

## Perpetual Investment Funds

# PERPETUAL ESG CREDIT INCOME FUND - CLASS A

July 2023

### FUND FACTS

**Investment objective:** To provide investors with regular income and consistent returns above the Bloomberg AusBond Bank Bill Index (before fees and taxes) over rolling three-year periods by investing in a diverse range of income generating assets that meet Perpetual's ESG and values-based criteria.

**Benchmark:** Bloomberg AusBond Bank Bill Index  
**Inception date:** June 2018  
**Size of fund:** \$67.8 million as at 30 June 2023  
**APIR:** PER1744AU  
**Mgmt cost:** 0.59%pa\*  
**Benchmark Yield:** 3.89% as at 31 July 2023  
**Suggested minimum investment period:** Three years or longer

### FUND BENEFITS

Provides investors access to an actively managed credit and fixed income fund and the opportunity to align their investments with their personal values and ESG preferences.

### 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 July 2023

	1 MTH	3 MTHS	6 MTHS	1 YR	2 YRS PA	3 YRS PA	5 YRS PA	7 YRS PA	INCEPT PA
Perpetual ESG Credit Income Fund – Class A	0.67	1.83	3.21	6.79	2.51	3.32	2.76	-	2.74
Bloomberg AusBond Bank Bill Index	0.37	0.97	1.81	3.15	1.67	1.13	1.20	-	1.23

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

- RBA on hold: Yield curve flattens;
- Domestic credit spread tightens; Bank sub outperforms;
- Primary market issuance very light; secondary demand robust
- The outlook for credit has improved to neutral.

### ESG AND VALUES-BASED CRITERIA

The Fund invests in quality issuers that meet Perpetual's ESG and values-based criteria as detailed below.

#### VALUES-BASED CRITERIA

The Fund will not invest in issuers that derive a material proportion (5% or more) of their revenue\*\* from:

- the manufacture or sale of alcohol or tobacco\*\*\*
- the operation of gambling facilities or the manufacture or supply of gambling products
- uranium and nuclear
- armaments (including weapons)\*\*\*
- fossil fuels (exploration and extraction)
- genetic engineering
- pornography
- animal cruelty (cosmetic testing)

\*\*Generally calculated using the total gross amount of income generated by the sale of good or services from normal business operations.

\*\*\*For involvement in the production of tobacco, manufacture of nicotine alternatives and tobacco-based products and the development, production and maintenance of controversial weapons, a 0% revenue threshold is applied.

#### ESG CRITERIA

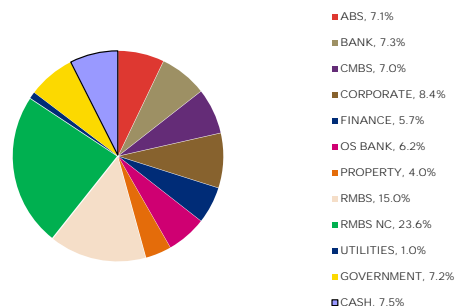
Additionally, issuers are scored (both positively and negatively) on a broad range of ESG factors such as the issuers environmental policy and strategy, how it considers ESG factors in its supply chain management and whether it has been involved in any corporate misconduct.

#### SOVEREIGN ISSUERS

Governments are 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 ESG and values-based criteria please refer to the PDS.

### PORTFOLIO SECTORS



### PORTFOLIO COMPOSITION

	BREAKDOWN
Senior Debt	39.10%
Subordinated Debt	52.64%
Hybrid Debt	8.26%
Running Yield <sup>^</sup>	5.81%
Portfolio Weighted Average Life	2.85 yrs
No. Securities	112
Modified Duration	0.60

\* 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

Global financial markets consolidated on a strong first half for risk assets in July. Equities continue to grind higher, while credit spreads tightened across multiple markets. Bond yields were mixed with domestic yields sedate following the RBA's decision to hold in early July, while US long term yields moved higher, responding to further tightening from the Fed.

