

Perennial Tactical Income Trust

Monthly Report as at 31 December 2011

	Month %	Quarter %	FYTD %	1 Year %	2 Years % p.a.	3 Years % p.a.	Since Inception % p.a.#
Perennial Tactical Income Trust*	0.56	1.19	2.19	6.42	7.32	-	8.96
UBS Bank Bill Index and UBS Composite Bond Index (0+years) equally weighted	0.59	1.58	4.56	8.15	6.75	-	6.30
Value Added (Detracted)	-0.03	-0.39	-2.37	-1.73	0.57	-	2.66
Net Performance	0.52	1.08	1.96	5.95	6.84	-	8.47

*Gross Performance. #Since inception 16 June 2009. Past performance is not a reliable indicator of future performance.

- The Trust finished the month up.
- The Australian bond market recorded moderate returns over December.
- Credit markets recovered some of the margin widening that occurred in the prior month.

Performance

The Australian bond market provided moderate returns over the month. Longer term bond yields fell as a result of continuing sovereign issues in Europe, with risk free government bonds being by far the best performing sector.

The UBS Composite Bond Index (0+years) returned 0.78% and the UBS Bank Bill index returned 0.40%.

The Tactical Income Trust (the Trust) finished the month up 0.56%, slightly underperforming the UBS Bank Bill Index and UBS Composite Bond Index (0+years) equally weighted (the Index) return of 0.59% by 0.03%.

In terms of tactical asset allocation, the Trust's weighting to fixed interest was minimal as we maintained 'cash like' duration over the month based on our view that bond pricing was expensive. This positioning detracted slightly, as bond yields fell somewhat over the month. We continue to maintain a material underweight position to bonds as they are expensive relative to our assessment of the domestic economic fundamentals, expected future path of monetary policy and our assessment of 'fair value'.

The Trust also maintained overweight allocations to credit sectors, including a small allocation to higher yielding securities, which added value due to some narrowing in credit spreads. This reversed some of the previous month's widening. The Trust's exposure to floating rate credit occurs via its unit holding in the Perennial Cash Enhanced Trust and the Perennial Australian Fixed Interest Trust, both of which have meaningful exposures to investment grade corporate debt and via direct investment in a small number of hybrid /high yielding securities.

Perennial Tactical Income Trust

The Trust aims to provide investment returns in excess of the Trust's benchmark the UBS Bank Bill Index and UBS Composite Bond Index (0+years) equally weighted by investing in a diversified portfolio of Australian income producing assets. The Trust aims to provide a total return (after fees), that exceeds the benchmark.

Portfolio Manager:

Glenn Feben

Risk Profile:

Moderate

Trust FUM (as at 31/12/11):

AUD199 million

Income Distribution Frequency:

Quarterly

Team FUM (as at 31/12/11):

AUD5.0 billion

Minimum Initial Investment:

\$25,000

Trust Inception date:

June 2009

APIR code: IOF0145AU

Ratings: Zenith Recommended, Lonsec Recommended, Van Eyk 'BB' and Standard and Poor's 4 star.

Research House Ratings must be read in conjunction with the appropriate disclaimers available at www.perennial.net.au/Ratings_Disclaimers1.pdf

Since inception, the key features of the Trust's performance are:

- Strong absolute return, with a since inception net return of 8.96% p.a.
- Strong relative performance, with an excess net return of 2.66% p.a.
- Consistent positive monthly returns.
- A more stable return profile than traditional fixed interest.

Market Review

The Australian bond market recorded moderate returns over December, with yields flat to lower. At the shorter end of the curve, three year government bonds rallied over the first two thirds of the month, helped along by a cut in the official cash rate from 4.5% to 4.25% on 6 December and a number of weaker domestic economic readings. These included softer than expected building approval, labour force and housing finance approval data. Despite recent monetary easing, consumer sentiment fell sharply with consumers particularly bearish on the outlook for economic conditions one year ahead. After getting down to as low as 2.99%, the three year government bond yield rose again towards the end of the month, on stronger US economic data, finishing the month at 3.13%. This was largely unchanged from November's close of 3.12%.

Not all domestic data releases were softer than expected. GDP rose 1% over the September quarter, lifting the yearly growth rate from 1.9% to 2.5%.

Expectations for the future path of the cash rate varied over the month, with periods of heightened uncertainty about prospects for European sovereign debt coinciding with markets pricing in a very aggressive easing cycle. The yield on the August 2012 30 day interbank futures contract got down to 2.81% on 19 December, before ending the month at 3.07%.

At the longer end of the government curve, ten year bond yields continued to benefit from flight to quality flows. Yields fell progressively and ended the month at 3.67%, a fall of 26 basis points. As a result of these moves, the spread between 10 year and 3 year government bond yields narrowed by 27 basis points to 54 basis points.

