

From partying hard to doing the hard yards

By Vivek Prabhu

19 August 2021



Market returns across most asset classes have been supercharged since the lows of March 2020, spurred by accommodative monetary policy, stimulatory fiscal policy and an improving global economic outlook as the COVID vaccine rollout gathers pace. What has this all meant for Perpetual's Diversified Income Fund?

The COVID-induced market volatility played to our strengths as an active manager. In Perpetual's Diversified Income Fund, this active management included:

- Positioning the fund defensively (pre-COVID), by rotating out of BBB rated (bottom of the investment grade spectrum) securities into predominantly (over 50%) AAA rated (top of the investment grade spectrum) securities, the highest AAA exposure in the fund's 15-year history;
- Taking advantage of the repricing of risk post-COVID and using the large firepower available (from the high AAA exposure) to rotate back into BBB rated securities, which were now more attractively priced, including exposures to long-dated banks, financials and corporates; and
- Over the last 12 months, taking profit on many of these BBB rated exposures and returning the portfolio to a more defensive posture once again (by increasing the allocation to AAA rated securities) as credit spreads contracted to historical lows.

Our active management generated strong performance for investors in the Diversified Income Fund, with the fund achieving its highest rolling 12-month net returns (8.85% in March 2021) in almost a decade (since May 2011). This was a particularly strong result considering that the current RBA cash rate is just 0.10%, compared to 4.75% a decade ago when fund returns were last this strong. Consequently, fund distributions for FY21 were also the healthiest in seven years (since FY14) at just over 4%.

Whilst the credit fundamentals (low interest rates, an improving global economic outlook and strong technicals) remain supportive, many credit premiums are at historic lows (below pre-COVID levels and in some cases below pre-GFC levels), making it prudent to return the portfolio to a more defensive posture, albeit remaining fully invested. So, whilst investors have enjoyed partying hard with the supercharged returns of the last 12 months, we believe that return prospects for the coming year will be more modest. There still remains scope to generate returns commensurate with the fund's performance objective (bank bills plus 2% p.a. before fees). With a strong focus on investor outcomes, we believe the Diversified Income Fund has been a consistent and reliable performer through many market cycles, over the short, medium and long-term, comfortably exceeding its return objective over the last decade.

With credit yield premiums now at historic lows, the margin for error has reduced and investors will once again need to do the hard yards. In this environment, investors will need to be much more discerning and active management will be more important than ever to generate return whilst managing downside risk.

Perpetual's active management style positions us strongly to navigate this investment landscape.

[Read the full newsletter.](#)

Find out more about Perpetual's Diversified Income Fund.

This information has been prepared by Perpetual Investment Management Limited (PIML) ABN 18 000 866 535, AFSL 234426. It is general information only and is not intended to provide you with financial advice or take into account your objectives, financial situation or needs. You should consider, with a financial adviser, whether the information is suitable for your circumstances. To the extent permitted by law, no liability is accepted for any loss or damage as a result of any reliance on this information.

The information is believed to be accurate at the time of compilation and is provided in good faith. This document may contain information contributed by third parties. PIML does not warrant the accuracy or completeness of any information contributed by a third party. Any views expressed in this document are opinions of the author at the time of writing and do not constitute a recommendation to act. Any views expressed in this document are opinions of the author at the time of writing and do not constitute a recommendation to act. This information, including any assumptions and conclusions is not intended to be a comprehensive statement of relevant practise or law that is often complex and can change.

The product disclosure statement (PDS) for the relevant Fund, issued by PIML, should be considered before deciding whether to acquire or hold units in the fund. The PDS and Target Market Determination can be obtained by calling 1800 022 033 or visiting our website www.perpetual.com.au. No company in the Perpetual Group (Perpetual Limited ABN 86 000 431 827 and its subsidiaries) guarantees the performance of any fund or the return of an investor's capital. Past performance is not indicative of future performance.