Realm High Income Fund

June 2015

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	-0.47%	0.16%	-0.63%	-0.42%
3 Months	-0.02%	0.52%	-0.54%	0.10%
6 Months	0.91%	1.09%	-0.18%	1.14%
1 Year	3.31%	2.36%	0.95%	3.79%
2 Years p.a	5.76%	2.44%	3.32%	N/A
Since Inception p.a*	6.42%	2.60%	3.82%	5.69%

*Ordinary units Inception 26 September 2012. Wholesale units Inception 2 October 2013

Fund Statistics

Running Yield	5.28%
Volatility*	1.09%
Interest rate duration	0.77 years
Credit duration	4.05 years
Average Credit Rating	A-
Number of positions	64
Average position exposure	1.56%
Worst Month*	-0.47%
Best Month*	1.12%
Sharpe ratio*	3.50
Information Ratio*	3.52

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

Fund Update

Our **cash** weighting decreased to approximately 8% over the month. Proceeds were primarily deployed into Government Bonds with a small increase into corporate bonds as the sell-off in credit intensified into the end of the month. The decision to switch cash into Government debt was motivated by our desire to protect the portfolio against single event risk.

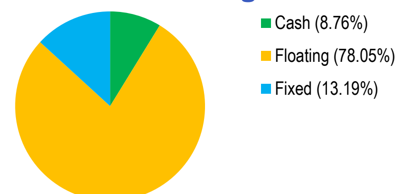
We continued to increase our exposure to **fixed rates and government debt** over the month. While concerns abound in relation to rate rises in the US, our key focus was maintaining a healthy exposure to assets that would outperform in an environment of increasing uncertainty. While our allocation to rates delivered a negative return attribution over the month, we do feel that the bonds will deliver a strong benefit in the event that circumstances relating to Greece, or the Chinese equity market sell-off, deteriorate further. From a fundamental perspective we feel Australian long bonds will begin to present value if they sell-off in sympathy with US long term rates as the Fed belatedly begins to raise rates.

Our **corporate bond** exposure increased over the month by approximately 5.0% driven by our decision to allocate cash to credit within the last week of the month. Price weakness was driven by technical and capital as well as the threat of the looming Grexit. We took this opportunity to make an opportunistic increase in our Tier 2 exposure. Big 4 Basel III complying tier 2 had widened close to 40/50 basis points over the last two months driven by new issuance. NAB's recent 2020/25 issue sold off by approximately 2.00%, which we feel reflects fair value. We are unlikely to meaningfully build on our Tier 2 exposure at these levels, however we do note that the sub-sector at least now sits within the fair value range.

Our **Hybrid allocation** was moderately reduced by approximately 3%. This was largely driven by the sale of specific names at the shorter end of the curve, including ANZPA, ANZPC and IAGPC. There were small increases to holdings including CBAPD and CGFPA. The sub-sector remains a position of high conviction based on our fundamental assessment of fair value. That said we accept that the sub-sector has exhibited a high degree of volatility over the last quarter. We have noted previously that regulatory developments will deliver safer institutions that are better capitalised, this remains a positive for Hybrid asset quality. Equally we have noted that the majority of off-shore Tier 1 refinancing has run its course, which will likely see technical pressure from here on in ease. Indeed it is fair to suggest that at current levels, you are unlikely to see issuers rushing to the market. All of that said, the strength of the sell-off in certain names over the last couple of months has been surprising. More specifically I speak of CBAPD, the issue has traded at volumes that are in order of magnitude higher than other large issues. On the basis of values the sector is reflecting spreads that are consistent with what we saw during the GFC. Considering where we are in the credit cycle, and looking at the increased focus of the regulator on asset quality and bank core equity, we feel that the sector presents the best value within our universe.

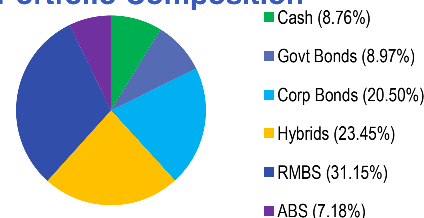
Our **RMBS** allocation reduced moderately over the month to approximately 31% of fund assets. We mentioned in our previous monthly that new investments would be considered on a deal by deal basis. We have also amended our risk classification for certain cohorts and increased our risk weighting for certain geographical areas.

