Perpetual Asset Management Australia

# INSTITUTIONAL UPDATE

July 2024

## AUSTRALIAN EQUITIES STRATEGIES

The S&P/ASX 300 rallied strongly in July, rising by 4.1%. The Australian market benefited from a global rotation favouring cyclicals over technology. This shift saw Financials soar by 6.25%, contributing nearly half of the benchmark return. The Consumer Discretionary and Real Estate sectors were also significant contributors, along with healthcare. The backdrop was reasonably benign, with strong domestic employment growth and high hopes for a soft landing in the US. While concerns about high inflation persisted at month-end, a consensus quarterly inflation number alleviated fears of further rate hikes and boosted markets.

Markets finished July on a high note, but difficulties are emerging. A sudden deterioration in economic data in the US during the first week of August led to a sharp sell-off in US and other equity markets. This accelerated the rotation in equities that began in July and raised the spectre of a recession for the first time in months. Coinciding with this was the Bank of Japan's decision to raise interest rates to near generational highs, which appeared to trigger a reappraisal of asset allocation and a potential unwind of the multi-trillion-dollar Japanese "carry trades" that have been in place for many years. The Nikkei had its worst day since 1987, though it bounced back a day later. Nonetheless, the sharp correction in markets, with the NASDAQ repeatedly underperforming the Dow and S&P, increases the risk that a broader realignment could finally be here.

| Gross Performance | 1M% | 3M% | 6M% | 1Y% | 2Y% | 3Y% | 5Y% | 7Y% | 10Y% |
|---|---|---|---|---|---|---|---|---|---|
| Perpetual Australian Share Fund | 4.1 | 5.7 | 7.5 | 9.5 | 11.6 | 8.2 | 9.3 | 9.3 | 7.6 |
| S&P/ASX 300 Accumulation Index | 4.1 | 6.0 | 7.3 | 13.3 | 12.2 | 7.1 | 7.5 | 9.3 | 8.0 |
| Excess | 0.0 | -0.3 | +0.2 | -3.8 | -0.6 | +1.0 | +1.9 | +0.1 | -0.4 |
| Perpetual Concentrated Equity Fund | 3.7 | 6.0 | 8.9 | 11.6 | 12.6 | 10.2 | 9.3 | 9.4 | 8.1 |
| S&P/ASX 300 Accumulation Index | 4.1 | 6.0 | 7.3 | 13.3 | 12.2 | 7.1 | 7.5 | 9.3 | 8.0 |
| Excess | -0.4 | 0.0 | +1.6 | -1.6 | +0.4 | +3.1 | +1.9 | +0.1 | +0.1 |
| Perpetual ESG Australian Share Fund | 4.6 | 4.2 | 9.7 | 14.0 | 13.9 | 9.7 | 11.4 | 9.6 | 9.7 |
| S&P/ASX 300 Accumulation Index | 4.1 | 6.0 | 7.3 | 13.3 | 12.2 | 7.1 | 7.5 | 9.3 | 8.0 |
| Excess | +0.5 | -1.7 | +2.5 | +0.7 | +1.7 | +2.6 | +3.9 | +0.3 | +1.7 |
| Perpetual Pure Equity Alpha Fund – Class A | -0.4 | 0.7 | 5.4 | 7.7 | 9.0 | 9.3 | 10.6 | 9.2 | 8.9 |
| RBA Cash Rate Index | 0.4 | 1.1 | 2.2 | 4.4 | 3.8 | 2.6 | 1.7 | 1.6 | 1.7 |
| Excess | -0.8 | -0.4 | +3.2 | +3.3 | +5.2 | +6.7 | +8.9 | +7.6 | +7.1 |
| Perpetual Share-Plus Long-Short Fund | 2.4 | 3.7 | 7.3 | 13.6 | 14.6 | 11.8 | 11.7 | 11.1 | 10.1 |
| S&P/ASX 300 Accumulation Index | 4.1 | 6.0 | 7.3 | 13.3 | 12.2 | 7.1 | 7.5 | 9.3 | 8.0 |
| Excess | -1.7 | -2.3 | 0.0 | +0.3 | +2.5 | +4.7 | +4.3 | +1.8 | +2.0 |
| Perpetual Smaller Companies Fund | 2.8 | 1.7 | 6.7 | 6.4 | 8.3 | 6.5 | 11.2 | 10.6 | 10.6 |
| S&P/ASX Small Ordinaries Accumulation Index | 3.5 | 2.0 | 5.4 | 9.3 | 4.9 | -0.6 | 3.5 | 6.6 | 6.3 |
| Excess | -0.7 | -0.3 | +1.3 | -2.9 | +3.3 | +7.1 | +7.7 | +3.9 | +4.3 |
| Perpetual Strategic Capital Fund - Class S | 2.6 | 5.4 | 7.1 | - | - | - | - | - | - |
| S&P/ASX 300 Accumulation Index | 4.1 | 6.0 | 7.3 | - | - | - | - | - | - |
| Excess | -1.5 | -0.6 | -0.2 | - | - | - | - | - | - |

