



# Realm High Income Fund

February 2015

## Investment Objective

- Provide a 3% Net Return over cash over 3 year period.
- 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	0.35%	0.17%	0.18%	0.39%
3 Months	1.21%	0.59%	0.62%	1.33%
6 Months	2.14%	1.22%	0.92%	2.37%
1 Year	5.85%	2.48%	3.37%	6.33%
2 Years p.a	7.07%	2.57%	4.50%	-
Since Inception p.a*	7.19%	2.66%	4.53%	6.73%

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

## Fund Update

Our **cash** weighting increased from 21% to approximately 25% over the month. Our Portfolio positioning reflected a lower score in our top down screen. This was driven by weaker data in the US and China as well as Geopolitical factors out of Europe and the Ukraine. This is consistent with the manager's safety first approach.

**Government Bonds** had their second weakest month since March 2014. Our view remains the same, bonds are technically supported by ECB and BOJ asset purchases and also benefit off regulatory rules which drive banks to own highly liquid assets. We believe that pricing is distorted and supported by environmental factors which are not constants and could change at some point. That said, while these factors persist bonds will remain tethered. We note that a near term catalyst could be an increase in US rates. However, recent weakness in data has seemingly reduced the prospect of any rate rise prior to the 4<sup>th</sup> quarter. Given this environment, we have increased our notional interest rate exposure to a little over 1 year, primarily through the use of options, which provide upside exposure while limiting the downside in the event of a sell off.

**Corporate Bonds** allocation remained mainly static at approximately 18%. There was no movement in the portfolio. The allocation remains overwhelmingly invested within the senior debt of the big 4 banks, with the biggest position in the portfolio remaining the NAB 2021 Climate Bond. Our positioning within big 4 senior reflects our belief that some of the proposed bank capital rules may lead to current senior bonds being replaced with lesser securities as they mature. Our expectation is that this will improve the risk/return dynamics of these securities which combined with scarcity should drive superior relative performance.

**Hybrid** allocation remained static over the month. Small increases to individual positions were the primary drivers. We increased holdings within ANPC, ANZPA, WBCPC, WBCPD and also participated in the new NAB 5 year issue. With only Westpac and CBA to come in tier 1 issuance here domestically through to year end and in light of stronger equity market and lower deposit rates, we feel a goldilocks environment could form over the next two quarters within the sub-sector which could act to drive meaningful price performance. Given current weighting within the hybrid market, we are well placed to benefit off this dynamic.

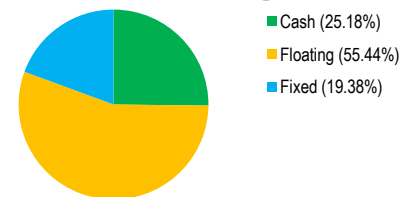
**RMBS** allocation moderately increased over the month. We added AA rated home loan risk issued out of CUA as well as investing across three tranches out of Suncorp's Apollo series. We expect to moderately increase our exposure over the month of March further via non-banks as well as Regional Bank who are likely to issue. We continue to maintain a very constructive view on the sub-sector with Lenders Mortgage Insurance downgrades and methodology changes having driven a widening in spreads which we believe are attractive given the implied risk.

## Fund Statistics

Running Yield	5.47%
Volatility*	0.96%
Interest rate duration	0.88 years
Credit duration	1.91 years
Average Credit Rating	A-
Number of positions	49
Average position exposure	2.04%
Worst Month*	-0.11%
Best Month*	1.12%
Sharpe ratio*	4.71
Information Ratio*	4.73

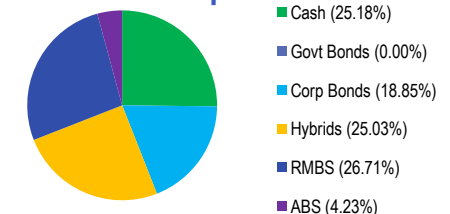
Calculated on Retail Units unless otherwise stated  
\*Since Inception 26 September 2012

## Fixed and Floating Breakdown



The fixed rate exposure is calculated based on the portfolios interest duration expressed as a percentage of the Bloomberg 0+yr Composite Bond Index.

## Portfolio Composition



## 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%

## Fund Update Continued

ABS exposure sits just below 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 two months ago delivered 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 moving 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, when combined with a cash weighting approximating 25%, we feel the portfolios posture is well balanced and reflects our positive view of certain sub-sector while maintaining cash and cover to protect against a larger negative move in credit spreads.

## Fund Outlook

At the commencement of March, our environmental macro score is as poor as it has been in some time. In our previous monthly we noted the financial performance of certain assets such as the Swiss Franc and the oil price and noted that the severity of price movement was largely a function of record investor positioning which was based on the false premise of un-conditionality.

There is a lesson here for investors everywhere. The number of individual asset classes which could be described as "distorted" are many and varied, all of them to a greater or lesser degree constrained or supported by the tether of central bank activity or regulations.

This points to the potential for a significant rise in multi standard deviation events in the coming years. The triggers for such events could come from anywhere. While many may identify the trigger as the cause, the real problem is the stored conviction which is reflected in various asset prices.

In the short term, investors are looking no further than the un-conditionality of systemic support. From Brussels to New York and everywhere in between, central bank behavior could only be described as decisive. In jurisdiction's like Australia, the impact will be more muted in mainline credit while within the European Union where the scene is set (sans a Greek debacle) for peripheral debt to roar in tighter.

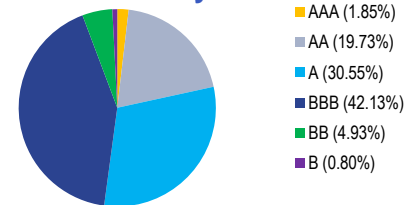
Back to Australia, our paradigm is set by where we sit in the credit cycle. Declining cash rates will be the key concern to a large number of super annuitants who have benefitted from very high compensation for a risk free position. Lower rates are intended for one thing and one thing alone, that is to drive a mobilization of capital. If net savers do not respond, rates simply move lower and lower. If they get low enough, this can act as an artificial impost or even a tax on immobilized money. Anyone who doubts this need, look no further at the portion of European sovereign debt that trades with a minus in front of it.

The issue here in Australia will be a lack of general confidence which is totally justifiable when one considers the headwinds driven by a collapse in private capex and a slow-down in global commodity demand. For now, most households look at the future with a large degree of trepidation, due to uncertainty regarding their employment prospects and a high cost of living. Our sense is that more breathing space is required to drive a response which could act as a realistic counterbalance to the weakness in our terms of trade and investment.

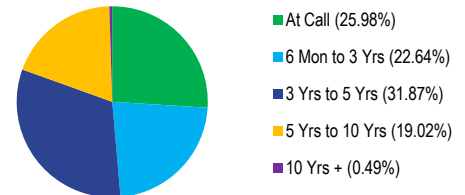
In that context, our decision to maintain an above average weighting to retail credit instruments, combined with a building weighting to RMBS is expected to bear fruit over the year. At the same time, we continue to maintain a healthy cash balance with a quarter of the fund in short term liquid assets. This is also complimented by a number of long derivative positions which are there to provide protection against a strong negative price movement.

On this basis, we believe the fund is well balanced in seeking to exploit the developing environment here in Australia while also reflecting our concern relating to building global risks.

## 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](http://www.oneinvestments.com.au/Realm)
- Unit Price History: [www.realminvestments.com.au/media/4](http://www.realminvestments.com.au/media/4)

## Platform Availability

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

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