Realm High Income Fund

December 2014

Investment Objective

- Provide a Net Return of 3% over cash.
- Preserving the value of your investment.

Net Performance

Period	Ordinary Units (incl. franking)	RBA Cash Rate	Excess Return (incl. franking)	Wholesale Units (incl. Franking)
1 Month	0.63%	0.21%	0.42%	0.66%
3 Months	1.66%	0.62%	1.04%	1.76%
6 Months	2.37%	1.25%	1.12%	2.61%
1 Year	6.32%	2.50%	3.82%	6.82%
2 Years p.a	7.45%	2.62%	4.83%	
Since Inception p.a*	7.45%	2.69%	4.75%	7.05%

*Ordinary units Inception 26 September 2012. Wholesale units Inception 9 October 2013

Fund Statistics

Running Yield	5.87%
Volatility*	0.96%
Interest rate duration	0.35 yrs
Credit duration	3.30 yrs
Average Credit Rating	A-
Number of positions	43
Average position exposure	2.33%
Worst Month*	-0.11%
Best Month*	1.12%
Sharpe ratio*	4.89
Information Ratio*	4.99

* Calculated on Retail Units since Inception 26 September 2012

Fund Update

Our **Cash** weighting increased from 11% to approximately 17% over the month of December, driven primarily by a moderate reduction to the fund's hybrid and RMBS exposure. This change is consistent with a moderate deterioration in our top down macro scores.

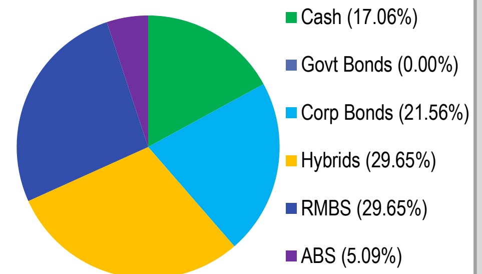
Government Bonds experienced another strong month, with the Aussie 10 year settling around 2.74% at month's end, having started the month above 3%. The Aussie 10 year is now yielding 1% less than it was in mid-September, delivering a total return in excess of 10% over the period. The month also saw wholesale reductions in Australian GDP and CPI estimates and with it rate expectations. These lesser expectations were already priced in our view, meaning that the drive lower in yields now seems to presume an even more meaningful slow-down in Australia's growth prospects. Our positioning in this environment has been moderately long; recognising the support provided by European plans around asset purchases, as well as the continuation of Japanese quantitative easing. Equally we note that fundamentally the price reflects the distortions of global quantitative easing and could not be justified as fair on a stand-alone fundamental basis. The most recent rally in the second half of the month has driven bonds into expensive territory domestically given the information we currently have at our disposal. The pathway required for the next leg lower to be justified would require monetary policy to be largely in-effective on the real economy and would likely require a further deterioration in commodity markets.

Meanwhile US rates also rallied despite wholesale upgrades to GDP, illustrating that there is more than fundamental reasoning driving the trade. We are likely to move to a neutral position under the status quo.

Corporate Bonds allocation remained static over the last month at approximately 21%. There was movement within the portfolio with senior 5 year floating rate exposure in NAB and CBA being redirected into NAB's AA - rated fixed rate 7 year security. This security is a "Climate Bond", meaning the money can only be used to fund green projects. The deal priced in line with conventional senior and piqued our interest, given its niche appeal. Though it is not unreasonable to assume that this green designation could drive a premium over time, this is not presently observable. The NAB 2021 Climate Bond is the single largest position within our portfolio as at year end.

Hybrid allocation was reduced by approximately 3% over the month. ORGHA was reduced in November, which provided the space to increase the holding intra month. Furthermore, the strength into month end allowed the position to be taken back to its starting point by the end of December. Outside of that, we heavily reduced our exposure to CBAPC and increased our holding of ANZPC substantially. The remaining activity could be described as trimming and adding around intermediate price movement.

Portfolio Composition



Sector limits

Sector limits	Asset Allocation Range	SAA Target
Cash	0% - 100%	10%
Government Bonds	0% - 100%	10%
Corporate Bonds	0% - 60%	10%
Corporate Hybrids	0% - 10%	5%
Bank Tier 1 Hybrids	0% - 25%	15%
Sub Debt Hybrids	0% - 25%	15%
RMBS	0% - 60%	30%
ABS	0% - 20%	5%

RMBS exposure moderated over the month to just under 26%. We remain constructive on certain parts of the sector. The dynamic created by S&P's downgrade of Genworth's lenders mortgage insurance business has been a key driver of widening in spreads. This drove our increase in exposure last month. In the current month we added newly issued securities out of the Torrens trust (mortgages securitised by Bendigo Bank). The reduction in weighting came out of our non-conforming RMBS holdings. Our activity over the last month clearly illustrates that our behaviour is entirely price and value dependent. Last month we noted that the weakness in conforming insured RMBS was episodic in our view. This was reflected in the strong pricing of the Torrens deal which saw the equivalent of the A rated security we purchased last month in AMP's Progress deal, priced over 1% dearer.

