Perpetual Investments

ANNUAL UPDATE

Welcome to your annual update from Perpetual, which covers:

- **An overview of how investment markets have performed over the past 12 months**
- **Insights from our investment experts about what to expect in the year ahead**
- **Answers to some frequently asked questions around end of financial year**

Additionally, if you'd like more information about how your account has performed or need help understanding your statement, please speak to your financial adviser or contact our Investor Services team on 1800 022 033.

HOW ARE WE INVESTING YOUR MONEY IN TODAY'S CLIMATE?

We are now nine years into a market environment in which share prices have risen, encouraging investors to buy. This is commonly referred to as a 'bull' market.

From the lows of 2009 amid the Global Financial Crisis (GFC) to today, equity markets have risen 195.6% globally; equivalent to an annual rate of return of 12.4%*. Many would agree that such rates of return may not be sustainable over the long term.

Over this same period interest rates have remained extremely low, and companies and individuals alike have taken advantage of readily available credit to take on more debt.

This is not the first 'bull' market cycle Perpetual has seen, nor will it be the last. And although history doesn't repeat, in investing, it often rhymes. One thing we have learned in more than 50 years of investing money for clients is that as surely as cycles begin, at some point, they always come to an end.

Our role as your investment experts is not to just invest for the good times but more importantly position for down times. Our conservative attitude towards managing your money and our ability to remain true to our core value management style has helped us navigate the markets' many ups and downs.

Our investment process has been part of Perpetual's culture since our flagship fund, the Perpetual Industrial Share Fund, first opened to investors in August 1966. It's a process that has been proven time and time again, through multiple market cycles.

In this environment, as the stewards of your financial future, we stand by a number of important principles, outlined here:

BE DISCIPLINED

We have successfully applied the same investment approach for decades, rigidly adhering to our tried and tested investment process. Rather than reacting to market hype, our experienced team focuses on being patient, staying liquid and moving quickly when we identify opportunities. And just as importantly, maintaining that discipline in selling investments when we believe the price of that asset has outstripped its earnings potential.

VALUATIONS MATTER

We believe that the price you pay for an asset today can have the largest impact on the success you might derive from that investment in the future. This value-based approach to managing money has helped us to grow wealth and minimise the downside for our investors over generations.

THERE IS NO SUBSTITUTE FOR QUALITY

Our investment teams have an unwavering focus on unearthing hidden pockets of quality investments that are unloved or underappreciated by the market, and then taking advantage of those opportunities to deliver across the wide range of investments we manage on your behalf.

BE ACTIVE

Rather than investing in an asset and then sitting back to see what will happen, our active management approach means we constantly apply our expertise, skill and judgement to actively buy, and sell, across the full spectrum of investments to help deliver the best outcome for our clients.

Irrespective of whether you invest with Perpetual for your investments, superannuation or pension, we thank you for entrusting us to help manage your financial future.

*As measured by MSCI World Net Total Return Index (31 March 2009 to 30 June 2018).

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2017/18 FINANCIAL YEAR AT A GLANCE

AUSTRALIAN SHARES – 13.2%

The Australian sharemarket, as measured by the S&P/ASX 300 Accumulation Index, rose 13.2% over the financial year.

GLOBAL SHARES – 15.3%

The global sharemarket, as measured by the MSCI World Index, rose 15.3% to 30 June 2018.

INFLATION – 1.9%

The inflation rate remained stable this year, with the rate of growth a steady 1.9% to the end of March 2018.

INTEREST RATE – 1.5%

Interest rates remained at low levels this financial year, with the Reserve Bank Cash Rate steady at 1.5% to 30 June 2018.

CREDIT SPREADS – 80.5bps

Credit spreads tightened this year, ending at a rate of 80.5 basis points to the end of the financial year.

INVESTMENT MANAGER VIEWPOINT

We asked Perpetual's experts what's in store for the coming year and where they are seeing challenges and opportunities for investors.

PAUL SKAMVOUGERAS
Head of Equities

The S&P/ASX 300 Accumulation Index trended higher over the financial year ending the period up 13.2%. Rising commodity prices, symptomatic of a maturing economic cycle, benefitted the resource sector which was among the best performing areas of the market. Industrials ex-financials continued to trade at historically elevated levels whilst the banking sector remained in the spotlight for much of the financial year owing to the government's decision to undertake a Royal Commission. Interestingly, we observed a shift in the behaviour of the banks following the many revelations of the Royal Commission and looking forward, we remain keen observers of the future of vertical integration in wealth management. Our value investment style has struggled in the current investment climate where a low interest rate setting has resulted in an underappreciation of market risks. Companies with strong balance sheets are being overlooked and little consideration is being given to the price paid for securities. At Perpetual, we recognise the importance of valuation in determining future returns and understand that it is fundamentals, not headlines which drive share prices in the long term. The Perpetual investment process and philosophy delivers a portfolio of well researched, differentiated ideas versus the "herd". Importantly, we are maintaining the investment process, philosophy and discipline over the long term and continue to search for investment opportunities in high quality companies that are out of favour or facing short-term earnings headwinds.

MICHAEL KORBER
Head of Credit

Following another financial year of strong performance for Perpetual's suite of cash and fixed income funds, our overall outlook for corporate credit has shifted to neutral.

Our valuation indicators are benign as corporate spreads now trade tight relative to their long-term averages across major credit markets. We continue to actively seek out and buy attractively priced securities on a relative valuation basis.

The macroeconomic outlook remains supportive of credit spread tightening. The improvement in US, European and Asian developed country economic data augment this positive view. Supply and demand dynamics are also supportive of the credit outlook with elevated market cash levels seeking out our new issuance for reinvestment.

Broader market technicals remain generally positive although any future spikes in market volatility may temper positive technical dynamics.

