REALM SHORT TERM INCOME FUND

REALM INVESTMENT HOUSE

MAY 2022

FUND OBJECTIVE

The Realm Short Term Income Fund seeks to produce a return (net of fees) that exceeds the total return of the RBA Overnight Cash Rate by 1.50%-2.00% p.a. over rolling three-year periods.

FUND DETAILS

Distribution Frequency: Monthly

Liquidity: Daily

Buy/Sell: 0.00% / 0.00%

Direct Minimum Investment:

Ordinary Units - $25,000

mFunds Units - $25,000

Inception Date: 21.12.2017

Fund size: AUD $555 million

APIR Codes:

Ordinary Units - OMF3725AU

mFunds Units - OMF8160AU

Management Fees (Net of GST):

Ordinary Units – 0.3075% mFunds Units – 0.3634%

NET PERFORMANCE

Period	Short Term Income Fund	RBA Cash Rate Return
1 Month	0.09%	0.03%
3 Month	-0.31%	0.04%
1 Year	0.67%	0.12%
2 Year	1.78%	0.14%
3 Year	1.97%	0.34%
4 Year	2.24%	0.63%
Since Inception*	2.29%	0.72%

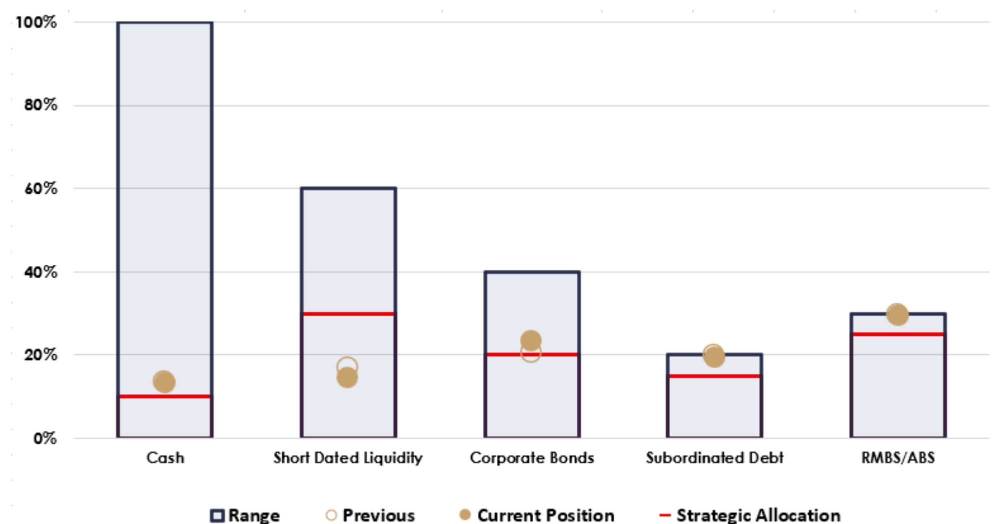
*Past performance is not indicative of future performance. Inception date is 21 December 2017.

FUND STATISTICS

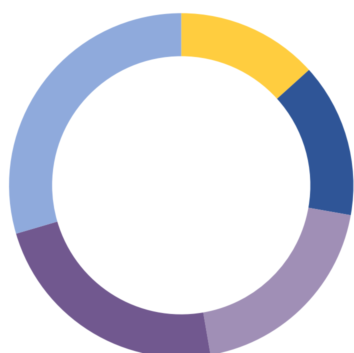
Running Yield	2.63%
Yield to Maturity	2.62%
Volatility†	0.30%
Interest rate duration	0.10
Credit duration	1.48
Average Credit Rating	A
Number of positions	164
Average position exposure	0.44%
Worst Month*	-0.26%
Best Month*	0.34%
Sharpe ratio∂	5.19

Calculated on Ordinary Units unless otherwise stated. *Since Inception 21 December 2017.
†Trailing 12 Months Calculated on Daily observations. ∂Since Inception Calculated on Daily observations

SECTOR ALLOCATION

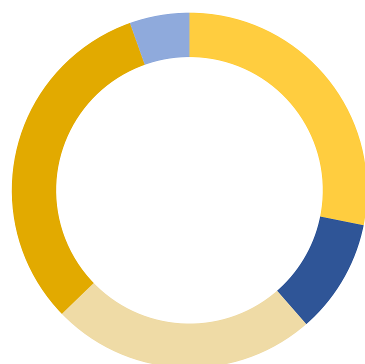


PORTFOLIO COMPOSITION



- Cash (13.31%)
- Short Dated Liquidity (14.47%)
- Sub Debt (19.50%)
- Corporate Bond (23.18%)
- RMBS & ABS (29.54%)

MATURITY PROFILE



- At Call to 6 Months (28.15%)
- 6 Months to 1 Years (10.43%)
- 1 Years to 2 Years (24.17%)
- 2 Years to 3 Years (31.81%)
- 3 Years to 3.5 Years (5.44%)

FUND UPDATE

Cash and Short-Term Liquidity Weighting: ↓ Cash and Short dated liquidity decreased to 27.78% from 30.28%.

