Perpetual Investment Funds
PERPETUAL
ESG REAL RETURN FUND
31 December 2024

FUND FACTS

Investment objective: Aims to target a pre-tax return of 5% per annum above inflation (before fees and taxes) over rolling five-year periods, while minimising downside risk over rolling two-year periods.

Inception date: May 2021
Size of fund: $37.0 million as at 30 September 2024
APIR: PER0761AU
Management Fee: 0.85% pa ^^Refer to PDS for Management Costs
Investment style: Diversified risk budgeting, active, value, ESG
Suggested minimum investment period: Five years or longer

FUND BENEFITS

Provides investors with access to a diversified portfolio of assets and the opportunity to align their investments with their personal values and ESG preferences. Perpetual may adjust the Fund's asset allocation to respond to changing market conditions and/or take advantage of new opportunities.

FUND RISKS

All investments carry risk and different strategies may carry different levels of risk. The relevant product disclosure statement or offer document for a fund should be considered before deciding whether to acquire or hold units in that fund. Your financial adviser can assist you in determining whether a fund is suited to your financial needs.

TOTAL RETURNS % AS AT 31 DECEMBER 2024

PERFORMANCE	1 MTH	3 MTHS	6 MTHS	1 YR	3 YRS PA	5 YRS PA	INCEPT PA	VOLATILITY^	3 YRS PA	INCEPT PA
Perpetual ESG Real Return Fund (Gross)	0.08	0.20	3.61	5.66	1.10	-	1.91	Perpetual ESG Real Return Fund	-	-
Perpetual ESG Real Return Fund (Net)	0.00	-0.01	3.17	4.76	0.25	-	1.05	Mercer Balanced Growth Median	8.57	7.73

Past performance is not indicative of future performance.^^ Information on Management Costs (including estimated indirect costs) is set out in the Fund's PDS^ Volatility and Mercer Balanced Growth Median data is lagged by 1 month

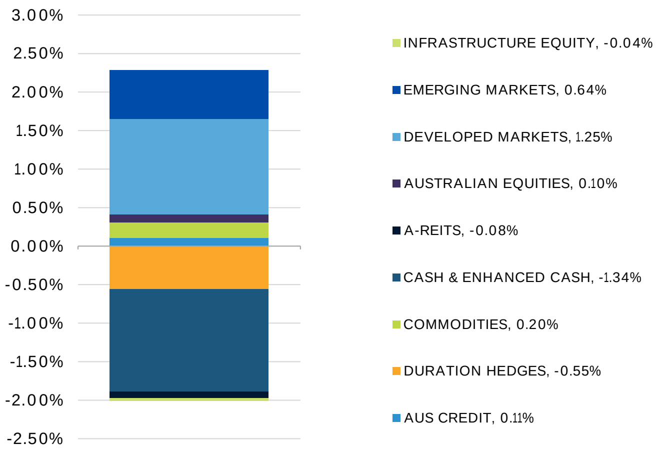
ESG APPROACH

The Fund may invest in underlying Perpetual funds which invest in Australian shares, fixed income and credit. Perpetual's ESG and value-based criteria, as described in the Product Disclosure Statement, are applied to these underlying funds. The Fund may also invest in underlying funds of Perpetual related bodies corporate which invest in international shares. A different ESG approach utilising ESG integration, positive and negative screening is applied to these underlying funds. The Fund may invest in other pooled managed funds and exchange traded funds that adopt different ESG approaches as determined by the applicable responsible entity or trustee of these funds. We do not have any influence over or assess the ESG approaches used by these other pooled managed funds or exchange traded funds. We do not consider any ESG factors (including labour standards) when deciding to buy, retain or sell an investment in any other asset class of the Fund.

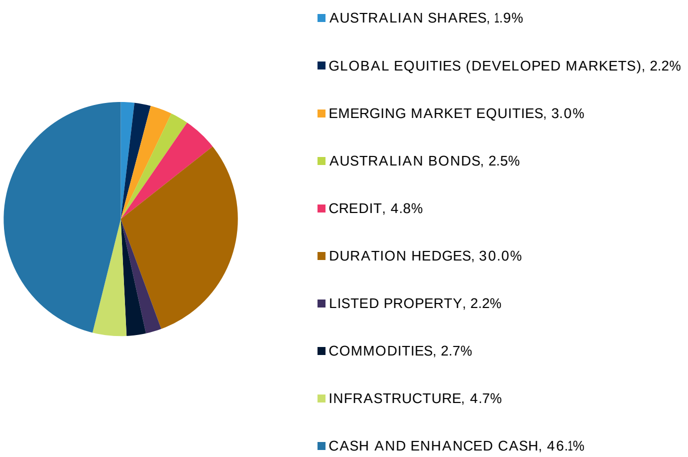
CHANGES IN ASSET ALLOCATION (%)

