REALM HIGH INCOME FUND

REALM INVESTMENT HOUSE

NOVEMBER 2023

FUND OBJECTIVE

The Realm High Income Fund is a fixed income strategy, that invests in domestic investment grade asset backed securities, bank-issued securities and corporate & government bonds. The objective of the Fund is to deliver investors a consistent return (net of fees and gross of franking) of 3% over the RBA cash rate through a market cycle.

FUND DETAILS

Distribution Frequency: Monthly
Liquidity: Daily
Buy/Sell: 0.05% / 0.05%
Inception Date: 26.9.2012
Fund size: AUD $1.63 billion
Management Fees (Net of GST):
Ordinary Units - 1.1182% Wholesale Units - 0.7175% Adviser Units - 0.7175% mFunds Units – 0.7175%
Direct Minimum Investment:
Ordinary Units - $25,000 Wholesale Units - $1,000,000
Adviser Units - $25,000 mFund Units - $10,000

NET PERFORMANCE

Period	Ordinary Units (incl. franking)	Wholesale Units (incl. franking)	RBA Cash Rate Return
1 Month	2.02%	2.05%	0.35%
3 Month	2.12%	2.22%	1.02%
6 Months	5.23%	5.43%	2.05%
1 Year	9.70%	10.18%	3.76%
3 Years p.a	3.64%	4.07%	1.62%
5 Years p.a	4.15%	4.59%	1.29%
10 Years p.a	4.17%	4.62%	1.59%
Since Inception p.a*	4.58%	4.64%	1.72%

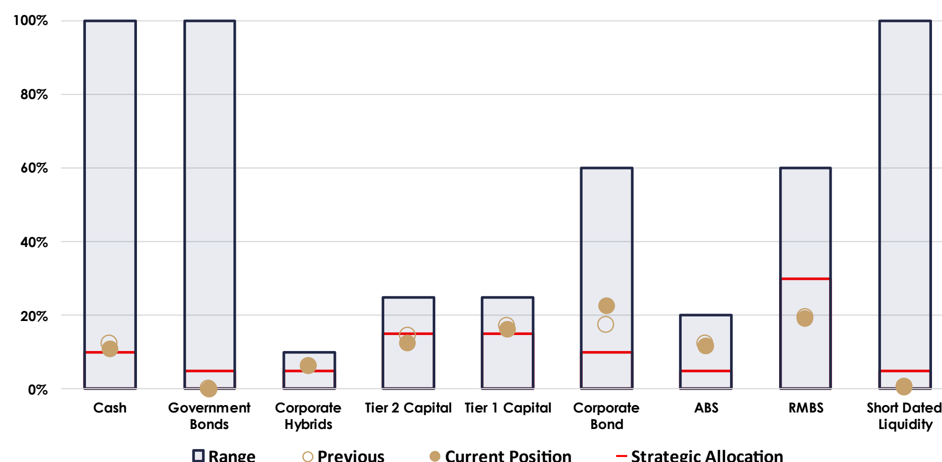
* Past performance is not indicative of future performance. *Ordinary units Inception 26 September 2012. Wholesale units Inception 2 October 2013.

FUND STATISTICS

Running Yield	6.19%
Yield to Maturity	7.89%
Volatility†	2.67%
Interest rate duration	0.85
Credit duration	3.09
Average Credit Rating	BBB+
Number of positions	366
Average position exposure	0.13%
Worst Month*	-1.99%
Best Month*	2.09%
Sharpe ratio∂	2.01

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

SECTOR ALLOCATION



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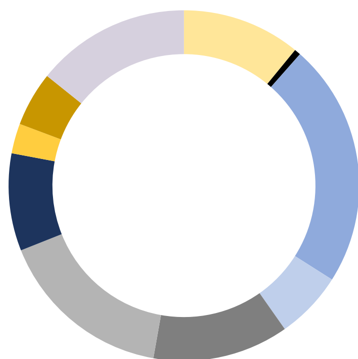
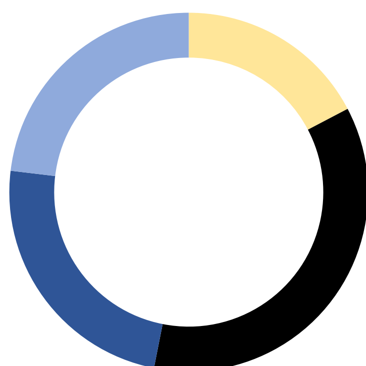
PORTFOLIO COMPOSITION



