Realm High Income Fund

January 2017

Investment Objective

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

Net Performance

Period	Ordinary Units (incl. franking)	Wholesale Units (incl. franking)	RBA Cash Rate
1 Month	0.34%	0.38%	0.13%
3 Month	1.27%	1.38%	0.38%
6 Months	3.00%	3.22%	0.75%
1 Year	6.51%	6.97%	1.69%
2 Years p.a	4.33%	4.80%	1.88%
3 Years p.a	4.88%	5.36%	2.09%
4 Years p.a	5.78%	N/A	2.24%
Since Inception p.a*	5.90%	5.60%	2.31%

Past performance is not indicative of future performance.
*Ordinary units Inception 26 September 2012. Wholesale units Inception 2 October 2013.
Adviser Units Inception 8 September 2016

Fund Update

Our **cash weighting** remained near 18% over the month, there were moderate reductions in the funds corporate and subordinated debt allocation and an opportunistic 1% increase in weight within the AT1 allocation to 10%. The fund maintains a position within AAA RMBS and senior corporate debt with a maturity of 12 months or less of approximately 11%, as such cash and cash like instruments approximate 27% of total portfolio value as at month end. This figure has increased to above 30% at the time of writing. Outside of that the fund did increase its allocation to government and semi government bonds to approximately 10%, meaning the fund holds approximately 40% of the fund in cash and defensives.

The fund is maintaining an **interest rate duration** position of approximately 0.6 years, with our technical overlay moving the position between 0.5 and 0.7 of a year. The weighted duration of the fixed rate portfolio is approximately 5 years long, and is bar-belled between shorter and longer maturities. The US long end remains moderately expensive on our estimates, with the US 10 year sitting approximately 10 basis points below a fair number. At the same time the Australian long end looks fair, shorter Australian maturities are fair to cheap depending on your cash rate outlook from here. Data momentum looks like it may have bottomed here in OZ over the last two months as commodities and energy have recovered, however at the same time the economy remains weak in absolute terms, as wages continue to lag. While we believe the outlook remains balanced over the medium term, we do believe that a stronger AUD should be quelling the debate around higher rates and ensures that lowering rates further remains an available option to the RBA.

Our **corporate** and **subordinated debt** allocation reduced moderately over the month. Within the corporate book maturities were the primary source of the reduction while our subordinated debt has been gradually reduced as the market has met what we deem to be good selling prices (4% reduction overall). The corporate bond allocation is bar-belled between very short corporate paper and 4/5 year maturities. Into month end we saw a very definite thaw as investors returned post Australia day and scratched their heads around what to do with swelling cash balances that have been a function of maturities. This led to a return of the bid for 5 year senior bank paper which seemed to tighten approximately 10 points (rise by half a percent). These are levels at which we are reasonably happy to reduce our senior back exposure. Outside of that there wasn't too much to get excited about, indeed it seems to be a seller's market right now, with investors largely motivated by refilling their books post the holiday hiatus.

Our **AT1** exposure increased by 1% over the month. Not much activity in the portfolio, with the only increase taking the form of a crossing in the name of ANZPG at levels we deemed to be reasonable. Everyone has their own approach to AT1 valuation however our view, very simply, is that the hybrid curve should be flatter, e.g. given that call risk always exists, you shouldn't see the difference you do between shorter and longer maturities. While this doesn't necessarily identify long names as cheap, it certainly highlights that the short end can be quite expensive at times. All in all longer maturities at or over 400 over look ok in light of constrained supply. It is muted that we will see a few deals over the next month or so, we await to see whether the retail demand remains as robust as it was moving into late 2016, and indeed whether the insto bid that was evident in the latter part of the year returns.

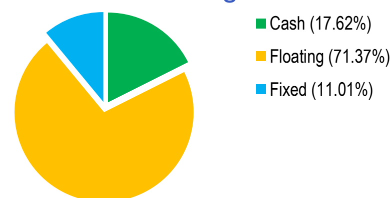
Our **RMBS** allocation remained more or less in line over the month, with the hiatus in issuance and the non-existence of investor inquiries over the holiday period. Once again this has changed materially post Australia day as three regional banks announced road shows and soundings, meanwhile we have received numerous inquiries for stock, which we once again believe is a function of bloated cash balances and a general absence of real value within unsecured markets. The liquidity premium within ABS seems to be getting targeted as a source of additional carry. In addition, price sounding seems to be speaking to demand that is willing to get filled inside existing market levels. The next few deals will identify if rumors of new investor interest in the sector are indeed true. If so we would view this as a positive signal for this market over the shorter to medium term. We have stated that this sector is earmarked for an increase, however this will be a function of price, if investor enthusiasm gets ahead of itself we are just as happy to provide the market with additional supply at a good price.

Fund Statistics

Running Yield	3.72%
Volatility†	1.04%
Interest rate duration	0.60
Credit duration	2.35
Average Credit Rating	A-
Number of positions	119
Average position exposure	0.73%
Worst Month*	-0.47%
Best Month*	1.22%
Sharpe ratio†	3.14
Information Ratio†	3.16

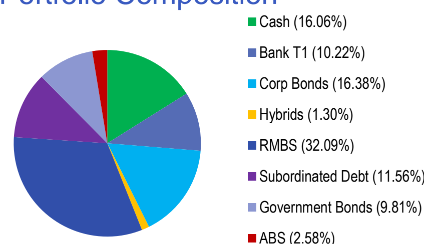
Calculated on Ordinary Units unless otherwise stated
*Since Inception 26 September 2012
†Trailing 12 Months Calculated on Daily observations

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%

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APIR Code: OMF0018AU- Adviser

Fund Outlook

Benchmark credit indices rallied all over the globe through the month of January. High beta indices such as US HY and EM are tighter than they have been in years. In the case of EM the index is trading at early 2013 levels (prior to the taper tantrum), this is despite the potential for a US/Chinese trade confrontation and the potential for higher US rates acting as a destabilizer. This was also the case here in Australia where ITRAXX AUS rallied another 10 points and Aussie bank senior 5 year insurance costs peaked their head below 0.6% per annum for 5 years.

