Wholesale Funds

PERPETUAL WHOLESALE BALANCED GROWTH FUND

August 2021

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 consideredbefore 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

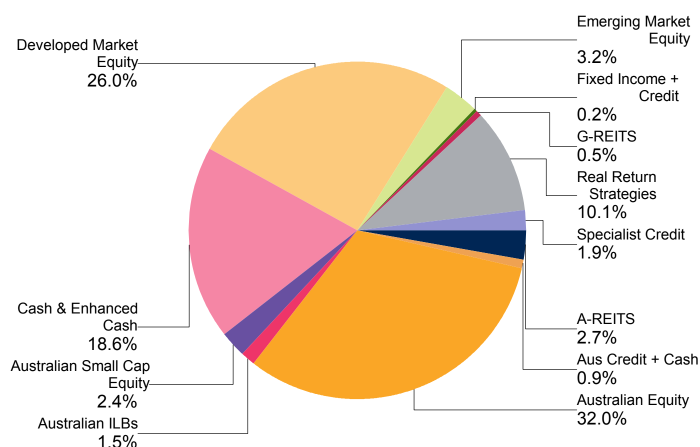
Management Fee: 1.04% p.a.

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



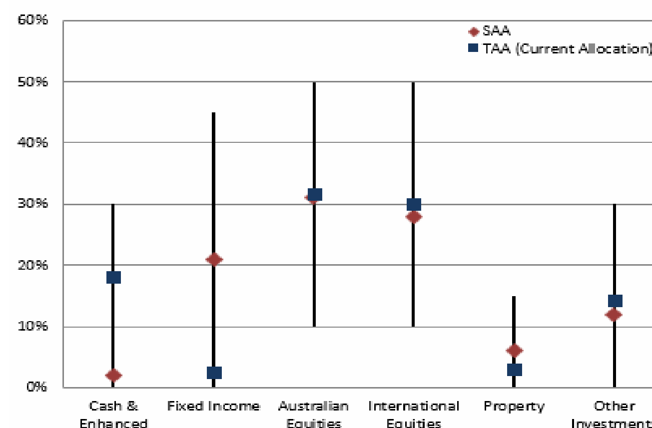
NET PERFORMANCE- periods ending 31 August 2021

	Fund	Benchmark	Excess
1 month	2.0	1.9	0.1
3 months	3.5	6.1	-2.7
FYTD	2.2	3.8	-1.6
1 year	23.5	20.3	3.2
2 year p.a.	10.1	10.4	-0.3
3 year p.a.	8.4	9.6	-1.2
5 year p.a.	8.0	9.8	-1.8
10 year p.a.	9.2	9.8	-0.6
Since incep.	7.6	7.6	0.0

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

ASSET ALLOCATIONS AND INVESTIBLE RANGES

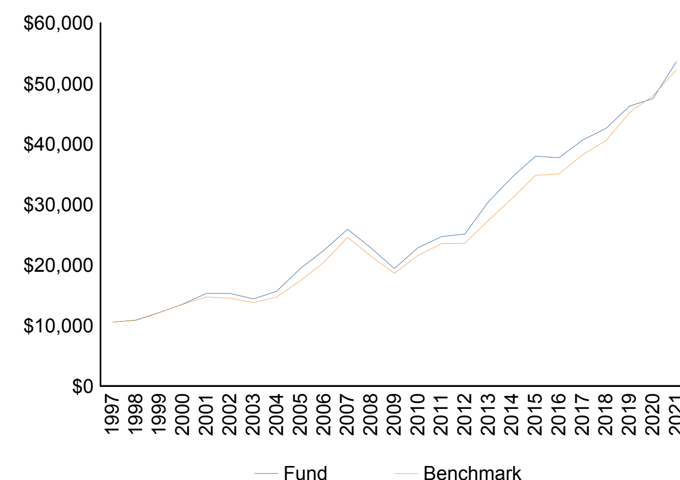
FUND TACTICAL AND STRATEGIC ALLOCATIONS INCLUDING ALLOWABLE MAXIMUM AND MINIMUM RANGES



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 economic growth expectations continued to be revised down in August as the highly contagious delta variant spreads – most notably in the US and UK. While growth is still expected to be extraordinarily strong through the second half of 2021, it has peaked and will slow significantly in the next year. In the near term, the recovery in the services sector has been restrained by the spread of the delta variant and the manufacturing sector continues to be affected by supply chain disruptions caused by the pandemic. In the medium term, the re-opening spur to growth will be over and fiscal policy will become progressively less stimulative.

At the same time, inflation should moderate. High inflation prints in the US over recent months have been largely attributed to supply chain disruptions and accordingly identified as 'transitory'. Core inflation is expected to subside from recent levels back towards 2% next year as some of these 'one-offs' reverse. This would be consistent with the US Federal Reserve (the Fed) achieving their objective of getting inflation up to 2% or higher on a sustained basis. Of course, there is also a risk that core inflation settles closer to 3% which would be very uncomfortable for the Fed, and therefore financial markets, with the prospect of significantly higher interest rates.