The RBA elected to keep rates on hold at 4.1% in July following the surprise hike in early June. 2nd quarter CPI released during the month showed moderating headline inflation however inflation in services sectors remains intractable and employment data remains robust. Futures markets at month end had priced an imminent peak in tightening suggesting less than one 25bps increase remaining. The domestic yield curve steepened during the month with long-term yields rising marginally while the short end rallied. US 10-year yields sold off as the Fed continued to raise rates and maintained its hawkish outlook and rhetoric.

Domestic credit spreads tightened over the month supported by improving investor risk appetites. Corporate and tier 2 financial spreads saw the most substantial tightening reflecting lack of supply in primary. Euro and US Dollar spreads continued to outperform domestic peers, rallying during July.

Primary issuance was subdued relative to average monthly volumes over the last 12 months. July saw the lowest aggregate monthly volume thus far in 2023. While this reflects seasonal trends – domestic issuers typically come to market after reporting season – it represents a significant cooling of issuance activity relative to the strong start to the year. Securitisation volumes remained resilient with Bank of Queensland pricing \$1B of RMBS while Think Tank raised \$500M in a CMBS deal.

## PORTFOLIO COMMENTARY

Income return was a substantial contributor to outperformance during the month, led by RMBS, banks and non-financial corporates. The portfolio's running yield was 5.8% at month end, with the spread measured at 2.1%.

Credit spread tightening was the most significant contributing factor to return during the month. Domestic spreads narrowed over the month on supportive supply dynamics and increasing investor risk appetites. Subordinated bank exposures performed well as tier 2 and hybrid paper tightened, reflecting elevated secondary market demand and a paucity of new issues. Tightening RMBS spreads also contributed to outperformance. Lastly, the Fund benefitted from exposure to foreign denominated credit across multiple sectors. USD spreads outperformed AUD counterparts and the Fund's exposure to USD denominated corporates, domestic and offshore banks were constructive. The Manager elected to lock in recent profits on a n EUR denominated bond from Ausnet following an extended rally.

In recognition of tightening financial conditions, the Fund continues to maintain a highly liquid sleeve (~15-18%) of cash and government securities which protects against liquidity tail risks. The Fund maintains a small (0.6 years) duration exposure as a result of the government bond allocation.

Primary market activity was subdued and the Manager was selective in purchases made during the month. The Fund increased its exposure to CMBS via a new \$500M Think Tank deal. Early in July, the Manager elected to add exposure to a recently issued EUR denominated Morgan Stanley senior bond which tightened throughout the remainder of the month, contributing to outperformance.

While the outlook for credit has improved, the Manager remains conscious of the implications of slowing growth and tightening financial conditions for credit valuations and liquidity. The Fund remains defensively positioned while retaining the capacity to take advantage of relative opportunities presented as the outlook improves.

The Fund invests in quality issuers that meet Perpetual's ESG and Values based criteria relating to what the company is in the business of and the way business operations are conducted respectively. Upon application of the ESG and Values based criteria, several bond issuers have been screened out. These include, 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 improved to neutral over the course of the month.

Valuation indicators remain negative. While spreads remain in range of historical averages across Australian and US investment grade, tightening US high yield spreads no longer offer attractive value relative to recent levels. Widening USD AUD basis swaps increase the attractiveness of domestic markets for issuers, continuing to detract slightly from the outlook.

Macro indicators remain negative. The slowing pace of economic growth and tightening financial conditions as described in the Fed's Senior Loan Officer continue to weigh on the outlook.

Supply and demand indicators have improved over the month and are now marginally positive. Demand has been robust across primary and secondary markets. While primary market activity eased in July, the elevated pace of issuance observed through the first 6 months of the year continues to weigh on the outlook.

Technical indicators have improved, providing a solidly positive signal by month end. Cash levels of real money accounts remain benign while intermediary demand is supportive. US credit, equity and equity volatility indicators are supportive for the credit outlook.

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## MORE INFORMATION

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