Perennial Australian Fixed Interest Trust

Monthly Report as at 28 February 2013

	Month %	Quarter %	FYTD %	1 Year %	2 Years % p.a.	3 Years % p.a.	5 Years % p.a.
Perennial Australian Fixed Interest Trust*	0.65	1.10	5.30	10.47	9.67	8.71	9.82
UBS Composite Bond Index (0+years)	0.59	0.55	2.57	8.18	8.99	7.82	8.22
Value Added (Detracted)	**0.06**	**0.55**	**2.73**	**2.29**	**0.68**	**0.89**	**1.60**
Net Performance	0.63	1.02	5.05	10.09	9.28	8.33	9.43

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

- The Trust outperformed the Index by 0.06% for the month and has exceeded the Index by 2.73% for the financial year to date.
- The Trust's overweight allocations to corporate debt and financial issuers, added value.
- Fixed interest return improved in February on the back of modest declines in yield.

Performance

Fixed interest returns improved in February on the back of modest decline in yields. In our view, this move is nothing more than a retracement in what we consider will be a difficult environment for bond markets over the next one to two years. As was the case during January, credit spreads were broadly stable, not surprising given the significant rally that occurred over the second half of 2012. We expect that this stabilisation in spreads will become the norm over the months ahead, supported by continued strong investor demand for quality yield in an otherwise low income environment.

The UBS Composite Index 0+ years (the Index) returned 0.59% taking its return for the current financial year to a meagre 2.57%. The Perennial Australian Fixed Interest Trust (the Trust) finished up 0.65% and outperformed the Index return by 0.06%. Financial year to date, the Trust's return is 5.30%, outperforming the Index by 2.73%.

Interest rate strategies, in the form of a short duration and curve steepening position, detracted marginally from performance. However this was more than offset by the value added from a combination of sector and security strategies. In regard to sector strategies, the Trust's overweight allocation to corporate debt was the key influence. At the security level, the overweight allocations to financial issuers, in particular Australian banks, and to AAA mortgage-backed securities added value.

Market Review

Bond yields trended higher over most of the month before rallying into the close on flight to quality flows resulting from an inconclusive outcome from the Italian election. The resultant modest fall in yields over the month resulted in some capital gain which helped boost fixed interest returns.

Perennial Australian Fixed Interest Trust:

The Trust aims to provide a total return (after fees) greater than cash and inflation, and that exceeds the UBS Composite Bond Index (0 + years), measured on a rolling three-year basis.

Portfolio Manager: Glenn Feben	**Risk Profile:** Medium
Trust FUM (as at 28/02/13): AUD1.3 billion	**Income Distribution Frequency:** Quarterly
Team FUM (as at 28/02/13): AUD6.4 billion	**Minimum Initial Investment:** $100,000
Trust Inception date: August 2002	**APIR code:** IOF0113AU

On the economic data front, releases were on the soft side and reinforced the picture of sluggish economic conditions late last year. Retail sales, building approvals and housing finance all fell over December. On the brighter side, consumer confidence bounced strongly in February and there was a small lift in business confidence in January, albeit off low levels. Perhaps the key release for the month was Q4 capital expenditure. The first look at the 2013/14 spend was $152.5 billion, which compared with a spend of $168 billion for 2012/13 suggests that business investment will modestly detract from growth over the coming financial year.

Against this backdrop, the three year government bond yield rose to a high of 2.94% before ending the month at 2.74%. Yields at the shorter end of the curve were little changed, with three and six month bank bills ending the month at 2.97% (up 2 basis points (bps)) and 2.93% (down 2 bps).

At the longer end of the yield curve, the ten year government bond yield rose to a high of 3.59% on stronger global risk appetite before the inconclusive Italian election result triggered flight to quality flows that helped the long bond end the month 10 bps lower at 3.35%. Given these moves, there was some minor flattening in the spread between three and ten year government bonds, which came in 2 bps, to +61 bps.

Credit markets finished the month 7 bps tighter with the iTraax index at 114 bps, thus continuing the strong start to 2013. The earnings season produced an overall positive set of results, particularly in the banking sector. Primary markets took a breather after an active January, but it did not stop the CBA and Westpac both raising over $2 billion by issuing residential mortgage backed securities into the domestic primary market. The month concluded with the inaugural AUD bond issued by the National Bank of Abu Dhabi. This issue provided further evidence of both the demand for AUD denominated debt as well as the continued diversity of companies issuing bonds in the Australian corporate bond market.

Market Outlook

Recent data releases vindicated the decision by the Reserve Bank of Australia (RBA) to ease monetary policy in December by cutting the cash rate to 3.0%. Subsequent commentary from them suggested that they were holding a reactive mindset; and, we suspect that the run of weak data in the interest rate sensitive sectors and easing in price pressures will help to build the case for further monetary easing towards the middle of the year.

