PERENNIAL FIXED INTEREST

Perennial Australian Fixed Interest 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 Australian Fixed Interest Trust*	1.38	2.01	6.72	9.35	9.63	9.05	9.78
UBS Composite Bond Index (0+years)	1.54	1.94	3.94	6.99	9.08	8.31	8.15
Value Added (Detracted)	**-0.16**	**0.07**	**2.78**	**2.36**	**0.55**	**0.74**	**1.63**
Net Performance	1.35	1.93	6.40	8.97	9.24	8.67	9.39

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

- Global bond markets delivered strong gains during April, as a run of softer economic data led markets to reassess the outlook for monetary policy.
- The key influence on the Trust's relative performance was its short duration.
- During the month we extended our short duration position which at month end stood at one year below the Index.

Performance

Global bond markets delivered strong gains during April, as a run of softer economic data led markets to reassess the outlook for monetary policy. In Australia, the markets, having largely removed the prospect of future monetary easing earlier this year, once again priced in the expectation of the Reserve Bank of Australia (RBA) cutting the official cash rate from 3.0% to 2.5% over the next three to six months. This shift in market expectations was the catalyst for a 30 basis points decline in longer term yields which saw the UBS Composite (0+ years) Index (the Index) return 1.54% for the month.

The Perennial Australian Fixed Interest Trust (the Trust) finished up 1.38%, underperforming the Index return by 0.16%. Financial year to date, the Trust's return is 6.72%, outperforming the Index by 2.78%.

The key influence on the Trust's relative performance was its short duration, which detracted value (20 basis points) as bond yields fell. Yield curve positioning also detracted value (4 basis points) due to our curve steepening bias, with the largest fall in yields occurring at the longer end of the yield curve. These influences were partially offset by a positive contribution from credit strategies. Our overweight allocations to both semi-government and corporate debt added value (five basis points) as these sectors continued to benefit from strong investor demand for high quality yield. At the security level, further spread tightening within the financial and RMBS sectors had a positive impact on performance.

Market Review

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

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 30/04/13): AUD1.3 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:** IOF0113AU

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 On the data 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	2.97
Index	3.97
Active Position	-1.00

Interest rates – underweight duration:

During the month we extended our short duration position which at month end stood at one year below the Index. Our defensive mindset reflects both longer term valuations concerns as to the level of both real and nominal yields, along with the fact that the market is now fully priced for a 2.5% official cash rate within the next few months. Should this not eventuate we would expect bond yields to give back some of their recent gains.

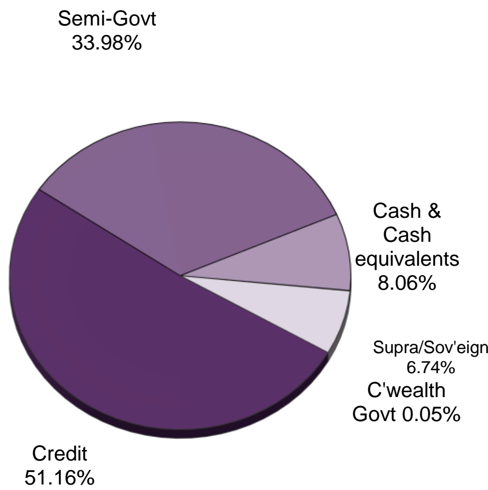
Overweight Corporate Debt:

We remain overweight this sector, albeit a bit less so than has been the case over the past 6 to 12 months. While credit spreads have tightened considerably over the past six to nine months, and have provided a terrific tailwind to performance, we feel that it is prudent to reduce exposure to this sector at current levels. We would describe credit spreads at the moment as broadly ‘fair value’ and as such have taken some of the previously overweight allocation out of the sector favouring government sectors such as semi-governments.

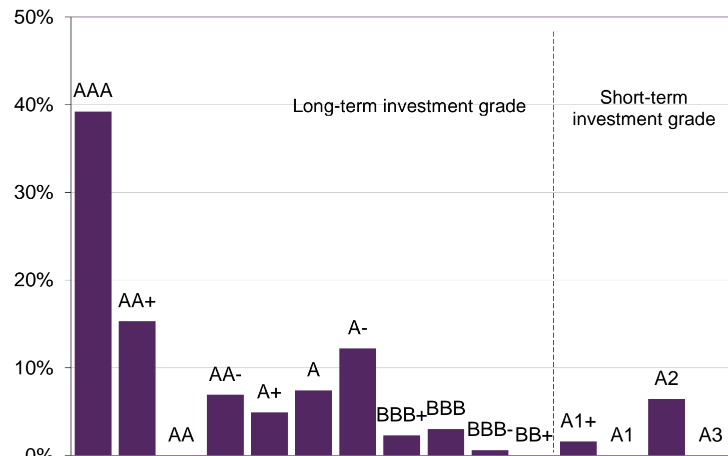
Overweight semi-governments (including government guaranteed):
Our government exposure is concentrated in semi-government and government guaranteed securities. We have recycled some funds from other sectors, such as credit, into what we believe to be this relatively stable and very attractive sector within the bond market. In our view, the yield advantage, relative to government bonds, justifies a meaningful allocation to the sector with some prospect of the bond/semi-government margin narrowing in the future as state governments work towards a more solid footing in their fiscal balances.

Trust Snapshot

Sector Allocation



Credit Rating Distribution



Rounding accounts for small +/- from 100%.

Signatory of:

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