REALM HIGH INCOME FUND

REALM INVESTMENT HOUSE

OCTOBER 2022

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 $1.38 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	0.32%	0.31%	0.22%
3 Month	-1.05%	-1.00%	0.55%
6 Months	-1.22%	-1.06%	0.75%
1 Year	-2.03%	-1.66%	0.80%
3 Years p.a	1.62%	2.04%	0.44%
5 Years p.a	2.35%	2.78%	0.82%
10 Years p.a	3.95%	#N/A	1.49%
Since Inception p.a*	3.97%	3.92%	1.51%

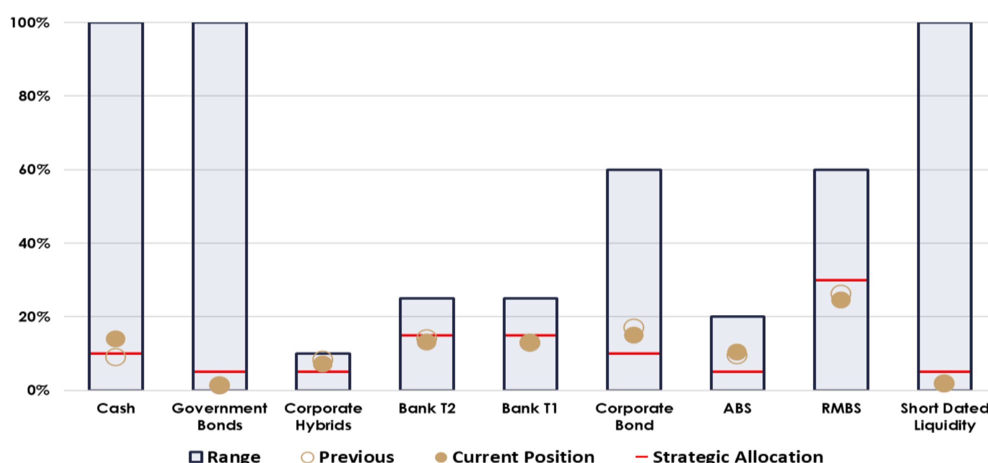
* Past performance is not indicative of future performance. *Ordinary units Inception 26 September 2012. Wholesale units Inception 2 October 2013.

FUND STATISTICS

Running Yield	5.24%
Yield to Maturity	6.84%
Volatility†	2.47%
Interest rate duration	1.17
Credit duration	3.30
Average Credit Rating	BBB
Number of positions	316
Average position exposure	0.18%
Worst Month*	-1.99%
Best Month*	1.94%
Sharpe ratio∂	2.00

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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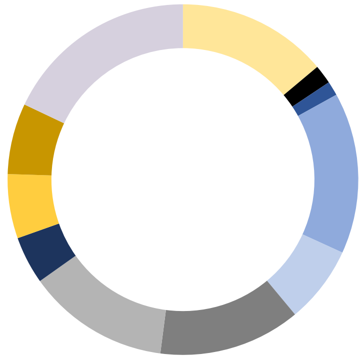
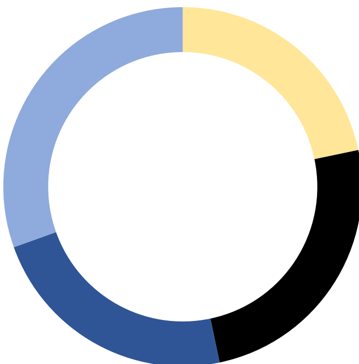
PORTFOLIO COMPOSITION



- Cash (13.89%)
- Commercial Paper (1.75%)
- Government Bonds (1.32%)
- Corporate Bond (14.88%)
- Corporate Hybrids (7.13%)
- Bank T2 (13.10%)
- Bank T1 (13.12%)
- ABS Public (4.40%)
- ABS Private (5.93%)
- RMBS Private (6.54%)
- RMBS Public (17.96%)

MATURITY PROFILE



- At Call to 6 Months (21.72%)
- 6 Months to 3 Years (24.99%)
- 3 Years to 5 Years (22.83%)
- 5 Years to 10 Years (30.47%)
- 10 Years + (0.00%)

FUND UPDATE

Cash and Short-Term Liquidity Weighting: ↑ The allocation to highly liquid assets (cash, commercial paper and government bonds) increased from 12.05% to 16.96%. This largely reflected lower allocations to corporate bonds and subordinated debt, and both public RMBS and ABS; partly offset by increased allocations to ABS Private.

