PERENNIAL FIXED INTEREST

Perennial Cash Enhanced Trust

Monthly Report as at 30 April 2013

	Month %	Quarter %	FYTD %	1 Year %	2 Years % p.a.	3 Years % p.a.	5 Years % p.a.
Perennial Cash Enhanced Trust*	0.41	1.33	5.60	6.48	5.97	6.21	6.69
UBS Bank Bill Index	0.26	0.73	2.78	3.46	4.16	4.42	4.63
Value Added (Detracted)	**0.15**	**0.60**	**2.82**	**3.02**	**1.81**	**1.79**	**2.06**
Net Performance	0.39	1.25	5.35	6.18	5.68	5.92	6.40

* Gross Performance. **Past performance is not a reliable indicator of future performance.**

- Money market yields fell fairly sharply over the month of April, as the RBA left rates on hold and a number of key economic indicators came in weaker than expected.
- The Trust outperformed the Index return by 0.15% for the month, bringing the financial year to date outperformance to 2.82%.
- We continue to look for opportunities to lighten our overweight positions to the credit sector and switch out of assets that have rallied the most and no longer represent good value.

Performance

Money market yields fell fairly sharply over the month of April, as the Reserve Bank of Australia (RBA) left rates on hold and a number of key economic indicators came in weaker than expected including unemployment (full time jobs in particular). As a result markets priced in another easing taking the expected cash rate down to 2.5% by year end. Globally, economic data was not much better causing bonds to rally, yields lower, across short and longer term maturities. Credit markets on the other hand performed particularly well, as credit margins narrowed with investors chasing the additional yield on offer in this low yield environment. This assisted corporate floating rate notes (FRNs) to comfortably outperform bank bills.

The UBS Bank Bill Index (the Index) returned 0.26% over the month. The Perennial Cash Enhanced Trust (the Trust) returned 0.41% and continued its run of outperformance exceeding the Index return by 0.15%.

Interest rate management, including a short duration stance, which was extended during the month, detracted value given yields fell through the course of April. However, sector strategies again added meaningful value over the month. Major bank senior debt outperformed most other "like" securities. Other areas of note were the higher running yields achieved on prime AAA rated Australian residential mortgage back securities (RMBS) as well as some listed property trusts (LPTs) and infrastructure debt.

At month end, the weighted average yield of the Trust was 3.86%, as compared to the Index yield of 2.97%.

Perennial Cash Enhanced Trust

The Trust aims to provide a total return that exceeds the benchmark, UBS Bank Bill Index, over rolling three-year periods by 0.50% p.a. (before fees).

Portfolio Manager: Noel Murphy	**Risk Profile:** Low
Trust FUM (as at 30/04/13): AUD1.5 billion	**Income Distribution Frequency:** Quarterly
Team FUM (as at 30/04/13): AUD6.7 billion	**Minimum Initial Investment:** $100,000
Trust Inception date: August 2002	**APIR code:** IOF0111AU

Market Review

Yields ended the month lower on softer real economy and price data, with the resulting capital gains helping to boost fixed interest performance.

On the economic front, a rising unemployment rate, deterioration in business conditions and a benign inflation outlook, opened the door to further monetary easing. In the labour market, total employment fell 36,100 while the unemployment rate rose to 5.6%. Business conditions fell from -3 to -7 in the NAB Survey, with persistent currency strength a headwind. Both headline inflation and the average of the RBA's statistical measures, rose by 0.4% over the quarter. However, not all domestic data releases were weak, with building approvals and retail sales data for February much stronger than expected. Importantly, it is these sectors, together with the external sector, that the RBA are looking for to take up the slack as the mining

investment boom comes to an end over the next one to two years.

The short end of the curve responded to the data flow by bringing forward the timing of the next easing and increasing the amount of remaining easing in the current cycle from 25 to 50 basis points. At the very short end of the curve, three and six month bank bills rallied 19 and 25 basis points to end the month at 2.91% and 2.87%, respectively. Further along the curve, the yield on a three year government bond ended the month 28 basis points lower at 2.59%.

Bond yields also fell sharply at the longer end of the curve, with steps by the Bank of Japan to significantly expand its quantitative easing program enhancing the relative attractiveness of longer dated Australian government bonds. The yield on a ten year government bond ended the month 33 basis points lower at 3.09%. Given these moves, there was some further flattening in the spread between three and ten year government bonds, which narrowed by 5 basis points, to +50 basis points.

Credit markets again performed well over the month, as strong demand for yield remained a dominant theme among investors. Credit spreads narrowed as a result, with the Australian ITRAXX Index in 11 basis points to 110 basis points. Financials, including short and medium term major bank paper, performed particularly well. Primary issuance continued to be very well received by the market along with keen demand in the secondary market. Reflecting the cautious attitude of corporations, the overall level of new issuance remained relatively subdued.

