.


*** The benchmark for the Fund was previously reported as both the Bloomberg AusBond Bank Bill Index and the Bloomberg AusBond Composite Index. As at 29 April 2015, the benchmark for reporting was updated to a composite benchmark comprising 50% Bloomberg AusBond Bank Bill Index & 50% Bloomberg AusBond Composite Index. The change in benchmark was to better reflect the investment strategy. The performance table above reflects the change in benchmark applied across all periods.

## MORE INFORMATION

Adviser Services 1800 062 725
Investor Services 1800 022 033
Email investments@perpetual.com.au
www.perpetual.com.au