There remains a dichotomy between economies with higher levels of vaccinations and/or natural immunity and those with lower levels. With high rates of vaccination and natural immunity, the UK and Europe (and to a lesser extent, the US) have demonstrably broken the nexus between infections and hospitalisations. This will be tested further through the northern hemisphere winter. Conversely, economies with low natural immunity and low vaccinations rates (Australia) or questionable vaccine efficacy (China and many other emerging economies) are more exposed to disruption. The reduced risk of serious infection has allowed the reopening of European economies to continue despite the increasing case numbers. With the benefits of reopening still to be fully realised, Europe and the UK are the regions with the most promising growth outlook.

Conversely, the most dramatic downgrades in growth expectations were seen in China, Australia and New Zealand. Economic activity in China remains highly levered to the path of the virus as the zero-tolerance strategy ensures that strict lockdowns remain a threat. Chinese service sector purchasing manager index plunged below 50 (into contraction), reaching levels last seen in February 2020 while manufacturing slowed for the fifth successive month. In addition, the prospect of more structural reforms and potential stress in Chinese debt markets continues to impact growth expectations and investor confidence.

The outlook for Australia is delicately poised given the combination of a highly contagious variant and low (but rapidly increasing) levels of vaccination. The National Accounts show the economy was slowing before the full impact of the lockdowns and a substantial fall in activity in the September quarter is inevitable. More recently, the Covid zero strategy has been abandoned by NSW and Victoria. As a result, this re-opening is going to be very different to what happened in the second half of last year. Added to that commodity prices, including iron ore, are now falling precipitously (from extraordinarily high levels) due to the slowdown in the commodity intensive sectors of China.

As a result, ongoing fiscal support in Australia will be crucial to the path of recovery. In the lead up to next year's Federal election there is little doubt that further stimulus is in prospect which is likely to underpin a robust recovery. There remains however, an unusual amount of uncertainty about the outlook.Notwithstanding falling economic growth expectations, equity markets continue to perform very well reflecting a number of factors:

• Earnings remain extraordinarily strong in all key regions – the US, Europe and Asia;
• Monetary policy settings are extremely accommodative globally with central banks indicating that stimulus will only be withdrawn very slowly over coming years; and
• In part due to central bank policies, bond yields remain close to all-time record lows. Against this backdrop, equities have become the yield of last resort.

One exception has been Chinese equities which continue to under-perform. Credit growth has been slowing for many months in response to a tightening of policy which is creating stress in the highly levered parts of the economy, including a liquidity crisis faced by property developer, China Evergrande. Alongside the economic slowdown, Chinese equities are pricing in an increasing regulatory risk following the clamp down on the technology and education sectors in July.

Much of the stunning rally in risk assets over the past 18 months has been fuelled by abundant liquidity which has underpinned high investor risk appetites. With the recovery fully priced into markets, any upward shift to interest rates could negatively impact equity market valuations. While the global economic recovery is now well established, there has been very little change so far in the guidance for monetary policy from the key central banks (the Fed, the European Central Bank and the Bank of Japan). The Fed now appears likely to begin tapering late this year. Nonetheless, the strongest year of economic growth in many decades and a series of upside inflation surprises sits very awkwardly with current policy settings.

While the actions of central banks shapes to be the most significant factor in financial market performance over the coming months, as always there are also a number of tail risks. Failure of the vaccination rollout to curb the spread and public health impact of the delta variant or the emergence of a subsequent strain remains a key risk. During the month, we were also reminded of heightened geopolitical risks by the US's messy withdrawal from Afghanistan. While not consequential for markets during the month, the geopolitical climate (most notably, the US's strained relationship with China) remains a critical risk for the future market outlook.

Equity exposures drove absolute return during August. Developed market equities continued to rise supported by strong earnings results. The Fund's equity exposures performed broadly in line with the benchmark. Stock selection in Australian equities contributed to relative performance but was offset by global equity stock selection which detracted.

The Fund is around benchmark weight in global and Australian equities. All equity exposures retain their long-standing quality and value bias which significantly contributes to the defensive attributes of the Fund. This style positioning is complemented by elevated exposure to UK and European equities which we believe offer good relative value. The Fund also holds reduced exposure to areas of the market where valuations are most extended. This includes put spreads on the S&P 500 and the US technology heavy Nasdaq.

The Fund retains its very low allocation to fixed income and credit. The Fund has substantial foreign exchange exposure diversified across a number of developed and emerging market currencies. Finally, 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

The extraordinary monetary and fiscal policy response to the COVID-19 crisis has been very successful in minimising the damage of a massive shock to the global economy. The policy response has also had a pervasive impact on the valuation and outlook for many key markets. The massive monetary expansion led by the US Federal Reserve has limited the attractiveness of defensive assets including government bonds. In addition, credit markets are distorted with spreads much tighter than would be indicated by the state of the economy and the risk of default. Finally, extraordinarily low interest rates are intensifying the hunt for yield and contributing to very expensive equity valuations. In this climate the fund remains well positioned to benefit from the continued economic recovery, while maintaining a defensive profile through its value and quality biases in equity exposures and allocation to sources of uncorrelated returns.

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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