It looks like growth will be sub trend in both Q4 and Q1, with this view finding support from weak business and labour market conditions. While the RBA's forecasts allow for some lift in the unemployment rate, a rise towards 6% would most likely bring about another easing. However, if recent gains in equity markets are held onto, positive wealth effects have the potential to create a virtuous circle that drives a recovery in business and consumer spending, negating the need for further policy easing.

At the time of writing, markets were factoring in one further 25 bp easing by April/May with the chance of another over the second half of the year. Such a profile is not that far off our own view and we continue to regard the shorter end of the curve as broadly fairly valued. We still regard the longer end of the curve as being on the expensive side of fair value and offering investors' little protection against an ongoing improvement in risk appetite or further improvement in the economic outlook. While we remain of the view that a major sell-off at the long end is still some time away given offshore policy settings, we continue to hold a strategic defensive duration bias.

We have noted the strong rally in credit spreads which has released a large portion of the value we identified in the sector. That said, credit spreads at current levels remain moderately attractive in a low yield environment and we continue to maintain an overweight allocation to spread sectors, most notably semi-government and corporate debt. However given the extent to which these sectors outperformed during 2012, and mindful that corporate fundamentals may be peaking, our strategic bias is to use any further rally in spreads as an opportunity to trim exposure.

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	3.25
Index	3.95
Active Position	-0.70

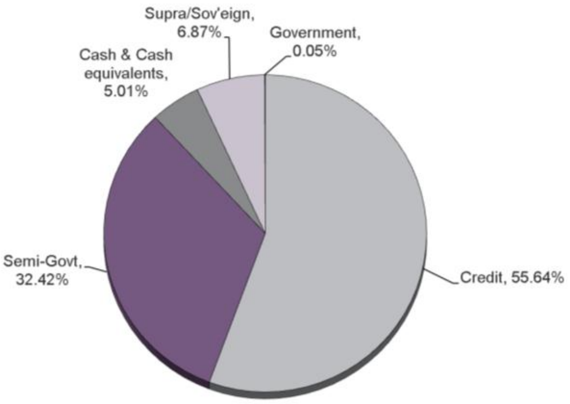
Interest rates – underweight duration:
During the month, we used the modest rally in bond yields as a further opportunity to reduce the duration of the Trust's investments. Having commenced the month with duration at around 0.5 year below Index, we reduced this by a further 0.25 and at month end were positioned at 0.7 below Index duration. We feel that we have entered a more difficult phase of the interest rate cycle for bond markets, with the growing confidence that we are getting very close to the end of the monetary easing cycle. As we have indicated in previous reports, we are also mindful of the risks of a more sustained rise in global bond yields should, as we expect, the economic recovery in the US gain further momentum.

Overweight Corporate Debt:
While credit spreads have tightened considerably over the past six to nine months, we maintain our belief that this sector is poised to outperform risk free assets on a 12 month forward looking basis due to the demand for 'yield', which should be supportive for credit spreads as well as the higher running yields these securities provide. While we are not looking to add to our positions, we are comfortable with our overweight allocation to this part of the bond market. Our favoured sub-sectors continue to be the debt of the 'big four' Australian banks, listed property trusts and infrastructure debt. We also see value in AAA mortgage backed securities, which have somewhat lagged the rally in corporate debt and should be supported by recent indications that home prices are starting to rise.

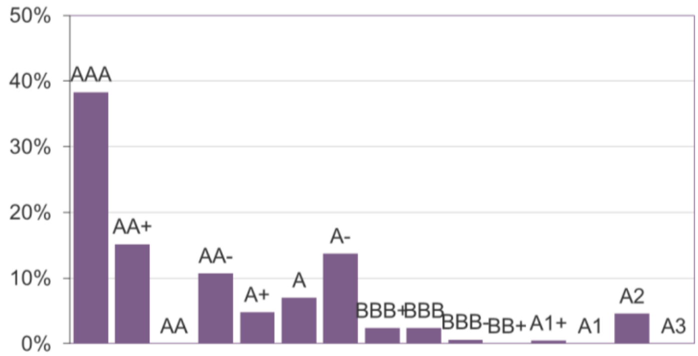
Overweight semi-governments (including government guaranteed):
Our government exposure is concentrated in semi-government and government guaranteed securities. This not only provides a yield advantage relative to government bonds, but also participates in the bond/semi margin contraction which we believe will occur at some stage as the state governments work towards a more solid footing in their fiscal balances. Our largest overweight is to Queensland Treasury Corporation given its medium term commitment to restoring its AAA credit rating.

Trust Snapshot

Sector Allocation



Credit Rating Distribution



Rounding accounts for small +/- from 100%.

Signatory of:

PRI Principles for Responsible Investment