- Cash (10.93%)
- Commercial Paper (0.58%)
- Government Bonds (0.00%)
- Corporate Bond (22.49%)
- Corporate Hybrids (6.25%)
- Tier 2 Capital (12.54%)
- Tier 1 Capital (16.19%)
- ABS Public (8.98%)
- ABS Private (2.76%)
- RMBS Private (5.03%)
- RMBS Public (14.25%)

MATURITY PROFILE



- At Call to 6 Months (17.32%)
- 6 Months to 3 Years (35.79%)
- 3 Years to 5 Years (23.80%)
- 5 Years to 10 Years (23.10%)
- 10 Years + (0.00%)

FUND UPDATE

Cash and Short-Term Liquidity Weighting: ↓ The allocation to highly liquid assets (cash, commercial paper and government bonds) decreased from 13.03% to 11.51%. This mainly reflected higher allocations to corporate bonds which was partly offset by lower allocations to T2 capital and T1 capital.

Corporate & Subordinated Debt Allocation: ↑ Weighting to corporate bonds and subordinated debt (corporate hybrids and T2 capital) increased from 38.09% to 41.28%. Global credit markets rallied strongly over the month - in sympathy with government bond yields - with notable outperformance from T1 and T2 capital. Domestically, credit spreads also tightened but underperformed global credit markets. This saw the fund take some profits from EUR/USD T2 capital and increase allocations to AUD corporate bonds. Fund performance also benefited from the buyback of our high conviction position in Scentre Group corporate hybrids which were tendered at a 6% premium. Primary issuance in November moderated compared with the heavy issuance month observed in October. Notable new deals include senior bonds from NAB, Westpac, Suncorp and Macquarie; T2 capital from Westpac; and a corporate hybrid from APA Group.

Interest Rate Duration Position: ↓ IRD positioning decreased from 1.21 to 0.85 years. Market moves in the government bond sector reflected the macroeconomic data releases and central bank rhetoric. Soft unemployment and CPI prints contributed to significant rally in the US. European inflation data also pointed to softening conditions. Unsurprisingly, the FOMC and BoE kept cash rates on hold while the RBA raised rates narrowing the gap. Market expectations priced in rate cuts globally in 2024 and the Australian terminal rate was wound down to 4.41%. Consequently, the US and AUS 10-year bonds rallied 56 and 49 basis points respectively. And as such, the portfolio IRD was wound down to reflect these conditions.

Residential Mortgage-Backed Securities (RMBS): ↓ Weighting to RMBS securities decreased from 19.62% to 19.28% over the month. Structured credit markets continued to rally over the course of November, driven by both a widespread rally in credit markets and supply constraints as dealflow is limited into year end. New transactions in primary markets remain substantially overbid, while secondary markets continue to trade very tight relative to primary markets into year end, with very limited stock remaining on dealer inventory sheets. With respect to market performance, Prime arrears as reported by S&P's SPIN index for October remained in line at 0.92%. Nonconforming arrears also improved 16bps to 3.70%. Both results remain very strong in comparison to both market expectations and historic index levels.

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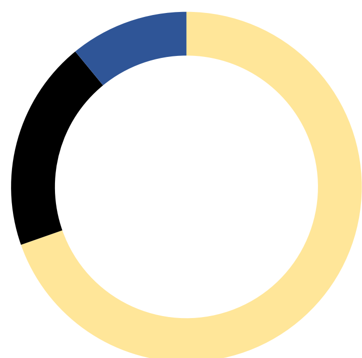
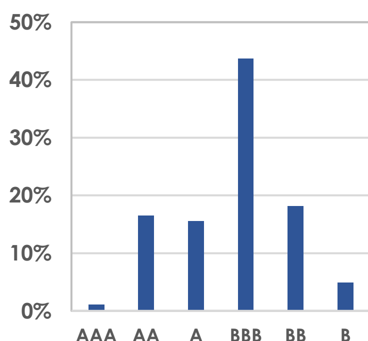
ISSUER DOMICILE



