Perennial Yield Plus Conservative Trust

Monthly Report February 2022

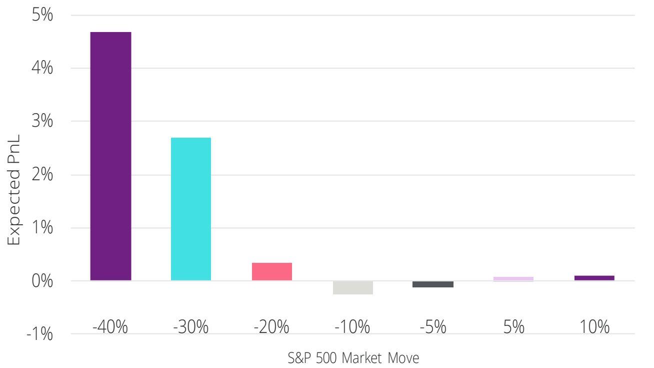
	Month (%)	Quarter (%)	FYTD (%)	Since Inception^ (%)
Perennial Yield Plus Conservative Trust (Net)	-0.5	-0.4	-0.9	-0.9
RBA Cash Rate Total Return Index	0.0	0.0	0.1	0.1
Value Added	**-0.5**	**-0.4**	**-1.0**	**-1.0**

^Since inception: June 2021. Past performance is not a reliable indicator of future performance.

Overview

- Geopolitics took centre stage in February, with Europe awakening to a theatre of war that may portend a generational shift in the political and economic structure of the continent. The volatility this unleashed lead to a loss of 0.49% in the trust, net of fees, largely driven by the Core Income strategy.
- Performance in the Core Income strategy was negatively impacted by wider credit spreads (particularly in offshore names) that impacted most sectors. Higher yields across government curves also drove non-government fixed rate bond yields higher. These effects together overwhelmed coupon income received for the month.
- The Option Strategy produced a modest loss for the month as we have yet to see a “tail event” which would trigger meaningful gains. However, the option market structure is somewhat more favourable for the strategy, looking forward.

Estimated PnL Outcomes by Market Move



The chart provides the total expected portfolio PnL given a high velocity move in the S&P500.
Source: Perennial Value Management. As at 28 February 2022.

The above figures are forecasts only. While due care has been used in the preparation of forecast information, actual outcomes may vary in a materially positive or negative manner.

Fund Characteristics

The Trust aims to generate income by harvesting equity, credit and volatility risk premia; with a conservative risk profile. A portion of this income is invested in an explicit rules-based equity option defensive strategy to offset, or benefit from, market drawdowns.

Portfolio Manager
Michael Pollard

Trust FUM
AUD $14.7 million

Distribution Frequency
Quarterly

Minimum Initial Investment
$50,000

Trust Inception Date
June 2021

Fees
0.6% p.a.

APIR Code
WPC3204AU

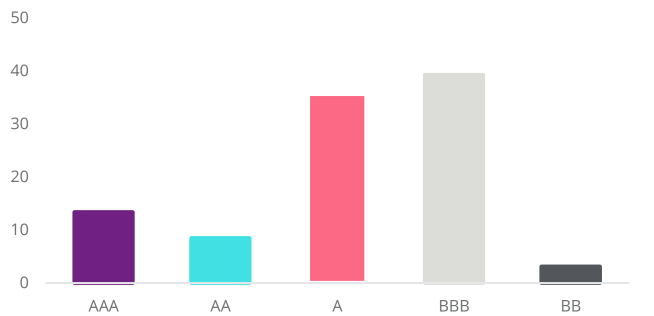
Expense Recovery
Capped at 0.1% p.a.

Portfolio Characteristics	
Modified Duration (Yrs)	0.3
Spread Duration (Yrs)	3.36
Portfolio Yield (%)	1.86
Average Credit Quality	A-

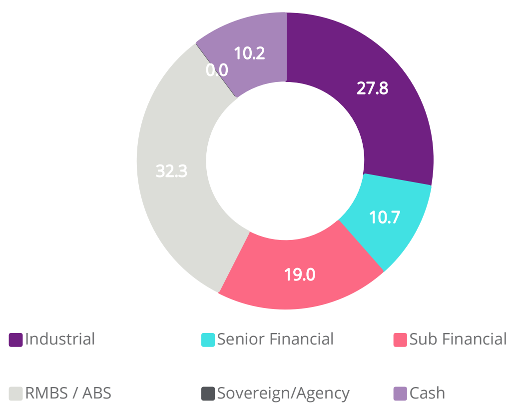
Source: Perennial Value Management. As at 28 February 2022

Portfolio yield is the expected return over the next year, assuming no changes to either portfolio composition or market yields. Average credit quality excludes overlay positions. Portfolio yield and spread duration reflect the net credit default swap exposures in the portfolio.