Market Outlook

We suspect that the latest round of economic soundings has bought the RBA to the cusp of easing. The inflation data was soft, with persistent exchange rate strength dampening inflation in the tradeables sector. While there are tentative signs of recovery in the interest rate sensitive sectors of the economy, ongoing currency strength is making the required rebalancing task in the economy more difficult and in our view, further modest easing would help facilitate the transition.

That said, we do not see the case for a significant easing from here given that the economy has already started showing signs of responding to interest rates cuts and that fiscal policy will not be as tight going forward given that the path to a balanced budget is being pushed back. Furthermore, if the global economy recovers momentum later this year as the effects of tighter fiscal policies wane, market attention is likely to shift back to the implications of unwinding current quantitative easing programs. As we saw over March, such a reassessment is consistent with higher yields at the longer end of the curve. Against such a back drop, we also anticipate that the RBA will gradually begin removing monetary accommodation from 2014 onwards towards a more neutral setting. We continue to hold a strategic defensive duration bias and regard further rallies in yields from current levels as an opportunity to extend that position.

In a world where offshore central banks are forcing term structures lower, investors across the globe continue to search for yield and compress spreads in non-government debt. Our overweight allocation to corporate debt has benefited from this search yield as well as sound corporate fundamentals. Nevertheless, with investment grade spreads close to their tightest post GFC lows, we maintain our bias to trim our overall exposure to this sector. More generally we view the current level of spreads as being around “fair value” and expect future outperformance to be driven more by the higher income the sector offers as opposed to the capital gain that occurs as spreads tighten.

Investment Strategy

The following is a summary of the key strategies in the Trust.

Interest rates – at the end of the month, the duration position of the Trust was as follows.

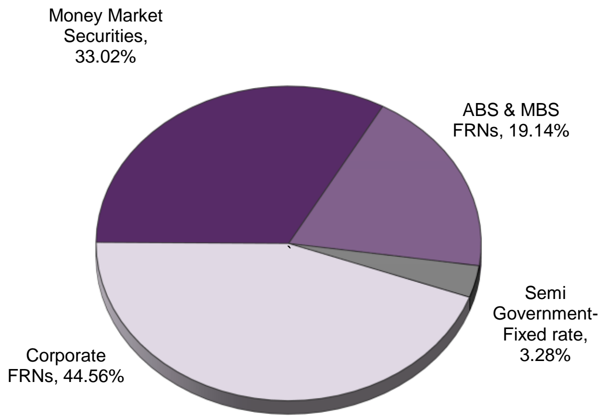
Modified Duration	Years
Trust	-0.20
Index	0.12
Active Position	-0.32

Interest rates – underweight duration:
As yields fell further through April, we increased the underweight duration stance to now about 0.3 years below the Index. Bond yields are now well below what we would consider ‘fair value’. While we can rationalise why bond yields have fallen so far, including quantitative easing offshore and foreign buying of Australian government bonds, it is very difficult to make a compelling case for why bonds are good value at current prices. In our assessment, the risks of bond yields rising are greater than falling meaningfully from these levels. Accordingly, we maintain a short duration stance fully appreciating that it may take some time for such strategies to deliver performance.

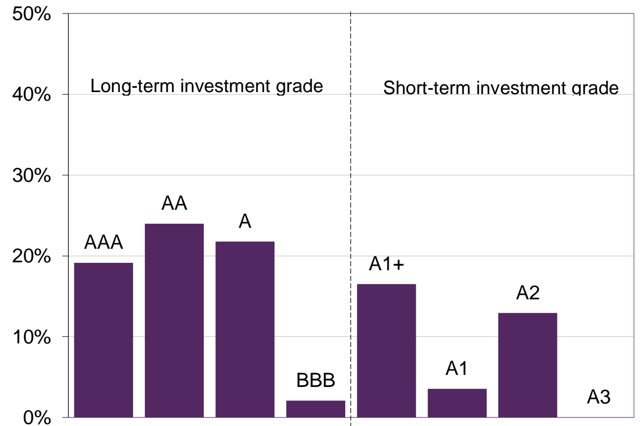
Corporate debt and asset backed securities – overweight:
We continue to look for opportunities to lighten our overweight positions to the credit sector and switch out of assets that have rallied the most and no longer represent good value. This is the case with short to medium term senior bank FRNs. Meanwhile, prime AAA rated Australian RMBS seem to offer better relative value and have been of greater interest to us. On average, these RMBS have a credit spread of about 85 basis points which is roughly double an equivalent term major bank senior FRN. Other sub-sectors we favour are senior debt of LPTs and infrastructure. Overall, we continue to run an overweight position to take advantage of the running yield advantage the sector has to offer.

Trust Snapshot

Sector Allocation



Credit Rating Distribution



Signatory of:

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