Interest Rate Duration Position: → 0.10 years. The strategy will maintain interest rate duration of approximately 3 months as an average. Having a low IRD number has limited the losses of the fund in May from a continued bond market sell-off. The strategy will, as a rule, only takes modest interest rate risk.

Corporate & Subordinated Debt Allocation: ↑ Increased to 42.68% from 40.15%. Additions within the sector were skewed to Subordinated debt and towards optimising short dated liquidity. Corporate bonds continue to present modest relative value over bank senior bonds; however, this value is eroding as bank senior bonds are repricing wider. Over the month, short dated financial and corporate bonds continued to sell-off, although the momentum moderated. The short, conservative nature of the sector aided in cushioning the market volatility in May.

Residential Mortgage-Backed Securities (RMBS) & ABS:
→ Allocation remained in line with last month at 29.5% as funds remained optimally deployed within the structured credit sector. As at month end, the portfolio maintained an A- average credit rating and a relatively short weighted credit duration of 1.69 years.

Public Structured credit markets continued to be weaker, with credit spreads widening alongside global credit markets. There were several transactions in market over the course of the month; most notable were three transactions issued by regional banks, who returned from being absent in the Australian market for some time.

Average prime arrears levels (SPIN) improved in February by 1 basis point to 0.78%, while non-conforming arrears weakened 4bps to 2.58%. Both data prints remain strong in comparison to historical arrears levels.

Targeted risk across the Fund: ↑ Targeted risk increased to 0.69% from 0.64%, reflecting the optimisation within portfolio limits. Meanwhile, realised standard deviation is at 0.30%. This has risen over the month due to increased volatility in mark to market valuations. The portfolio remains defensively positioned although despite this, the fund has performed relatively well over the last 12 months, delivering 0.67% after fees. This is evidence that the strategy is well designed, delivering a reasonable premium over cash while maintaining a very tight distribution of returns month on month. The fund remains compliant with the portfolio ESG risk limits.

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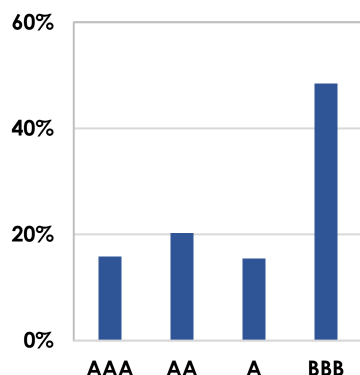
CREDIT QUALITY



PORTFOLIO ESG RISK LIMITS

Sector	Direct Exposure	Direct Limit	Indirect Exposure	Indirect Limit
Fossil Fuels	0.0%	0.0%	0.0%	2.5%
Non-Renewable & Nuclear Energy	0.0%	0.0%	0.0%	2.5%
Alcohol	0.0%	0.0%	0.07%	2.5%
Gambling	0.0%	0.0%	0.0%	2.5%
Mining	0.0%	0.0%	0.0%	2.5%

MARKET OUTLOOK

Financial markets produced mixed outcomes over the month although they were generally characterised by a mid-month bout of risk aversion which was subsequently unwound.

Equity markets returns diverged. The S&P500 moved into bear market territory during the month but recovered to close marginally higher. The Nasdaq fell as much as 8.7% over the month, but recovered to record a loss of 2.1%. The ASX 200 recorded a 3% loss with small capitalisation stocks down 7.1%. Whilst the European STOXX 600 finished marginally lower, the UK FTSE and Japanese Nikkei 225 gained. The VIX was elevated during the month as equity markets weakened, but closed lower into month-end.

Australian 10-year bond yields traded over a 40bps range to finish slightly lower, although 3-year bonds were largely unchanged. Global bond markets rallied during the month as the possibility of a Fed pause in September gained support, but this expectation was subsequently unwound as several FOMC members spoke out against this. Australian bonds benefited temporarily as the Wage Price Index reading came in slightly below expectations. The markets were largely unmoved by the Federal election outcome. The RBA surprised the market by raising rates by a 'business as usual' 25bps in early May, bringing rates to an unusual 0.35% level. Despite a protracted period of communicating that they would be patient and await actual evidence of wage pressure before raising rates, the RBA ultimately decided that enough information was available from business liaison activity. They went on to surprise the market again by lifting rates by 50bps in June, citing upward revisions in inflation outcomes from gas and energy prices which had emerged and ongoing resilience in expected household spending.

The ECB conditioned the market for an end to the negative interest rate policy and asset purchases by Q3. German CPI recorded a 50-year high at 8.7% for the year.

Australian Credit softened along with global markets for much of the month but, unlike global credit markets, did not rally towards the end of the month. A significant volume of senior bank debt was issued which required relatively high concessions to clear, and this saw spreads widen. Subordinated and hybrid debt followed suit. Banks are recording solid lending growth but are issuing at an elevated rate as they seek to refinance their Term Funding Facility borrowings from the RBA. Corporate debt took a lead from the performance of financials and their performance is further constrained by the weight of issuance which had been deferred as markets weakened in recent months. Issuance of structured credit is at the highest year to date volume in 10 years and spreads are also widening as the market is finding better value in foreign markets. Recent issuance has generally arrived in the market substantially pre-placed to limit pricing risks in a weak market. Arrears remain limited, but we are early in the rate tightening cycle. Property prices declined over the month at a national level, led by the major capital cities.