- Australian/NZ Domiciled Issuer (69.63%)
- Foreign Domicilied Issuer (19.44%)
- Cash (10.93%)

CREDIT QUALITY



PORTFOLIO ESG RISK LIMITS

Sector	Portfolio Exposure	Portfolio Limit
Fossil Fuels	3.69%	10%
Non-Renewable & Nuclear Energy	0%	10%
Alcohol	0.22%	10%
Gambling	0.14%	10%

Additional Tier 1 (AT1) Exposures: ↓ Weighting to T1 capital decreased from 17.03% to 16.19%. Global AT1's have been the clear outperformers in November as well as the start of December. The fund took profits into the strength, but maintains a strategic overweight to global AT1's as valuations continue to remain attractive. Fund performance in December will also benefit from S&P's upgrade of Deutsche Bank, where we hold high conviction positions across both T1 and T2 capital. In terms of new issuance, following UBS' bumper USD$3.5B deal in early November, we saw new deals from Barclay's and Banco Santander. Domestically, Westpac issued its Capital notes 10 (WBCPM).

Asset Backed Securities (ABS): ↓ ABS allocation decreased from 12.24% to 11.74%. Each of the ABS exposures within the fund continue to perform in line with expectations. These assets are typically very short dated, continue to offer healthy yields and remain highly sought after by market participants.

Targeted risk across the Fund: ↓ Targeted portfolio risk decreased from 2.90% to 2.64%. This reflected the contribution of lower interest rate duration (from 1.21 years to 0.85 years) and lower credit duration (from 3.17 years to 3.09 years). The fund remains compliant with the Portfolio ESG risk limits.

FUND OUTLOOK

Global investment grade spreads rallied over the month. The ICE BofA BBB US Corporate Index Option-Adjusted spread of 1.39% at month end is relatively tight by historical standards. This is unusual given the outlook for below-trend growth in the coming years and reflects a strong sense of relief that inflation now appears to be better controlled than just months ago. Central banks are also expected to cushion adverse developments. In recent decades, spreads in this market have only been sustainably lower during periods like the lead-up to the Russian financial crisis (1998), during what seemed to be the golden period of the Greenspan era (2004-2006) and in the year following the Trump election (2017) where significant stimulus was added to an economy functioning close to full capacity already.

Corporate credit markets remain captive to the projected actions of central banks which took a significant dovish turn over the month. The increased likelihood that we are at the top of this rate cycle in key markets created a strong rally. Valuations in credit are now more challenged in absolute terms, but remain reasonable when compared to equities. One clear risk to markets at present is a re-emergence of concerns relating to inflation stickiness. Another is a downside economic development, possibly through a sharp contraction in new credit creation. An alternative scenario of an ongoing rally is possible if core inflation should fall more quickly than expected without an associated economic crisis.

Structured credit markets also rallied. Part of this relates to reduced supply heading into year-end. However, we note that issuance by non-banks is increasing again as they regain market share following a period of intense competition for prime mortgages amongst the banks that has now subsided.

PLATFORM AVAILABILITY

- Australian Money Market (Retail Units)
- BT Wrap
- BT Panorama
- Credit Suisse
- Crestone
- First Wrap
- Hub24
- Macquarie Wrap
- Mason Stevens
- MLC Navigator/Wrap
- Netwealth
- Powerwrap
- Praemium
- uXchange
- Xplore Wealth
- mFund: RLM03

OTHER FUND DETAILS

Responsible Entity: One Managed Investment Funds Ltd

Custodian: State Street Australia Limited

Unit Pricing and Unit Price History: https://www.realminvestments.com.au/ourproducts/Realm-high-income-fund/

The typical dynamic into year end sees investors seeking to re-invest paydowns from public securities into a market with next to no primary activity. This should support prices through to the new year. Arrears performance remains well behaved in the circumstances. With housing prices reaching new highs, loss exposure is presently minimal in RMBS.