Corporate & Subordinated Debt Allocation: ↓ Weighting to corporate bonds and subordinated debt (corporate hybrids and bank T2) decreased from 39.46% to 35.11%. Global credit spreads continued to sell-off in the first half of October, breaching YTD wides again, before closing firmer for the month. The second half was supported in part by some market stability as systemic concerns over the UK bond market and rumours of a Credit Suisse failure subsided. Domestically, credit was resilient in the first half as global credit sold-off, providing the catalyst for us to reduce allocations to AUD corporate bonds & sub-debt. This was well timed as new bank senior and T2 issuance in the second half resulted in domestic credit spreads gapping wider towards month end. This included ANZ's senior unsecured notes and CBA's T2, which priced respectively 15bps and 30bps wider than the secondary curves. T2 performance deteriorated further in November as APRA published a letter highlighting their concerns around uneconomic calls in capital securities (T2 and AT1).

Interest Rate Duration Position: ↓ IRD positioning decreased from 1.22 to 1.17 years. Government bond volatility remained elevated through the month of October – with the US bond market being more volatile than our domestic market. The political resignation of Liz Truss in the UK contributed to global market sentiment, with the markets reacting positively to the appointment of Rishi Sunak as the UK PM. The major surprise domestically was the Q3 CPI outcome, which prompted an upward revision to CPI and terminal cash rate forecasts. Global central bank rhetoric was more balanced rather than for a pivot and as such, our positioning was influenced by the real yields that were on offer – favouring US government bonds over domestic.

Residential Mortgage-Backed Securities (RMBS): ↓ Weighting to RMBS securities decreased from 26.24% to 24.5% over the month. Public structured credit markets traded relatively flat in October, with new supply remaining limited as credit spreads remained wide. Issuers continue to opt to increase private funding capacity rather than issue into the public market volatility. Secondary markets remain active with offshore investors continuing to probe markets for liquidity, particularly from higher quality assets within the senior parts of the capital structure (AAA rated). Middle mezzanine markets (A/BBB rated) and junior mezzanine (Sub investment grade) remain wide in comparison to historic yields, and continue to display good relative value against other market sectors.

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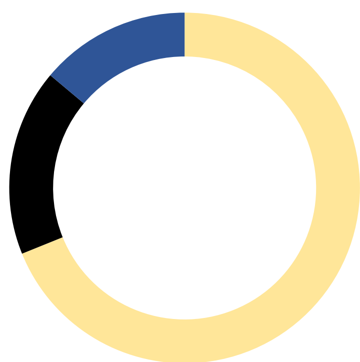
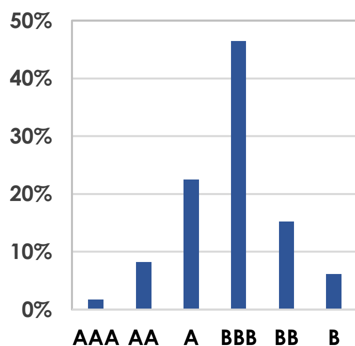
ISSUER DOMICILE



- Australian/NZ Domiciled Issuer (68.89%)
- Foreign Domicilied Issuer (17.23%)
- Cash (13.89%)

CREDIT QUALITY



PORTFOLIO ESG RISK LIMITS

Sector	Portfolio Exposure	Portfolio Limit
Fossil Fuels	5.82%	10%
Non-Renewable & Nuclear Energy	0%	10%
Alcohol	0.16%	10%
Gambling	0.08%	10%

Additional Tier 1 (AT1) Exposures: ↑AT1 exposure increased modestly from 12.83% to 13.12%. Our AT1 book comprises largely of offshore securities as domestic listed AT1's continue to look expensive in a global context. Despite the richness, the retail market continues to support ASX listed AT1's with CBA and BOQ launching new deals for refinancing purposes.

Asset Backed Securities (ABS): ↑ ABS allocation increased from 9.42% to 10.33% . Each of the ABS exposures within the fund continue to perform well, with shorter duration assets limiting the impact of weaker credit markets, which makes them highly sought by the market and well bid.

Targeted risk across the Fund: ↓ Targeted portfolio risk declined from 2.86% to 2.73%. This reflected higher cash holdings as well as a reduction to both credit duration (from 3.6 years to 3.3 years) and interest rate duration (from 1.22 years to 1.17 years). The fund remains compliant with the Portfolio ESG risk limits.

MARKET OUTLOOK

Markets recovered some of their poise following the market dislocation associated with the failed Trussonomics experiment. Equities generally finished firmer, although the HK and Chinese markets did not respond well to the confirmation that the Chinese Communist Party had appointed President Xi to a 3rd term. The composition of his Standing Committee suggested a strong ongoing commitment to zero-covid strategies and his common prosperity agenda.

Whilst the US reporting season has produced some earnings downgrades, these have not been as much as feared in aggregate. The VIX declined, albeit after a solid jump mid-month as the US CPI proved much stronger than expected. The USD soared and this sent the AUD towards 62 cents, a level last seen during the acute phase of the covid affected markets of 2020.