Near term risks include uncertainty around rising interest rates, inflation and the pace of unwind of Quantitative Easing by both the US Federal Reserve and the European Central Bank.

Should market volatility in credit markets increase in the coming year, we have the ability to take advantage of attractively priced and appropriately risked opportunities that may arise. Through stringent research and careful diversification, we remain poised to take advantage of securities offering superior income with less risk than many other assets.

MICHAEL O'DEA
Head of Multi Asset

The global economy has grown at a robust pace in the past year led by the two biggest economies, China and the US. This is boosting profits globally (most notably in the US where the company tax rate has been cut as well), yet there is a tension between the strength of this economic growth, how much has been priced in by the market, and the reduction of monetary support (higher interest rates).

Extraordinarily low interest rates over the past decade have spurred what is now the second longest bull market in the US, but rising interest rates are often responsible for ending the cycle. Of course, central banks are very aware of this risk, but 'taking away the punch bowl' at the right time is an imprecise science. Too soon and the economy will slow, possibly abruptly. Too late and the economy could experience higher inflation which could scare bond investors. Investors should invest in well-diversified portfolios, rather than assume that policy makers will be able to engineer it precisely.

Over the long term, Australia's economy gives us a lot to be optimistic about. Government debt is low, our floating currency helps our economy adjust to shocks, we have strong trade links with the growing markets of Asia, and we enjoy very high asset prices which underpin consumer confidence. However, asset prices are variable and household debt is fixed (i.e. debt must be paid off even if house prices fall), so it is worth considering the risks to the economy of record high household debt if house prices fall significantly.

Likewise, Australia's high trade and financial exposure to China has been a huge advantage as China's economy surged ahead. It now presents a challenge as the Chinese authorities continue their pursuit of reducing financial leverage.

The question at the centre of every investment decision we make is whether our clients will be adequately rewarded for the risk they are taking. Taking risk is important to generate returns which exceed that of the safety, and very low returns, from holding cash. Prices (or valuations) are currently high and markets go through cycles. Managing the late stages of an economic cycle is when diversification and risk management is critical. While the current market environment favours being selective, investment opportunities will be plentiful again at some point in the future. It pays to focus on "value" and investing in portfolios which are genuinely diversified.

GARRY LAURENCE
Global Equities Portfolio Manager

The financial year was dominated by ongoing changes to US policy settings as the Trump administration settled into office. On the one hand the revival in confidence, cemented by large tax cuts at the end of 2017, helped drive economic activity to new highs despite the longevity of the current business cycle and allowed the US Federal Reserve to lead other central banks into tightening policy. The good news on the economy was tempered by rising concerns about trade protectionism.

The revival in growth, combined with still low interest rates, saw growth stocks continue to outpace value stocks over much of the year. The continued dominance of a handful of large technology platforms meant that the tech sector delivered the best sectoral returns. Energy and Materials stocks benefited from the continued reflation theme in the global economy. The threat of rising interest rates caused yield proxy and leveraged sectors like Telecommunications, Consumer Staples and Utilities to underperform.

Looking forward, we continue to search for quality businesses with solid balance sheets at reasonable valuations, which are often temporarily mispriced by the market due to short-term news. Our quality value style has performed relatively well despite the challenging environment of ultra loose monetary and fiscal settings, but we believe it will do even better as we edge closer to the mature end of the business cycle in which value investing performs best. In the meantime, we remain invested in a suite of high quality businesses at a discount to market valuation multiples.

YOUR KEY QUESTIONS ANSWERED

It's important you understand your investment and how we are performing for you, so Perpetual welcomes the contact we receive from investors every year. Here are some of the most commonly asked questions around the end of the financial year.

WHY DID THE UNIT PRICE OF MY FUND GO DOWN AFTER 30 JUNE?

The unit price of a fund reflects the value of a fund's investments, including any income that has been accrued but not yet distributed. When distributions are paid, the unit price of a fund will usually decrease by an amount equal to the distribution. As a result, if your fund pays a distribution on 30 June, for example, the unit price will generally decrease on the same day by the same amount.

WHAT DOES 'DISTRIBUTIONS AWAITING REINVESTMENT' MEAN ON MY STATEMENT?

Many of our clients choose to reinvest their distributions in order to grow their investment – it has been a proven strategy. Any distributions that will be reinvested are referred to as a 'distribution awaiting reinvestment'. For example, if you receive a distribution for the period ending 30 June 2018 that you intend to reinvest, that amount is referred to as the 'distribution awaiting reinvestment' on 1 July 2018. Once all processing has been completed this will appear as 'distribution reinvested'. On your annual statement for the 2017/18 financial year, the reinvestment amount will be incorporated into the opening balance and will not appear as a separate transaction.

WHERE CAN I FIND THE FEES I PAY ON MY ACCOUNT?

It's important that fees are transparent and that you understand what you are paying. The fees you are charged will be shown in a dollar amount on your annual statement. They can also be found in the current Product Disclosure Statement (PDS) or Offer document, available on the 'Forms, PDSs and Offer Documents' section of our website at: www.perpetual.com.au/Resources-and-documents

MY STATEMENT REFERS TO 'ATTRIBUTION MANAGED INVESTMENT TRUST (AMIT)'. WHAT DOES THIS MEAN?

Perpetual elected into the Attribution Managed Investment Trust (AMIT) regime for the majority of Perpetual's investment funds for 2017/18 and subsequent years. Each fund that has elected into the AMIT regime is now referred to as an AMIT. No change has been made to the way in which distributions for the 2017/18 year have been paid to you.

HOW CAN I UPDATE MY CONTACT DETAILS?

If you already have online account access, then simply log in to provide us with your updated contact details.

Otherwise, call us on 1800 022 033 and we'll change your details over the phone.

MORE INFORMATION

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

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