	CURRENT	3 MTHS	6 MTHS	1 YR
Cash	46.1%	2.5%	26.4%	8.2%
Fixed Income & Credit	37.3%	26.6%	-13.0%	-5.6%
Australian Equities	1.9%	-12.8%	-3.9%	-3.7%
International Equities	5.2%	-17.1%	-9.4%	-3.7%
Commodities	2.7%	1.7%	-0.1%	0.3%
Property	2.2%	-0.3%	0.0%	-0.2%
Other Investments	4.7%	-0.5%	0.1%	4.7%

3MTH CONTRIBUTION TO RETURN (GROSS)



PORTFOLIO SECTORS



FUND PERFORMANCE

The ESG Real Return Fund returned 0.2% (net) in the December quarter. Over the past 12 months, the Fund has returned 5.7% (net).

The Fund's US dollar and emerging market currency exposures performed very well over the quarter as the greenback rallied strongly reflecting the ongoing outperformance of the US economy and the expected impact of the incoming Trump administration.

Allocations to Australian and global equities was constructive during the quarter as equities moved higher. Stock selection among developed market and Australian equities detracted slightly as value underperformed. The ESG premia also detracted among global equities as global ESG focused indices underperformed their broad market counterparts. Equity option strategies had a positive performance in the quarter and over the full calendar year have only had a minor detraction from the total portfolio performance, which is a very good outcome considering the rally in equity markets.

The Fund's fixed income allocation detracted from performance as yields rose globally. Soft commodities continued to contribute, marking a very strong year, while the metals basket was down for the quarter.

1. RETURN SEEKING ASSET CLASSES

Beginning of the Quarter: Low Allocation
End of the Quarter: Low Allocation

Elevated equity valuations are underpinned by expectations of a soft landing for the global economy and supportive central bank action on policy rates. With so much good news already priced in, we maintain some caution. Allocation to global deep value was increased during the December quarter while exposure to Australian equity beta remains low. Our allocation remains focused on quality companies trading on low valuations, offering solid dividend yields, and good prospects for undertaking buy-backs.

The Fund's return seeking opportunities include;

- Global equities in addition to exposures in emerging markets and Australian equities all with a value and quality style bias;
- Global and Australian listed property; and
- Australian credit and a small position in emerging market debt.

2. DIVERSIFYING OPPORTUNITIES

Beginning of the Quarter: Medium Allocation
End of the Quarter: Medium Allocation

With the Fund's cautious positioning with regards to return seeking assets, diversifying opportunities remain a key focus for risk management. The Fund retains:

- A range of FX exposures including the US Dollar and some emerging market currencies;
- Stock selection alpha through the Australian Ethical SRI Fund and Trillium Global Sustainable Opportunities Fund.
- The Fund also maintains exposure to a select group of sustainable infrastructure stocks which are leveraged to the broader trend towards sustainability, while trading at a significant discount to NAV.

3. DOWNSIDE PROTECTION

Beginning of the Quarter: Medium Allocation
End of the Quarter: Medium Allocation

We continue to manage downside risks by maintaining little or no exposure to the most expensive parts of equity and credit markets and complementing this with sizable option protection when it is cheap to implement. These include put options on the S&P 500 and a call option on the USD versus the Hong Kong Dollar and the Chinese Yuan (which are low-cost downside protection for tail risks around China), in addition to a put option on the USD against the Japanese Yen.

The Fund also maintains its exposure to 2-year US government bonds alongside modest exposure to Australian and emerging market fixed income and US 10-year government bonds. Our focus on the short end of the US yield curve reflects its high running yield and its higher sensitivity to further easing of official interest rates by the US Fed, and it benefits from lower sensitivity to any upside risk in US inflation.

In addition, the Fund's cautious asset allocation is supported by a notable cash allocation, which provides solid income and significant optionality in the event of a market selloff.

4. INFLATION PROTECTION

Beginning of the Quarter: Low to Medium Allocation
End of the Quarter: Low to Medium Allocation

The portfolio has a low (direct and indirect) sensitivity to higher interest rates which should provide some stability to out investors if the monetary easing cycle currently underway sparks an unexpected and early reversal in the recent core dis-inflation trend that is evident in most regions.

The portfolio also maintains a small allocation to a basket of commodities (which includes gold, grains, livestock, silver, palladium, platinum and copper) which are typically positively correlated with inflation.

MARKET COMMENTARY

Financial markets saw elevated volatility during the December quarter as markets parsed the results of the US presidential election, moderating monetary policy easing expectations alongside political and fiscal concerns in Europe.