Credit markets recovered some of the margin widening that occurred in the prior month, with the Australian Itraxx 5 year series narrowing by 14 basis points to close the month at 181. However, there were a few subsectors that underperformed, including offshore financials. This was mainly on the back of Standard and Poor's (S&P) sector wide credit ratings downgrades of the banking system. The primary reason was some sweeping changes to the way S&P rate financial institutions. The new methodology, released by S&P in November 2011, changed ratings depending on an entity's 'systemic' importance, potential level of government support, country ratings (BICRA), notching of subordinated debt and strength of parental support for subsidiaries (in particular foreign), among others.

The industry wide changes adversely affected the ratings of a number of US and European financials, and included downgrades of Australia's 'big four' banks. While there was no credit deterioration in the underlying balance sheets, the downgrade of the Australian banks was country specific as a result of the respective BICRA rating. Conversely, oversold European supra-nationals, in particular those explicitly guaranteed by Germany, performed particularly well during December.

Market Outlook

The global outlook progressively deteriorated over the latter part of 2011, with the likelihood of a European recession in early 2012 increasing. The Chinese economy is also slowing more quickly than expected, with an engineered slow down compounded by developments in Europe. Chinese policy makers have already begun to respond but stimulus measures will take several quarters to grip. Growth in the US appears to be lifting but remains vulnerable to developments in Europe. The global economy appears most vulnerable over the first half of 2012 and, it is against this backdrop, that we look for the Reserve Bank of Australia (RBA) to ease in February with a further and final easing in May looking increasingly likely. A burst of front end loaded easing should provide a buffer against negative offshore developments and local fiscal tightening, as well as provide a fillip to the interest rate sensitive sectors of the economy. Once we move into 2013, the worst of the drag from fiscal policy should move behind us and pressure may mount on the RBA to shift monetary conditions from accommodative to neutral levels.

Markets continue to discount a more aggressive easing profile, implicitly factoring in a more dire outcome for Europe despite recent progress. While this remains a possibility, we do not believe it is the most likely outcome given the political capital invested in the Euro vision. In our view, bond yields remain well below fair value levels and we continue to maintain a defensive interest rate bias.

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	0.48
Index	1.97
Active Position	-1.49

Interest rates: underweight fixed interest/overweight cash.

Given our focus on capital preservation, we continue to maintain an underweight duration position. In our view, the current level of bond yields are very low and are poor value relative to our expectations for the cash rate and the outlook for the economy. In particular, we feel

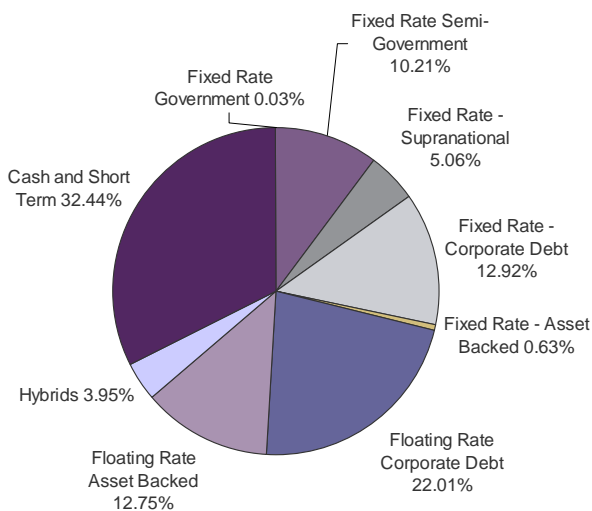
short to mid curve maturities are most overvalued and expect them to underperform as the RBA fails to validate the market's very aggressive view of how low the cash rate will fall over the next 6 to 12 months.

Sector allocation.

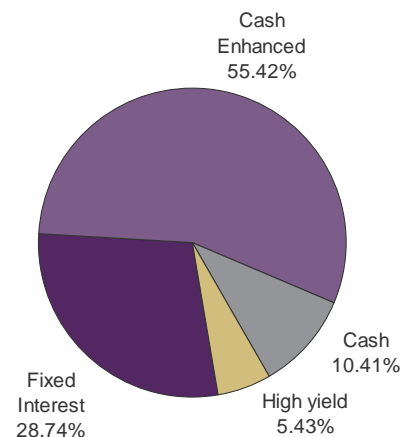
Solid corporate fundamentals, good levels of profitability and adequate risk premiums for investors make corporate debt an attractive investment option. We remain overweight this sector and expect that it will outperform risk free assets over the medium term. We view the recent widening in spreads as presenting an opportunity to increase exposure. Our government exposure is concentrated in semi government and guaranteed bank securities, on the basis of the attractive yield advantage they offer relative to government bonds.

Trust Snapshot

Asset Allocation



Sector Allocation



Rounding accounts for small +/- from 100%.