

Perpetual Investment Funds

PERPETUAL BALANCED GROWTH FUND

September 2022

FUND FACTS

Investment objective: The fund aims to provide long-term capital growth and income through investment in a diversified portfolio with an emphasis on Australian and international share investments.

FUND BENEFITS

Provides investors with access to a diverse range of growth and income producing assets. Active management and asset allocation techniques are employed in order to further enhance the fund's return 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: Balanced Growth Index (Internally generated composite)

Inception Date: October 1997

APIR: PER0063AU

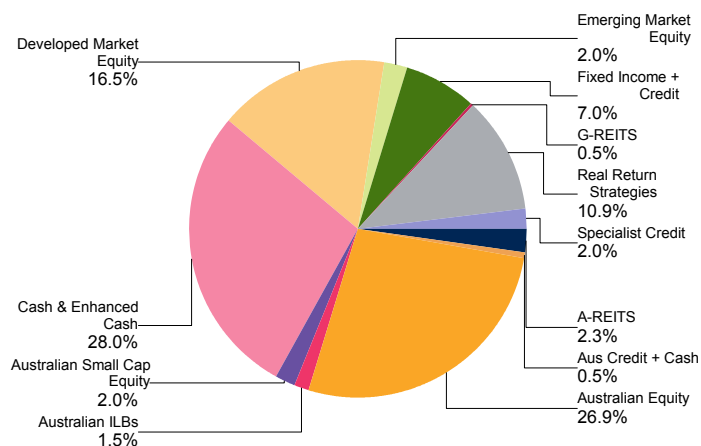
Management Fee: 1.04% p.a.

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: Five years or longer

PORTFOLIO SECTORS



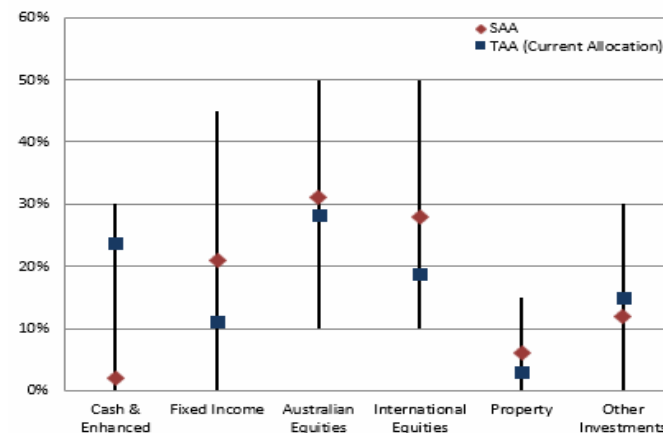
NET PERFORMANCE- periods ending 30 September 2022

	Fund	Benchmark	Excess
1 month	-2.1	-4.9	2.8
3 months	0.8	-1.1	1.8
FYTD	0.8	-1.1	1.8
1 year	-1.0	-10.6	9.6
2 year p.a.	10.6	3.3	7.3
3 year p.a.	5.6	1.7	3.9
5 year p.a.	6.4	5.2	1.2
10 year p.a.	7.9	7.4	0.5
Since incep.	7.2	6.7	0.5

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

ASSET ALLOCATIONS AND INVESTIBLE RANGES

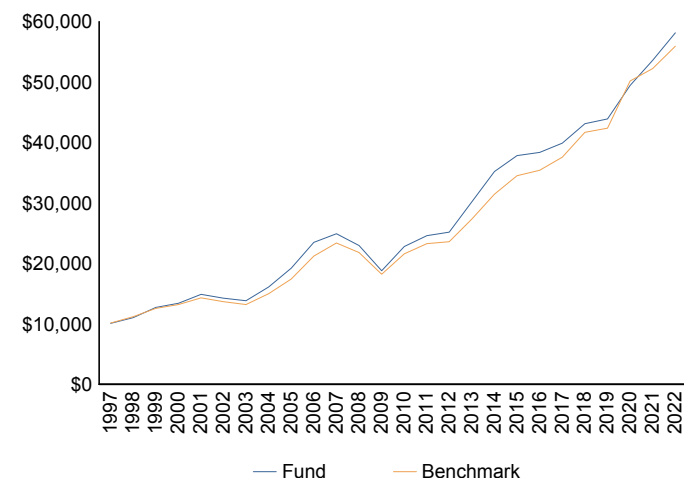
FUND TACTICAL AND STRATEGIC ALLOCATIONS INCLUDING ALLOWABLE MAXIMUM AND MINIMUM RANGES