## GLOBAL EQUITIES STRATEGIES

During July, we saw enough daily headlines to last an entire year, especially in the U.S. Early in July we saw an attempted assassination attempt of the former President Donald Trump, the current U.S. President U.S. Joe Biden pushed off the Democrat ticket, and the ascension of his Vice President Kamala Harris to the ticket, thus altering the course of the election cycle in the U.S. Further, soft economic data in the U.S. regarding jobs and manufacturing output brought the word "recession" back into the realm of possibilities. Outside the U.S., we saw central banks in Canada, the UK, and other western-oriented central banks lowering rates while Japan raised rates. Finally, China has continued to garner headlines for the wrong reasons as the economy has failed to recover post COVID on the back of underwhelming stimulus by the government. This latter point may be somewhat forgivable as there has been a lot of rhetoric around tariffs and the fact that the U.S. Federal Reserve (the Fed) has continued to maintain tighter rates causing China to pause until there is greater clarity.

Despite the muted market returns in July, sentiment shift may be afoot, as we have seen material rotations over the last month. We note the large spread (+20%) between small cap stocks and the NASDAQ; as measured by the Russell 2000 Index small cap stocks were up more than 10% in the month. That said, this may not be sustained if economic concerns broaden, as small cap stocks are likely to be hurt in this scenario. Softening economic numbers and stagnant inflation over the last few months have all but guaranteed a rate cut by the Fed in September. This will come on the heels of other central banks that have already cut. However, the issue regarding cutting rates is less about who is cutting and when that first rate comes, but more about why rates are being cut. If the Fed and other central banks have to move quickly in cutting historically high rates as a result of softening economic growth versus sufficiently tame inflation, it will pull the soft-landing scenario off the table and we could continue to see a violent rotation away from high multiple stocks in favour of lower multiple stocks. This may be further aggravated if we do officially enter into a recession. The Fund has been tilted more to the defensive areas of the market over the last few years. This positioning, though challenging for performance over the last 12-18 months, has allowed the strategy to provide downside protection – not only in the rotating markets in July, but during August to date as we deal with markets continuing to stumble.

| Gross Performance | 1M% | 3M% | 6M% | 1Y% | 2Y% | 3Y% | 5Y% | 7Y% | 10Y% |
|---|---|---|---|---|---|---|---|---|---|
| Barrow Hanley Emerging Markets Fund | 0.2 | 0.6 | 6.3 | -1.9 | - | - | - | - | - |
| MSCI Emerging Markets Net Total Return (AUD) | 2.6 | 4.3 | 14.4 | 9.7 | - | - | - | - | - |
| Excess | -2.3 | -3.7 | -8.1 | -11.6 | - | - | - | - | - |
| Barrow Hanley Global Share Fund - Class A | 5.7 | 3.6 | 10.3 | 11.7 | 16.0 | 10.0 | 12.4 | 13.1 | - |
| MSCI World Net Total Return Index ($A) | 4.1 | 7.9 | 13.8 | 22.1 | 19.8 | 11.1 | 13.3 | 14.0 | - |
| Excess | +1.6 | -4.2 | -3.4 | -10.4 | -3.8 | -1.1 | -0.9 | -0.9 | - |

## CASH & FIXED INCOME STRATEGIES

Financial markets consolidated during July with global equities ending the month higher while bond yields fell. Markets were relatively subdued throughout July before below consensus expectations US non-Farm payroll data and the Bank of Japan's 31 July decision to increase interest rates precipitated a spike in volatility in the first days of August.

Domestic bond yields fell aligning with a broader global trend that saw bonds rally through July. 10-year Australian yields rallied 19bps while 10-year US yields led the way, falling 32bps. Slowing core inflation in the second quarter CPI print saw expectations of an August RBA rate increase ease. While inflation has been more subdued through the first half of 2024, there remains a long way back to the central banks target range, which is reflected in the hawkish pricing of potential rate cuts.

