# Why the PCI is watching COVID winners, banks

**By Perpetual Asset Management**

30 August 2021



The Perpetual Credit Income Trust invests in a pool of fixed income and credit assets with the objective of delivering a consistent and regular rate of return to investors. Portfolio managers

Michael Korber and Anne Moal discuss how the PCI has been managed in the current market conditions and the opportunities they are seeing in credit and fixed income more broadly.

The Perpetual Credit Income Trust (PCI) targets a return of 3.25% above the RBA cash rate through the economic cycle by investing in a broad range of credit assets. The core of the portfolio are investment grade securities such as bonds and floating-rate notes issued by large corporate issuers, banks, insurance companies and occasionally governments. PCI augments returns by selective investments into high-yielding securities. As Anne Moal explained at a recent investor day presentation, PCI increases allocations towards specific high yield assets when we have identified particular relative value opportunities. Many companies restructured in 2020 in response to the Covid pandemic and, as a result, we have seen improved cashflow, balance sheets strengthened and simplified capital structures from issuers. These are positive attributes for when we assess issuers that we may lend to.

PCI's investment guidelines are deliberately broad and as Michael Korber explained, the objective is to have a flexible investment strategy. This allows PCI to maximise the opportunity for returns in different segments of the credit market over time while still allowing us to minimise risk by being well-diversified across markets and individual issuers. To do this, a key part of the process is research and underlying risk control to determine how much risk we put into portfolios. Every security, every bond, every loan that we invest into is scrutinised by a team of research analysts, who spend a lot of time making sure that the assets we include in the portfolio are of the highest quality and meet that defensive characteristic that we're looking for in the portfolio.

With financial markets having risen on the back of strong economic growth expectations, supportive monetary and fiscal policy, and continued Covid vaccine rollout globally, we note that credit margins for both investment grade and high yield have rallied and returned to pre-COVID levels. Looking forward, we see strong positives in terms of the macroeconomic environment, patterns of issuance and maturities, and some technical factors. We think that the short-to-medium term outlook remains robust. The base case for investing remains quite sound and, with RBA closing its funding facility to the banking sector, we expect to see the banks returning to the credit market. That will generate an increased investment opportunity but, at the same time, it may put a little bit of pressure on spreads.

Our view is that investment grade assets in general have had a good run over the last four months. Over the next 12 months we may see a little bit of pressure coming into the market from increased issuance by banks. As a result, within our portfolios, we've been selectively increasing allocations to some specific high-yield assets that we've identified as being particularly strong relative value opportunities. In relation to companies that have been affected by Covid, and for which we have had good and timely information on performance and cash flows, they have strengthened balance sheets and raised liquidity. Some of the issuers have done very well through Covid and been provided with opportunity to deleverage

or simplify their capital structure or acquire and this has provided us with some investment opportunities.

Looking a little further ahead future opportunities, we're fortunate as a result of the volatility around Covid to have a portfolio that is currently really well set. We believe that we've got good, solid, relatively high-running yield in the portfolio and so the pressure to take risk is not significant within the portfolio. One place we see opportunities is in the securitisation markets.  We're in an environment where yields have been really low, so we have gradually built up a position there. Currently, we have around 16% of the portfolio in different asset-backed sectors, the largest of them being the residential mortgage market. The sector has been very resilient, and we've built our position because we think it will continue to offer competitive relative value and perform very well going forward. As at 30 **June** 2021, allocations to residential mortgage backed securities (RMBS), asset backed securities (ABS) and commercial mortgage backed securities (CMBS) comprised 16.1% of the portfolio.

[View the latest PCI webinar or the slide pack]

**Find out more about the** [Perpetual Credit Income Trust.]

This information has been prepared by Perpetual Investment Management Limited (PIML) ABN 18 000 866 535, AFSL 234426. It is general information only and is not intended to provide you with financial advice or take into account your objectives, financial situation or needs. You should consider, with a financial adviser, whether the information is suitable for your circumstances. To the extent permitted by law, no liability is accepted for any loss or damage as a result of any reliance on this information.

The information is believed to be accurate at the time of compilation and is provided in good faith. This document may contain information contributed by third parties. PIML does not warrant the accuracy or completeness of any information contributed by a third party. Any views expressed in this document are opinions of the author at the time of writing and do not constitute a recommendation to act. Any views expressed in this document are opinions of the author at the time of writing and do not constitute a recommendation to act. This information, including any assumptions and conclusions is not intended to be a comprehensive statement of relevant practise or law that is often complex and can change.

The product disclosure statement (PDS) for the relevant Fund, issued by PIML, should be considered before deciding whether to acquire or hold units in the fund. The PDS and Target Market Determination can be obtained by calling 1800 022 033 or visiting our website www.perpetual.com.au. No company in the

Perpetual Group (Perpetual Limited ABN 86 000 431 827 and its subsidiaries) guarantees the performance of any fund or the return of an investor's capital. Past performance is not indicative of future performance.