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

Global financial markets saw elevated volatility over the September quarter as a strong rally gave way to a sharp selloff predicated on hawkish central bank rhetoric and elevated global recession risk.

- US equities (-4.9%) gave back all their gains made in the June-July rally with September being the worst month for US stocks since the start of the pandemic.
- Australian equities (+0.4%) outperformed global peers, supported by robust corporate profit results, a lower currency and a less hawkish central banks.
- Emerging market equities (-8.0%) underperformed, led by China (-21.6%) which was impacted by moderating global demand, strict COVID protocols and the worsening property crisis.
- European equities (-3.7%) fell as the energy crisis intensified, while UK equities (-1.1%) were resilient despite turmoil in British bond and currency markets.
- Developed market bond yields rose substantially as monetary policy expectations were recalibrated yet again, giving back all their gains since June. Benchmark 10-year yields in the US rose by 82 bps, Australia by 23 bps and the UK soared 143 bps as a result of an unfunded fiscal expansion by the new British government.
- The US dollar powered to 20 year highs against a number of global peers on recession concerns and aggressive monetary policy tightening.

We maintain our view of the key pressures currently weighing on the market outlook.

- Even though equity valuations have improved this year, they remain expensive on many metrics.
- The transformation of the monetary policy outlook has caused a nasty bear market in government bonds and much tighter liquidity conditions.
- A slowdown in economic growth with elevated recession risks in the US and Asia and acute recession risk in Europe contributing to a likely sharp slowdown in profit growth.
- Growing geo-political risks in Europe due to the Russia/Ukraine war and in Asia reflecting a much more assertive China and heightened tensions over Taiwan's future.

The US Federal Reserve (the Fed) has a far more challenging task to bring inflation under control while avoiding recession. The Fed's tightening cycle thus far has been the most aggressive in 40 years. Alongside rising rates, financial conditions are set for further tightening in the months ahead as the Fed accelerates the reduction of its balance sheet by selling treasuries and some of its mortgage back securities. Recession indicators mounted during the September quarter with the US yield curve inverting between the 2 and 10 year tenors. At the same time, July saw the confirmation of a technical recession in the US with two successive quarters of marginally negative GDP growth, although private sector demand remained solid, with the consecutive contractions driven by small parts of the economy such as net exports and inventories.

With the US inflation driver switching from higher commodity prices to tight labour markets, the US Fed has refocused its strategy putting employment at the core of their plan to reduce inflation. Notwithstanding slight reduction in payrolls over the quarter, the labour market remains very tight relative to pre COVID levels. At quarter end, the unemployment rate of 3.5% was within striking distance of the lowest level in 50 years.

Thus far, central bank rhetoric and action has been determinative for asset valuations while having less impact on employment and demand. Hawkish commentary from Fed Chair Jerome Powell at the annual Jackson Hole Economic symposium during the quarter precipitated a sharp fall in equity valuations. Powell seemingly ruled out a short-term pivot of Fed policy given the inflation backdrop and warned of "some pain" while maintaining the aggressive monetary policy tightening which roiled markets in the first half of 2022. Financial markets are also proving very

sensitive to shifts in the economic outlook through the prism of the implications for interest rates. Stronger than expected August PMI data saw risk assets selloff sharply as the market priced in a more aggressive Fed.