The RBA somewhat surprised the market by deciding to raise rates by 25bps instead of by the 50bps step it had taken in four prior meetings, electing to take a more patient approach. This contributed to Australian bonds outperforming the US. At a time when bad economic news produces favourable market reactions, the outperformance of Australian bonds was further assisted when the flash PMI readings suggested that the global economy had cooled at a surprisingly quick rate. This view gained further traction when the US Q3 GDP figures were released and showed domestic activity had softened. A surprisingly high CPI print in Australia did not disturb the Australian bond market, nor did a weak employment outcome. The Chalmers Federal Budget was received without much disruption.

Whilst credit markets initially benefited from some return to normalcy in the UK, the combination of increased concerns for financial stability and market liquidity this created, together with the shock of another strong US CPI outcome, meant spreads generally widened over the month. Australian credit underperformed as the supply of bank debt weighed. Ongoing selling which was related to margin calls for the UK market dislocation also contributed, although these were reasonably well absorbed.

PLATFORM AVAILABILITY

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

OTHER FUND DETAILS

Responsible Entity: One Managed Investment Funds Ltd
Custodian: JP Morgan
Unit Pricing and Unit Price History: https://www.realminvestments.com.au/ourproducts/Realm-high-income-fund/

Australian housing prices continue to weaken as borrowing capacity is increasingly constrained. However, with employment levels so elevated, and the RBA's and Treasury's forecasts for Australia to avoid recession, impairment experience is expected to be very modest when it emerges. Nonetheless, CLO spreads have widened as the outlook for levered loans is more tenuous and this brought Australian structured spreads wider.

The market dislocation in the UK brought financial stability concerns to the fore. Market conditions had already shown signs of skittishness as liquidity conditions deteriorated, partly due to the run-off of some central bank balance sheets, and partly due to a deteriorating economic outlook. This contributed to fund manager positioning which is amongst the most bearish in their history and dealer inventory being heavily de-risked. For example, the cash holdings of equity funds are at 20-year highs which is materially at odds with economic estimates inferring a shallow recession in 2023 for some countries.

For its part, the RBA believes that the economy can be slowed without causing financial instability or a recession. However, whereas once central banks saw no trade-off between controlling inflation and long-term economic growth potential, they now more openly discuss a trade-off emerging with financial stability. Indeed, as the month ended, some Fed officials broke with a long period of single-minded hawkish conditioning of market and spoke of the need to consider such risks. Whilst the successful formation of a new government in Italy contributed to a narrowing of the premium paid to Bunds, fragmentation risks are never far from the mind of the ECB either.

Evidence is now emerging that labour markets are softening. Vacancies in the US are declining. Australian employment grew by only 900 people in September. Inflation expectations remained well anchored which augurs well for containing wage growth to reasonable levels.

Confidence has weakened. The latest NAB Business Survey showed that business confidence had fallen to below zero and consumer confidence is below GFC levels. Further afield, the Chinese economy continued to be affected by the zero-covid measures and hampered by issues within its enormous property sector. US homebuilders are extremely bearish.

Gas storages in Europe, supported by strong LNG exports from the US and weak Chinese demand, managed to reach virtually full capacity. Spot gas prices even went negative for a short period as LNG imports could not be distributed efficiently. Not quite the scenario which had been feared! Also, Russian troops were performing poorly and ceding territory.

These matters appear to have contributed to some equivocation from the ECB which, although raising rates by 75bps, became unclear about whether future rate rises would also be of this magnitude. The Bank of Canada surprised the market with a smaller rate rise of 50bps, lower than the 75bps that many had anticipated.

REALM INVESTMENT HOUSE CONTACTS

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Nonetheless, services inflation remains elevated and the outlook for household consumption remains uncertain. Geopolitical risks remain elevated and, during the month, OPEC opportunistically determined to curtail production to support prices.

We view the current market circumstances as one providing pockets where an unusually high level of risk aversion premium is available.

We retain a level of risk bearing towards the upper end of our general practices. The European market is particularly dislocated and we prefer large bank subordinated exposures. These can withstand truly historic levels of economic distress. Australian sourced credit exposures issued in USD and EUR are also providing far better spreads than found domestically in some cases. We retain strong liquidity levels. We have added protective buffers which will serve to offset mark to market losses in the event another dislocation emerges. We have reduced nominal bond duration as the term structure flattens. Our exposures to private structured credit are now close to optimal levels.

Our sub-investment grade exposures are concentrated into public RMBS and bank capital. These can withstand a GFC-style event and more.

We believe a well-diversified BBB-rated portfolio with moderate sensitivity to credit spreads and low default exposure appears compelling for medium-term investors when accompanied with a Yield to Maturity of approximately 7% per annum.

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