Levered Loan prices continued to trade sluggishly to larger markets but also ground higher. The market is seeing balanced two-way flow amongst higher quality issuers and is benefiting from a strong CLO creation pipeline. The more dovish rate path expectation from central banks has seen a large number of issuers enter the market and stronger bidding as the deals are priced. Demand for CLOs is strongest amongst structures which are close to the commencement of the amortisation period. Top tier managers and high quality pools have outperformed. Primary issuance of mezzanine tranches has attracted more interest with the improved credit outlook and rally in loan prices. The new issuance pipeline looks strong, with the US market remaining active through to the end of the year as issuers look to benefit from the better market tone.

Bond markets rallied along with risk markets, once again demonstrating the powerful influence which monetary policy continues to exert on asset pricing. This correlated rally also reflects the ongoing outsized role of inflation expectations on market pricing at this time. Recent economic developments suggest a lower rate path can bring inflation to target levels within a reasonable timeframe.

The portfolio continues to hold above average risk levels. Whilst valuations have become less compelling for market segments as a whole, we continue to hold elevated risk exposures given the portfolio is concentrated into individual positions that continue to offer favourable opportunities.

Value can still be found in USD and EUR regulatory capital although the total weighting has been wound back slightly as spreads rallied. We remain close to our upper bound in foreign issuer exposure where the majority of our positions relate to regulatory capital of systemically important banks or large insurers whose balance sheet metrics are very strong.

As foreign positions are concentrated into offshore financial institutions, our corporate exposures are mostly invested into an idiosyncratic mix of domestic companies in AUD. In each case, spreads on offer are wide to comparable alternatives for reasons we are comfortable with. This includes situations where spreads on bonds issued in foreign currency trade manifestly wider than domestic alternatives from the same obligor.

Within structured credit, where total weights are below strategic levels overall, the portfolio remains overweight ABS. This reflects the shift in lending activity towards auto and equipment finance amongst non-banks. Arrears rates for RMBS remain stable and recent research from the RBA indicates that overall housing credit quality remains strong. The majority of the RMBS book is held in bank issued and conforming debt. The potential for permanent losses in this segment of the portfolio remains remote. Exposures to CLOs are a small part of the portfolio.

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Portfolio IRD was reduced to 0.85yrs as Australian and US 10-year bond yields rallied strongly. This remains towards the low end of our 0-5yr allowable mandate range and is slightly below the historical average. We are also maintaining material macro hedges via equity indices and single-name derivatives, which are screening as expensive relative to credit.

The portfolio's traded margin has narrowed as spreads have rallied. It remains historically wide and comes with limited default risk. Portfolio credit quality is strong at BBB+ with sub-IG exposures concentrated into regulatory capital of money center banks and structured credit capable of withstanding significant shocks. Given the credit quality of our exposures and a current yield-to-maturity of 7.9%, the portfolio has excellent forward-looking reward to risk characteristics. Bond and equity exposures will also provide meaningful downside protection in the event of a significant adverse development.

MARKET DEVELOPMENTS

Markets displayed strong pro-risk sentiment following a softening of inflation concerns. Bond yields moved sharply downward with US 10s rallying close to 60bps. Of this, breakeven inflation fell by approximately 20bps and movements in real yield represented the balance of ~40bps. The VIX fell from 18 to 13, a level not seen since pre-Covid and low by historical standards in any case. Credit synthetics rallied. CDX IG is trading at levels which have only been lower during periods like those following the Trump led fiscal stimulus in 2017 and during the period of peak monetary stimulus in 2021. Most equity markets performed strongly with the S&P500 up nearly 9%. In contrast, the Chinese market fell. Some of the safe haven premium for the USD unwound on the increased appetite for risk. The DXY fell nearly 3%. AUD rose over 4% against USD, finishing the month at close to 66 cents. Despite the outbreak of violence in the Middle East, ongoing production cuts by OPEC, and a weaker USD, WTI fell by almost 5%.