- Developed market equities (+2.0%) rose, marking the close of a robust year for risk assets. US equities (+2.4%) rose, responding positively to the results of the US presidential elections and expectations for corporate profit growth under a second Trump administration. A strong November bookended by negative months, reflecting some pressure as expectations for US monetary policy moderated.

- European equities (-1.8%) were mixed with German stocks rallying (+3.0%) despite political uncertainty while French equities (-3.2%) fell on sovereign debt concerns. Ongoing political instability and the anticipated impact of US trade policy exacerbated persistent growth concerns in the world's largest trading bloc.

- UK Stocks (-0.2%) trailed the broader developed market. Domestically focused sectors fell on the weakening macro outlook. UK stocks were also impacted by rising long-term bond yields reflecting inflation expectations and concerns over the new government's fiscal policies in the budget published in October.

- The ASX 300 (-0.8%) declined, impacted by rising bond yields alongside the potential ramifications for Chinese commodity demand from proposed US tariffs.

- Japan equities (+5.4%) led developed markets, rebounding from their 3rd quarter decline and benefitting from the weakened yen improving the earnings outlook for exporters.

- Emerging Markets (-4.2%) fell throughout the quarter. The rising US dollar provided a significant headwind. Trump's election victory and associated trade policy weighed on emerging market equities, particularly China (-7.0%).

- Global bond markets saw elevated volatility throughout the quarter with 10 year yields rising across Australia (+39bps), the US (+79bps) the UK (+57bps) and Germany (+24bps).

With the resolution of the US election and the Republican party sweeping both the legislative and executive branches, market expectations for US growth have remained positive. Accommodative tax policies and a reduced regulatory burden are expected to support a soft economic landing, underpinned by resilient employment, strong corporate earnings growth, and a vibrant consumer. Growth, employment and inflation data continue to imply that US rates have been considerably less restrictive that the Fed anticipated. The strength of services sector labour data in particular, provides a challenge for the Fed as service sectors is where wages growth and core inflation have the strongest correlation, and it's also where productivity is the hardest to move higher through innovation.

The Federal Reserve lowered interest rates by 25 basis points in both November and December. However, the Fed's December meeting triggered a stock market sell-off after the release of the new dot plot, which showed a median forecast of only two additional rate cuts in 2025. While this aligned with market expectations, the tone from the Fed was more hawkish, indicating that the committee was reconsidering the "extent and timing" of further cuts.

While concerns over President Trump's proposed tariffs have unsettled markets and saw bond yields climb in the December quarter, we believe the impact on growth will be modest and unlikely to significantly influence Fed policy. Our primary concern remains the unsustainable fiscal deficit, which stands at 6.4% of GDP and is set to widen through tax cuts. This raises concerns about the long-term trajectory of fiscal policy and its potential impact on bond markets and equity valuations.

Europe continues to struggle with weak economic data and political instability, including the collapse of the German coalition government and growing concerns about French debt. Composite PMI fell to a 10-month low in November before the December print showed improvement with the service sector returning to expansionary territory. The ECB cut rates by 25 basis points in October and December and signalled more cuts in 2025 amid ongoing growth struggles. In the UK, signs of economic weakness emerged, with the services PMI hitting its lowest level since November 2023 and unemployment rising to 4.3%.

Emerging markets struggled throughout the December quarter, pressured by rising concerns over the potential impact of US tariff increases alongside the strengthening US dollar. China's economic outlook remains fraught. A lack of further detail relating to the policy stimulus measures announced in September, together with investor concerns relating to the implications of proposed Trump trade tariffs on Chinese exports compounded the existing property sector overhang, sustained deflation, high debt and weak private sector confidence.

The Australian economy continues to struggle with higher inflation and elevated interest rates, leading to six consecutive quarters of contracting GDP growth per capita. Economic growth in 2025 is expected to remain subdued, driven by softening labour market conditions and constrained household consumption. The Reserve Bank of Australia held the cash rate at 4.35% in December, signalling confidence that inflation is moving towards target and acknowledging a more-than-expected easing in wage growth. Third-quarter GDP growth was weak at 0.3% quarter-on-quarter, with private investment and consumption showing little growth. The labour market remains firm, with unemployment at a record low of 3.9%.

The challenging economic outlook for ex-US markets and the uncertain path of inflation and monetary policy provide a difficult environment for investors to negotiate, especially given sustained elevated valuations in both the US and Australia. 2025 presents the prospect of higher volatility and low equity returns, which are unlikely to be diversified by duration. As always, our focus remains on identifying investments that can generate returns of CPI plus 5% per annum over a five-year horizon while maintaining an asset allocation that ensures that no individual position or cluster

MORE INFORMATION

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