Domestic credit spreads consolidated during July tightening marginally. Euro denominated spreads also rallied slightly while USD spreads were close to flat during the month. Financial spreads outperformed corporates while trading in a tight range. Government adjacent spreads including semi-government and supranational spreads outperformed credit. While July was relatively subdued for credit markets, the first week of August saw a spike in spread volatility.

Primary issuance was mixed during July with a busy mid-month period bookended by a slow start and a late month calm as markets anticipated key economic data releases. A number of offshore financial issuers met strong demand including Toronto Dominion, Banco Santander, Cooperative Rabobank and Sumimoto Mitsui Banking Corporation. ANZ raised $1.9B in a fixed rate subordinated transaction which was heavily oversubscribed before moving wider after pricing. Westpac issued subordinated bonds, raising $1.5B early in July.

| Gross Performance | 1M% | 3M% | 6M% | 1Y% | 2Y% | 3Y% | 5Y% | 7Y% | 10Y% |
|---|---|---|---|---|---|---|---|---|---|
| Perpetual High Grade Floating Rate Fund | 0.5 | 1.7 | 3.4 | 6.8 | 6.0 | 3.8 | 3.1 | 3.2 | 3.2 |
| Bloomberg AusBond Bank Bill Index | 0.4 | 1.1 | 2.2 | 4.4 | 3.8 | 2.6 | 1.7 | 1.7 | 1.9 |
| Excess | +0.2 | +0.6 | +1.2 | +2.4 | +2.3 | +1.2 | +1.4 | +1.4 | +1.4 |
| Perpetual Credit Income Fund | 0.4 | 1.6 | 4.0 | 9.2 | 8.1 | 4.9 | 4.4 | 4.3 | 4.3 |
| Bloomberg AusBond Bank Bill Index | 0.4 | 1.1 | 2.2 | 4.4 | 3.8 | 2.6 | 1.7 | 1.7 | 1.9 |
| Excess | 0.0 | +0.5 | +1.8 | +4.8 | +4.3 | +2.3 | +2.7 | +2.5 | +2.4 |
| Perpetual Active Fixed Interest Fund | 1.7 | 3.3 | 2.6 | 6.9 | 3.6 | -1.1 | 0.5 | 2.4 | 3.2 |
| Bloomberg AusBond Composite Index | 1.5 | 2.7 | 1.5 | 4.7 | 1.5 | -2.2 | -0.5 | 1.5 | 2.3 |
| Excess | +0.2 | +0.6 | +1.2 | +2.3 | +2.1 | +1.0 | +1.0 | +0.9 | +0.9 |
| Perpetual ESG Credit Income Fund- Class A | 0.4 | 1.7 | 4.1 | 9.1 | 8.2 | 5.1 | 4.4 | - | - |
| Bloomberg AusBond Bank Bill Index | 0.4 | 1.1 | 2.2 | 4.4 | 3.8 | 2.6 | 1.7 | - | - |
| Excess | 0.0 | +0.6 | +1.9 | +4.8 | +4.5 | +2.5 | +2.7 | - | - |
| Perpetual Pure Credit Alpha Fund - Class W | 0.7 | 2.3 | 4.9 | 10.1 | 9.3 | 6.3 | 5.5 | 5.5 | 5.9 |
| RBA Cash Rate Index | 0.4 | 1.1 | 2.2 | 4.4 | 3.8 | 2.6 | 1.7 | 1.6 | 1.7 |
| Excess | +0.3 | +1.2 | +2.7 | +5.7 | +5.5 | +3.7 | +3.8 | +3.9 | +4.1 |

## MULTI-ASSET STRATEGIES

Financial markets consolidated during July with global equities ending the month higher while bond yields fell. Volatility was elevated reflecting a number of key economic and political developments.
- Developed market equities (+1.3%) rose during July, and there was a notable rotation towards value oriented sectors and securities, and typically defensive markets were well supported.
- Australian equities (+4.0%) recorded its strongest monthly rise this year and led the pace of regional sharemarkets gains as falling bond yields and easing inflation concerns were constructive, with subdued expectations for the upcoming reporting season providing corporates with potentially a low estimate to beat.
- UK stocks (+2.5%) also outperformed, supported by highly attractive valuations and improving economic expectations given a decisive result in the UK election early in the month. Meanwhile, a continued downdraft in headline and core inflation is providing the room for the Bank of England to potentially begin their easing cycle when the policy group meets in early August.
- US equities (+1.2%) performed in line with the broader developed market as tech heavy sectors including information technology consumer discretionary were weighed down by some underperformance by the so called Magnificent Seven, despite some robust earnings results. Small caps also outperformed during the month in response to modest positioning in this area of the market.
- European equities closed lower (-0.3%) as economic data disappointed and several ECB speakers expressed uncertainty about the number of rate cuts which had been factored into market prices for 2024.
- Japan equities (-1.2%) underperformed in response to a strengthening Yen after the Bank of Japan raised official interest rates for only the second time in 17 years. The hike was expected but guidance explicitly signalled further tightening would occur if economic and inflation developments are consistent with the July outlook.
- Emerging market equities (0.7%) rose but trailed the performance of developed markets, as waning economic prospects in China (-1.3%)