OTHER DEVELOPMENTS

US economic activity moderated. Although the 2nd estimate for Q3 GDP came in slightly higher than expectations at 5.2% saar, retail sales (ex auto), core durable goods, housing starts and the Beige Book all pointed to slowing economic activity and a cooling labour market. Productivity surprised to the upside. Housing prices rose 6.1% over the year. The ISM PMI figures point to a rapidly declining level of manufacturing output and an ongoing level of activity in the services sector which is consistent with modest economic growth. Payroll growth materially underperformed expectations (150k vs 180k) and unemployment rose a notch to 3.9%. Hourly earnings rose by less than expected. The disinflationary impulse was supported by a core inflation reading of 0.2% during the month, slightly lower than expected. PPI figures showed a similar pattern.

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The Fed held rates still in the November and December meetings. They note that lower demand for loans and increased lending standards will contribute to a slowing economy. The banking system is considered to be resilient. The updated Statement of Economic Projections released with the December meeting surprised the market with expectations for 3 rate cuts in 2024.

The US political situation is threatening the supply of additional funding to support the effort in Ukraine. President Biden's meeting with Chinese President Xi resulted in a restoration of direct contact between the armed forces and an agreement for China to curb the production of key ingredients for the formulation of fentanyl.

The Australian economy also slowed. The manufacturing and services PMIs all point to an economy which is contracting quite rapidly. The NAB Business Confidence index moved into negative territory again and the related survey results revealed softer inflation outcomes. These were supported by a monthly inflation reading which, at 4.9% yoy, was lower than the expected 5.2%. Wages rose a relatively modest 1.3% qoq in Q3. Retail spending remained robust in nominal terms but the Westpac Consumer Confidence index fell over the month and remained in deeply pessimistic territory. With job advertisements falling and job creation arising largely via part-time positions, the outlook for wages suggests services inflation will be contained.

The RBA raised rates in November, by 0.25% to 4.35%, as it became uncomfortable with the projected time required to return inflation to the target band. Productivity remains a key uncertainty and needs to rise back to recent trends for current wage growth rates to be consistent with target inflation. The RBA kept rates unchanged in December but retained their data-dependent posture. Markets envisage that the RBA has completed its hikes for this cycle. The RBA points out that, whilst mortgage interest payments have increased, most households remain in sound financial condition. The total debt servicing burden is lower than the prior peak due to a lower level of personal debt outstanding.

Economic statistics from China were generally strong. Loan growth, retail sales and industrial production were all higher than expected. GDP for Q3 was reported at 4.9% yoy, comfortably ahead of expectations of 4.4%. These readings were somewhat at odds with official PMI figures suggesting the economy is hardly growing. Ongoing difficulties in the property sector continue to adversely affect investor confidence. Property investment is 9.1% lower on the year (YTD). Foreign direct investment is also 9.4% lower yoy (YTD). A fiscal stimulus of 0.8% of GDP was announced for disaster relief and infrastructure, which contributed to the ongoing strength in iron ore prices. The PBoC left prime rates unchanged. Moody's downgraded the outlook for China's sovereign debt to A1(neg) citing the likelihood of support required for local and regional governments, as well as for state-owned enterprises.

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Europe is slowing. Retail sales and industrial production all fell by more than expected. The PMIs suggest the economy is contracting. Unemployment was higher than expected at 6.5%. Given these outcomes, it was consistent for core inflation to undershoot expectations (3.6% yoy vs 3.9% expected). The ECB did not meet in November but kept rates unchanged in December. It intends to slowly wind down the pandemic emergency purchase program from H2 2024. Although the market is pricing peak cash rates for this cycle, President Lagarde would not be drawn on the timing for potential rate cuts. The BoE kept rates unchanged in November and December although the bias amongst the decision makers was for higher rates.

The German Constitutional Court has ruled that certain fiscal initiatives outside of the official budget, relating to climate change spending and industry support, are not legal and should be subject to existing limits. Approximately EUR 60bn of proposed expenditure is now uncertain. Similarly to the US, Europe’s funding commitment to Ukraine is becoming more unclear. Hungary recently blocked a EUR50bn funding package, but removed itself from discussions about accession.

Speculation continues to surround decisions relating to the BoJ ending its negative interest rate policy and abandoning its efforts to directly influence the trading band of the key 10 year rate. Moves in that direction were set back slightly with a core inflation reading of 2.9% yoy, marginally below expectations of 3%. PPI was -0.4% MoM suggesting limited inflationary pressure in the production pipeline.

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