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Fund Update Continued

That said there are a number of issuers lined up and due to market in the first half 2015. Any sign of volatility could drive delays, further congesting calendar. This could result in spreads widening. Our single largest exposure has been taken in AA- rated securities, within the last two conforming deals. This has been based on our value for risk methodology, which drives us to invest in the best compensation per unit of risk. This opportunistic and agnostic approach means that we are always in a position to exploit value regardless of where it avails itself in the capital structure. On that basis we are comfortable that pending issuance will see us increase our exposure, the only unknown being the rating and attachment point.

ABS exposure sits at our strategic asset allocation level of 5%, with no change over the last month. We are constructive on the sub-sector and feel that it delivers higher rated paper at an attractive rate. As a reminder, the A rated fleet partners note that increased the funds allocation last month delivers a return of 2.5% above the bill rate and benefits off amortisation features, as well as 17% in hard subordination and generous excess spread. What we will say however, is we have noted a flurry of new small financiers into the space who maintain broad offers for investors to participate in their programs. Needless to say, it's not apples with apples. We heavily favour diversity (bigger pools are better as it reduces idiosyncratic risk), track record (the ability to illustrate product and issuer performance), and margin (the issuer has the brand and presence to charge an amount which supports the product thesis, not discounting for cheap dollars and mispricing risk). This is an area which is highly specialised and is generally best left to professional and institutional investors.

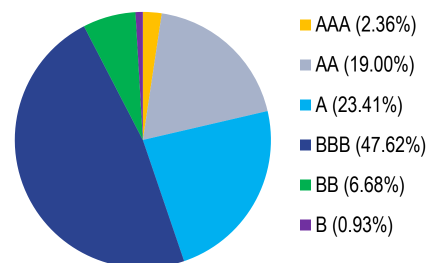
Portfolio insurance remains at an above average level, given the fact that we remain almost fully invested and in recognition of current market uncertainty.

Fund Outlook

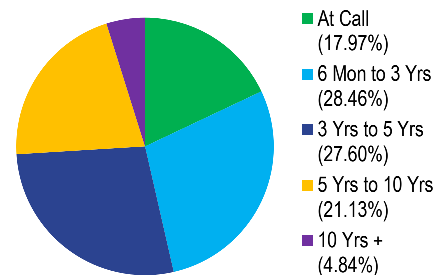
We are seeing an increasing number of sector or commodity specific events that are presenting a broader headwind of sorts. In the last month we saw Crude future prices fall sharply, emerging markets sell off and volatility generally increase across the board. The question is whether the increase in volatility is a sign of an impending event or just a sign of increasing investor awareness. In many ways the current environment exhibits signs of long absent normalcy. In oil we saw the build-up of record long positions by speculators in the face of increasing supply and moderating demand. What is strange is not the sell-off, but rather how the non-commercial market got itself positioned so long. This particular market remains extremely vulnerable to further weakness. Not because of fundamentals, but rather as a consequence of the financialisation of the commodity causing a significant increase in leverage. Think of this as a build up of energy that really only needed a spark to propel the market in a downward direction. In markets we become so pre-occupied with the spark and generally remain ambivalent to rising stores of financial energy that have the capacity to create a severe market trauma. In that regard, what we are seeing in emerging market debt, US High Yield Debt and a number of commodity prices could be viewed as healthy; as a release of stored energy that makes the future a safer place at the cost of the present's capital. This could very well be the theme for 2015, a year where the energy that is stored in markets through the process of QE continues to drive and support the system, while simultaneously creating idiosyncratic events, or financial fissures that will perhaps become more commonplace. In short, 2015 finds us in a cautious mood. The oil price shock of December is a welcome reminder of how benchmarked normal can be turned on its head in a blink of an eye.

The risk level in the short term remains heightened, with oil price effects, Russian solvency (and the potential impact on European banking) and the Greek elections likely to deliver an interesting start to the year. Looking a little further ahead the effectiveness of Japanese QE and the steepness of the Chinese economic descent could prove to have a say at some point during the year. We maintain strong views around fundamental value on all of our sub-sectors. This is not an environment to be taken lightly and investors must be compensated for the risk they take. With that in mind, we will continue to sell into strength and assess instances of market weakness as potential opportunities to increase our allocation to credit. We have proven that if fair compensation is there, we are happy to invest and expose the portfolio to risk, however equally when this is not the case we will continue to be driven by a safety first approach and will willingly remain under-invested in such periods.

Credit Quality



Maturity Profile



Fund Details

- Distribution Frequency: Quarterly
- Liquidity: Weekly
- Ordinary Units Management fee: 1.20% (incl. GST)
- Wholesale Units Management fee: 0.77% (incl. GST)
- RE: One Managed Investment Funds LTD
- Custodian: JP Morgan
- Unit Pricing: www.oneinvestments.com.au/Realm
- Unit Price History: www.realminvestments.com.au/media/4

Platform Availability

- Powerwrap
- IAS
- UBS
- Credit Suisse (HSBC)
- CFS FirstWrap (Private Label)
- Macquarie Wrap

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