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: OMF0001AU- Retail
APIR Code: OMF0009AU-Wholesale

Fund Update Continued

Our adjustments are fair and reasonable in light of the recent strength within collateral prices in certain markets coupled with industry based concentration in certain regional areas. It is entirely plausible that our allocation to the sector may gradually decline if there isn't a reversal in recent trends in issuance quality. Ultimately we are very comfortable with our existing holdings and are reticent to dilute our portfolio quality in the sub-sector for the sole purpose of maintaining our exposure.

Our **ABS** allocation increased slightly to 7%. The increase was due to our decision to invest within the most recent Flexigroup securitization. Flexigroup remain a preferred issuer in this sub-sector for small ticket finance. While there are a number of small providers in this space, few maintain the scale, diversity and program quality to compare with the better names in the sector. As we have stated previously the structure of these securities deliver meaningful subordination further supported by large levels of excess trust income. Our competence in assessing the sub sector equips us well to review risk and price accordingly. We will continue to move towards our strategic benchmark of 10% depending on issuance quality and margin.

Fund Outlook

Our environmental top down score remains in negative territory, on the back of the continuing Greek saga, a break down in Chinese equity markets and global macro-economic data which remains weak on a global basis.

Starting with the much vaunted **Grexit**, the event can be characterised as a low probability / high cost event. That said the market continues to underestimate the total potential risk and cost in our estimation. As unlikely as a Grexit and default may be, it is not a non-event. It's often the occurrence of the unthinkable which hurts the most. European data has been relatively positive off an exceedingly low base, however this is likely a temporary recovery, given that France and Italy are yet to feel the full brunt of austerity.

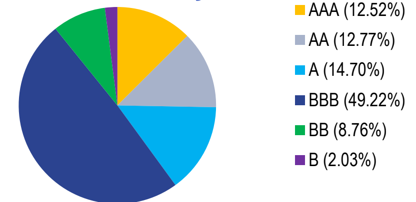
To **Asia** now and the end of the month has all been about the story in Chinese equities. While equities shake off the over-exuberance which propelled them into the stratosphere we also note the steady deterioration in trend growth in China. Despite the best efforts of the powers that be, Chinese nominal growth remains in a condition of decline. This is particularly evident within the commodity complex which is grinding lower, with the majority of commodities finding themselves at GFC type levels. The ramifications to Australia's terms of trade and private capex will be meaningful over the next few years and potentially beyond.

Moving to the **US** now, the main topic of interest has revolved around the likely timing of US rate rises. The premise of recent times has been that the US is approaching a point of strength which will allow nominal growth to move back towards pre crisis levels. This would in turn deliver a meaningful negative impact to long bond markets as yields kicked higher to reflect higher break-evens moving forward. At present the resurgence is expected to be driven by improving employment, a strengthening in wages and a rise in consumption, which remains the engine room of the US economy. We remain circumspect, while we believe the US economy is improving we feel the market may still be overly optimistic on medium term prospects.

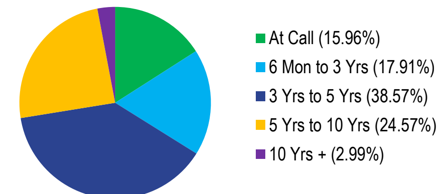
Here in **Australia**, RBA remains beset by challenges on all sides. Deteriorating terms of trade, an Aussie dollar which remains stubbornly higher than the central bank would prefer, investment and capex which is being gutted by plummeting commodity prices. Assuming that commodities are trending lower, Australian growth composition is going to be strongly challenged, the key will be the ability for the currency to respond and to move lower, providing an immediate productivity dividend. In its absence it is likely we will see further action out of the RBA.

In terms of positioning, we took advantage of technical weakness through the month of June to increase our risk exposure, meanwhile we also increased our government bond exposure, which will act to counteract the negative impact of event based risk on the portfolio. Ultimately the portfolio is positioned tactically with the Tier 1 overweight remaining the key conviction call. We believe that the price action of recent months has allowed us to purchase these assets at levels which are fundamentally cheap. We believe that this theme will be well supported by lower rates and by the withdrawal of technical pressure driven by excessive issuance through the period of 2013/2014, as well as the possibility that banks could soon be once again start issuing these securities off-shore, thus leading to scarcity. We believe that the existing portfolio delivers a healthy accrual of income in addition to providing the potential for appreciation in underlying assets over the coming quarter.

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)
- 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

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

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