We remain concerned about the outlook for economic growth and profits. The leading indicators suggest that recession risks remain elevated as the Fed attempts to get inflation back under control. But monetary policy operates with long and variable lags and the tightening cycle has a long way to play out. As a result, tighter financial conditions will continue to be required, implying higher bond yields and credit spreads and weaker equity markets and a continuation of the strength in the US Dollar. The combination of tightening financial conditions and slowing or negative growth also highlights the risk of zombie companies; heavily leveraged unprofitable firms that have only survived due to the incredibly low interest rates over the past decade.

While we highlight the actions of the Fed as the most crucial determinant of the market outlook, other major central banks have also embarked on aggressive tightening programs. The European Central Bank (ECB) raised interest rates by 125bps during the September quarter, representing the first increase in 11 years. Meanwhile, the likelihood of a deep European recession continues to increase against a backdrop of an ongoing energy crisis. The ECB faces a diabolical predicament, and the risk of policy error is high as the bank wrestles with the prospect of double-digit inflation, an energy crisis and a sharply slowing economy. Meanwhile, UK financial markets were in turmoil during September. Following a change in leadership, the British government embarked on an unfunded fiscal expansion which saw UK GILTs selloff dramatically. Sterling also plummeted which forced the Bank of England to temporarily cease its policy tightening to buttress the broader financial system.

Meanwhile, the Reserve Bank of Australia (RBA) continued its aggressive tightening cycle, having increased the target cash rate by 250bps between May and early October. Inflation remains the key concern for the RBA with trimmed mean inflation – the RBA's preferred measure – rising to 4.9% yoy in the June quarter, remaining well outside the target range (of 2 to 3%). While surging inflation will provide little comfort to the central bank, the print came in short of estimates and saw monetary policy tightening expectations wound back somewhat as a result. The RBA has a somewhat more favourable predicament – relative to the US and Europe – as inflation and wages growth are lower. The RBA also has a more powerful mechanism to address household spending as a result of highly leveraged household balance sheets which have greater sensitivity to policy rates given the prevalence of variable rate mortgages. While the Australian economy looks robust thus far, the RBA also has a delicate balance to maintain.

Through another challenging quarter for financial markets, the Fund continued to perform well. The Fund's defensive positioning significantly contributed to outperformance as financial markets struggled across equity bonds and credit.

The Fund's underweight equity exposure continues to mitigate the impact of falling equity markets. Net exposure to global equities was further reduced over the quarter as a result of adding put options on European and US equities. The Fund's direct downside protection positions performed well with global equity put options contributing substantially to outperformance. At quarter end, the Fund was underweight across global and Australian equities. All equity exposures retain their long-standing quality and value bias which are expected to continue to outperform against a backdrop of rising interest rates. Stock selection within Australian equities contributed to outperformance during the quarter.

The Fund's underweight allocation to property contributed to outperformance as Real Estate Investment Trusts (REITs) underperformed across global and Australian markets.

The underweight positioning of the Fund's fixed income allocations continues to contribute to outperformance as bond yields rose and credit spreads widened during the quarter. During the quarter, the Fund's US and Australian duration was increased while remaining underweight and short of benchmark duration. This was partially offset by the addition of a small short (negative) position in Japanese bonds. The Fund maintains a corresponding overweight cash position which continues to mitigate the impact of rising yields. The Fund maintains a significant foreign exchange exposure, diversified across a number of developed and emerging market currencies. The Fund's USD exposure contributed significantly to outperformance both via direct exposure and a USDCNH call option which performed well as the USD appreciated against all major currencies over the quarter.

The Fund's exposure to sources of uncorrelated returns were constructive during the quarter as major equity and bond markets fell. 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

Tightening financial conditions, very high inflation and slowing economic growth are a challenging environment for investors to navigate. High equity valuations were only supported while bond yields stayed low as inflation was contained. Equity valuations have adjusted (although there could be more to come), but now profit expectations need to be lowered to more closely aligned with the economic backdrop. In this climate the fund remains well positioned to navigate the tightening cycle and retains the capacity to add risk as valuations become more attractive.

The Balanced 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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