weighed on sentiment.
- Domestic bond yields fell in most maturities in most markets as falling core inflation trends, improved the prospect that central banks can begin their respective easing cycles. 10-year Australian yields declined -19bps whereas 10-year US yields fell -32bps.

US markets balanced a slowing economic growth outlook with increased expectations of near term central bank easing. Markets reacted well to softer than expected CPI early in July which strengthened expectations that the Fed would commence rate cutting soon. This was supported by continued softening growth data, culminating in a well below expectation employment print in the first few days of August. By month end, (and further solidified after the non-farm payrolls miss) markets had priced in a first Fed rate cut in September with expectations for almost four cuts brought forward into 2024.

he domestic economy remains a key battleground for the 2024 presidential election which saw a seismic shift during July as President Biden withdrew from the race, endorsing Vice President Harris whose strong early polling suggests the contest might be closer than had previously been assumed. The result of the election will be a crucial issue for markets given how reliant US economic growth has been on elevated fiscal expenditure in the years following the COVID-19 pandemic, with the FY24 fiscal deficit likely to be -6.5% of GDP which is highly expansionary and aligned with levels seen during previous economic downturns.

Meanwhile, European growth was steady at +0.3% in the June quarter of 2024 despite Germany posting a marginal contraction. The ECB held rates in place during July with Governor Lagarde stating that the decision on a further cut in September was data dependent. Leading activity indicators including the flash composite European PMI declined to stall speed in July, signalling that the economic recovery is lacking propulsion.

Elsewhere, the UK economy continued to strengthen from a low base, with the S&P UK Manufacturing PMI rising to a two year high of 52.1, which combined with the services gauge (52.5) suggests the UK economy should continue to expand in H2'23.

It remains hard to see a significant global growth acceleration this year, as the fiscal impulse is negative, restrictive monetary policy remains a headwind, credit growth is anaemic and employment growth is slowing. While trend growth is supportive for equities, a soft-landing with numerous rate cuts in both 2024 and 25 have already been priced into market expectations which increases the vulnerability to downside surprises from earnings, geopolitical shocks and any re-pricing in global fixed interest markets of central bank expectation.

| Gross Performance | 1M% | 3M% | 6M% | 1Y% | 2Y% | 3Y% | 5Y% | 7Y% | 10Y% |
|---|---|---|---|---|---|---|---|---|---|
| Perpetual Balanced Growth Fund | 3.2 | 3.8 | 6.2 | 9.6 | 8.9 | 6.9 | 7.9 | 8.3 | 7.7 |
| Balanced Growth Index | 3.1 | 5.6 | 7.8 | 13.0 | 10.4 | 5.0 | 6.6 | 7.8 | 7.6 |
| Excess | +0.1 | -1.8 | -1.6 | -3.4 | -1.5 | +1.9 | +1.4 | +0.5 | +0.1 |
| Perpetual Diversified Growth Fund | 2.7 | 3.4 | 5.1 | 8.5 | 7.0 | 5.2 | 6.1 | 6.7 | 6.4 |
| Moderate Growth Index | 2.6 | 4.7 | 6.0 | 10.6 | 8.0 | 3.3 | 4.7 | 6.1 | 6.1 |
| Excess | +0.1 | -1.3 | -0.9 | -2.1 | -1.0 | +1.9 | +1.4 | +0.7 | +0.3 |
| Perpetual Diversified Real Return Fund - Class W | 2.0 | 2.3 | 3.6 | 6.0 | 5.5 | 3.7 | 4.7 | 5.1 | 5.2 |
| Australian CPI +5% (Target Objective) | | | | | | | 9.0 | 8.4 | |
| | | | | | | | | | |
| Perpetual ESG Real Return Fund | 2.1 | 2.7 | 3.6 | 4.2 | 3.1 | 1.2 | | | |
| Australian CPI +5% (Target Objective) | | | | | | | - | - | |

## MORE INFORMATION

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* Due to CPI data being released by the Australian Bureau of Statistics later in the month after quarter end, CPI figures reported are lagged by one month.

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