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PLATFORM AVAILABILITY

- Australian Money Market
- AMP North
- BT Panorama
- eXpand
- Firstwrap
- Hub24
- Macquarie Wrap
- MLC Navigator/Wrap
- Netwealth
- Powerwrap
- Praemium
- Rhythm
- mFund code: RLM02

OTHER FUND DETAILS

Responsible Entity: One Managed Investment Funds Ltd

Custodian: Mainstream Fund Services Pty Ltd

Unit Pricing and Unit Price: https://www.realminvestments.com.au/our-products

Commodity markets were driven by two separate themes. China's ongoing lockdowns associated with their zero covid policy have softened spot prices for iron ore, coking coal and industrial metals. Premier Li called for additional stimulus as the Chinese economy appeared at risk of shrinking in Q2. On the other hand, energy and agricultural prices were elevated as supply from Ukraine/Russia was impaired and Europe took additional measures to wean itself off Russian energy. An agreement was struck to reduce Russian oil imports by 90% by end of the year, of which most will be implemented in the near term for seaborne supplies. Russian output is already 1.2mbpd lower and OPEC appears unable to fill the gap despite increased output guidance. A ban on Russian coal imports will be implemented in August. Replacing gas imports will prove more challenging and will require creating infrastructure to receive and distribute seaborne LNG.

The AUD cycled over the month in alignment with global risk appetite, falling below USD 69 cents for a time, a level last seen in July 2020. Differentials in interest rates continued to be a significant driver of exchange rates in key currencies. The USDJPY is at multi-decade highs.

The probability of recession has increased around the world as monetary accommodation is being withdrawn. Australian consumer confidence has been significantly impacted, although actual expenditure remains solid. The Bank of England's GDP estimate for June 2023 is for zero growth. Importantly for the banking system, the legacy of the GFC is a far better capitalised network. The ECB's latest stress tests included a severe scenario involving three consecutive years of negative growth. They conclude the system will readily withstand an even worse outcome. The same could not be said for cryptocurrencies with the TerraUSD stablecoin failing to sustain its linkage. More locally, APRA's investigations suggest there is no systemic issue with unsound mortgage lending as we proceed into a rapid rate tightening cycle.

As energy prices spiked elsewhere, it had been argued that Australia was less affected due to the segmentation of our energy market. This theory was laid to rest when coal supplies to Origin Energy's Eraring Coal-fired power station were interrupted and the effect cascaded through gas and electricity markets more generally. Given the constraints of Australia's energy infrastructure prevent quick restitution, inflation expectations for the coming year rose materially. Differing beliefs on Australia's future energy infrastructure also played out with the cancellation of the AGL Demerger proposal after superannuation fund HESTA sided with the arguments put forward by Grok Venture's (and Atlassian co-founder) Michael Cannon-Brookes, putting the threshold required under the Scheme of Arrangement out of reach.

Elsewhere in the world, evidence continued to mount that peak inflation may be close. Apart from some easing in supply chains, shares of retailers in the US like Walmart and Target were marked down sharply when they were unable to maintain their margins, absorbing inflation rather than fully passing it to consumers.

They also noted that changes in consumption habits which illustrated some measure of financial distress is accumulating. Amazon is looking to release excess warehouse capacity. It still appears that inflation will decline materially in 2023, although central banks are keen to ensure that inflation expectations do not become entrenched in wage-setting behaviour. To that end, it appears that wage settlements in Australia will not keep pace with inflation on the whole but households have significant financial resources to sustain their expenditure for now if they choose to.

There are many significant uncertainties. Failure to secure safe passage for grain from Ukraine could lead to instability in some emerging market economies as food prices escalate and other exporters protect home markets. China's Zero Covid Policy and impaired property market can produce large swings in trade, growth outlook and supply chain inflation. Although under official pressure to lend to support the property market, Chinese banks are concerned about the security of their loans and reportedly circumvent these targets by swapping loans with each other in some cases. China's recent efforts to extend its influence into the Pacific Islands are noteworthy, as were the first actions of our new Foreign Minister. The resilience of household spending and wage negotiations are very large unknowns and could shift the path of interest rates significantly as they develop. Removing policy accommodation so quickly, amidst an environment where forecasting has even less value than usual certainly comes with a high risk of policy error. The task of finding the neutral cash rate within this backdrop, when moving rates at this pace, shares more commonality with guesswork than settled science.

Recent returns have been affected by softer pricing of credit securities as monetary accommodation has been unwound. This is largely an unwinding of the strong support received in 2020 and has very little to do with any decrease in the credit worthiness of the assets. Whilst it had been hard to generate our target returns prior to six months ago, the forward-looking environment is favourable once again to generate returns that are 1.5-2% above RBA Cash. Whilst term deposit rates have been climbing, taking into account market pricing of the expected RBA Cash path, the portfolio will still be expected to produce a meaningful margin over these rates without requiring investors to forgo liquidity.

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