Rating Exposure



Sector Active Exposure



Trust Review

The Core Income Trust returned -0.38% for the month bringing the rolling three-year performance to 2.14% net of fees. Performance was negatively impacted by wider credit spreads (particularly in offshore names) that impacted most sectors. Higher yields across government curves also drove non-government fixed rate bond yields higher. These effects together overwhelmed coupon income received for the month. The fund continues to have a very modest neutral interest rate duration positioning of 0.30 years.

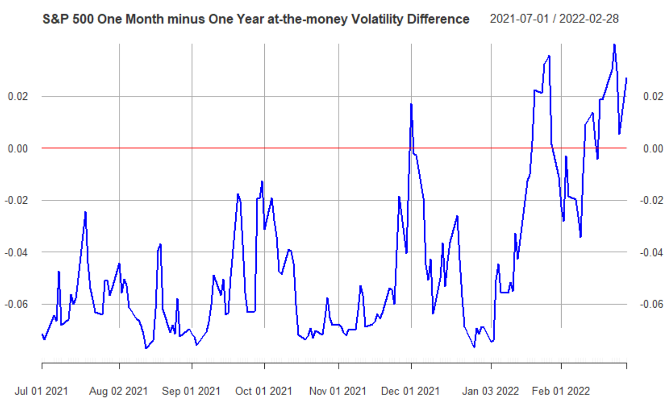
The option market structure has shifted fundamentally in the last few months, as compared to conditions seen during most of 2021. It is true that implied volatility has been marked higher overall, and as the Option Strategy is a net buyer of volatility, this is a hindrance.

However, another key input into the efficiency of the Option Strategy is the term structure, the difference between shorter-tenor implied volatility, and longer-tenor implied volatility, an example of which is shown below. In general, the Option Strategy sells options at a shorter-tenor, and buys them at a longer-tenor, so the market structure has shifted favourably on this front.

This shift in term structure should entail a greater premium received for the sold-option program, which can then be deployed for greater protection spending, or retained as an increased income component.

Trust Activity

New issuance in Australia was focused on the structured credit and financials sectors. There was little in the way of non-financial corporate issuance. We participated in structured credit issuance from Metro and AFG, as well as a GoldenTree collateralised loan obligation transaction.



* **Source:** Bloomberg, PSG

Outlook

February saw a continuation of the deterioration in sentiment that started in January. This is not surprising given the developing situation in Ukraine. Volatility in markets has naturally increased because of the associated uncertainty, a backdrop that is likely to remain in place for the foreseeable future.

Bond yields rose for most of the month, as the US printed a 7.5% annual CPI print for January and the market once again marked higher the likely trajectory of Fed rate hikes. In the last week of February, however, bond yields staged a sharp reversal lower as safe haven buying offset continuing inflation fears. The net result is that bond yields are higher for the month but not dramatically so; by way of example the Australian 10-year government bond yield has risen from 1.90% to 2.14% with the Australian bond market underperforming the US. Amidst continuing bond market volatility, it was interesting that expectations for the RBA Cash Rate have not changed meaningfully with money markets continuing to envisage four RBA rate hikes by the end of 2022.

Perhaps the main market move in February has been in US real yields, which after peaking in February have quickly fallen back to levels last seen in December. This move has been driven by a spike in the level of inflation expectations, with bond markets now pricing a stagflationary environment for the US over the next 2-3 years. Although risky assets (including credit) have suffered a fall in value because of the combination of geopolitical fears and heightened cash rate expectations across geographies, there is surprise in some quarters that the move has not been more severe given the enormous geopolitical uncertainty at this juncture. Lower real yields are likely part of the explanation, providing a support for equity markets in particular that would perhaps otherwise have experienced a more disorderly selloff.

Generally geopolitical events have seen quite rapid market rebounds as the headlines diminish, though we believe the current situation may not necessarily follow the same script. Apart from the reverberations the war in Ukraine is causing at the political level, Russia is a major agricultural and commodity exporter so the economic impacts will be widely felt. All this against a backdrop in which inflation was already the prime concern of many market participants. We will be watching closer for further signs of economic disruptions, such as broader embargos of Russian exports.

As always, our aim will be to generate a running yield from credit and fixed income markets, with a conservative risk profile, whilst deploying an options strategy that carries flat to small positive with potential upside in a large equity drawdown. If market conditions make striking a balance between return and protection difficult, we would tend toward prioritising protection.

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