In short, complacency continues to build. A search for credit carry at a time where fixed rates are presenting a challenging picture has compressed credit curves everywhere, this reach for carry will undoubtedly serve to tighten credit curves. Domestically there is certainly evidence of investors wanting to add credit beta to their portfolio. The interesting thing is that this all happens at a time where the macro-economic and geopolitical outlook for the world has never been quite so unclear.

There are a number of market positive soundbites that support a moderately bullish view however equally the status quo seems to be in-flux and it is impossible to prognosticate within reasonable level of certainty on what the potential array of outcomes may look like 12 months from now.

So what has changed?:

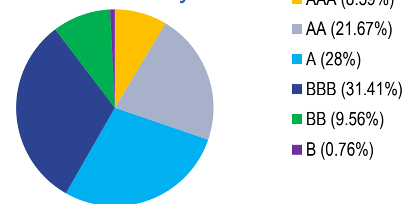
Regulation, at the time of writing the Trump administration has signaled its intent to make meaningful amendments to Dodd Frank and the fiduciary rule. The intention here seems to be to re-invigorate bank trading, and re-enable them to manufacture and sell products to their clients without needing to follow a best interests rule. It is a horrible idea, which takes the retail investor off the protected species list and once again makes them fair game in the hunt for enlarged profits. Prop trading ultimately is a very nice way of saying 'a way to make super-normal profits by selling 2's for 1's to unwitting retail investors.' There is a feeling that Glass Steagall will be buttressed at the same time, which will look to protect retail depositors from IB speculation however it will still allow investment banks to once again seek retail investors as greater fools. At the same time, across the pond the Germans are pushing back on risk floors and Basel: basically they want a test they can pass without needing to raise materially larger amounts of capita within their banking system. This has delayed a final decision by regulators. This adds weight to the idea that peak regulation may be behind us. If this is indeed the case it will mean that financial institutions on both sides of the Atlantic will be in the position to take more risk. This is good for markets here and now but doesn't bode well for financial stability further down the road.

EU/US relations. Europe finds itself at a cross-road in 2017. The Europeans will either plough ahead with deeper integration (although this may only involve a smaller number of core "homogenous" participants), or it begins to unravel into a loose federation before disintegrating altogether. Interestingly enough it is likely that Greece will once again act to highlight the divisions and lay of the land. With bailout discussions having stalled on the back of the IMF's reluctance to form part of the agreement, and Germanys insistence that the deal is dead without IMF participation, we are seemingly back to square one. The Americans may fairly take the view that Germany as the primary beneficiary of the European project should pick up the tab. This interestingly comes at a time that the British and the Europeans push ahead with Brexit discussions. It's a fascinating state of play, could the IMF be looking to trade European compliance on Brexit for assistance on a Greek bailout ? Will the Europeans bite the bullet on Greece and look to capitalize on Brexit by stealing London's market hub status? This also comes at a time that the Ukraine has become unsettled, Serbia and Kosovo tensions are heightened and Greco-Turkish relations are at multi decade lows. Not to mention a Turkey that is about to willingly vote for authoritarianism, the ongoing migrant crisis and of course Syria.

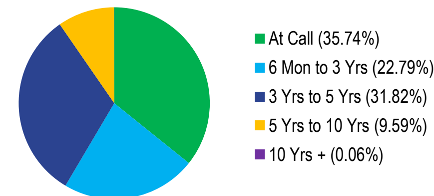
US/Chinese relations: The Chinese press are speaking of the inevitability of a military confrontation, US think tanks also speak to now being the time to bring China into line. The question is whether a confrontation of some kind (economic/military) is possible, likely or inevitable. Needless to say this would present an enormous risk to financial markets and world trade with severe effects on nations like Australia who are tied economically to China and militarily to the US. This is the most important bilateral relationship in global commerce, any impact on it will have a material impact on the global economy and financial markets.

The fund is positioned cautiously, returns have been solid over the last 12 months, with the fund having capitalized on the value the market presented through the first half of 2016, equally now risks have now turned asymmetric in many markets, leading to our decision to increase fund liquidity and reduce beta. This will allow the fund to be in a position to benefit off market volatility while maintaining sufficient credit exposure to be able to continue to deliver investors a reasonable return over cash.

Credit Quality



Maturity Profile



Fund details

- Distribution Frequency: Monthly
- Liquidity: Daily
- Ordinary Units Management Fee: 1.20% (inc. GST)
- Wholesale Units Management Fee: 0.77% (inc. GST)
- Adviser Units Management Fee: 0.77% (inc. GST)
- RE: One Managed Investment Funds Ltd
- Custodian: JP Morgan
- Unit Pricing and Unit Price History: www.realminvestments.com.au/media/4

Platform Availability

- BT Wrap
- Macquarie Wrap IDPS
- Powerwrap
- Hub24
- IAS
- UBS
- Credit Suisse (HSBC)
- CFS FirstWrap (Private Label)
- Netwealth (Private Label)
- Praemium

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