# REALM SHORT TERM INCOME FUND

**JULY 2023**

REALM INVESTMENT HOUSE

## 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 $1.01 billion
**APIR Codes:**
Ordinary Units - OMF3725AU
mFunds Units - OMF8160AU
**Management Costs (Net of GST):**
Ordinary Units – 0.3075%
mFunds Units – 0.3634%

Zenith RECOMMENDED

## NET PERFORMANCE

| Period | Short Term Income Fund | RBA Cash Rate Return |
|---|---|---|
| 1 Month | 0.51% | 0.34% |
| 3 Month | 1.49% | 0.99% |
| 6 Month | 2.84% | 1.84% |
| 1 Year | 4.85% | 3.17% |
| 3 Year p.a | 2.56% | 1.18% |
| 5 Year p.a | 2.63% | 1.12% |
| Since Inception p.a* | 2.64% | 1.16% |

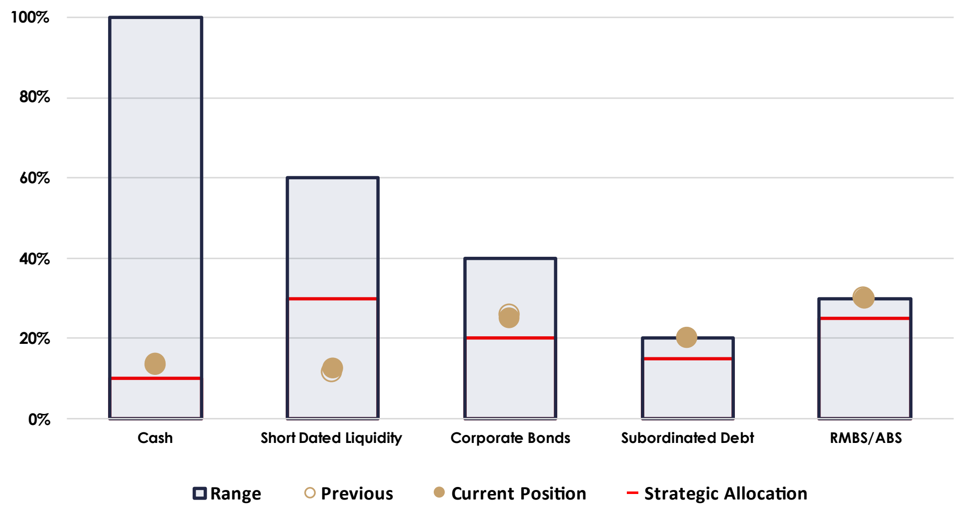
*Past performance is not indicative of future performance. Inception date is 21 December 2017.

## FUND STATISTICS

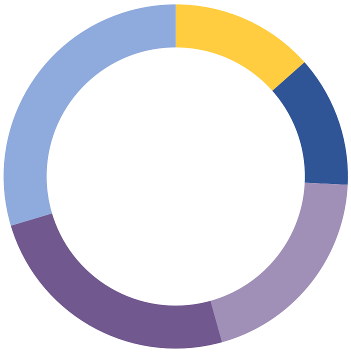
| | |
|---|---|
| Running Yield | 5.57% |
| Yield to Maturity | 6.01% |
| Volatility† | 0.44% |
| Interest rate duration | 0.09 |
| Credit duration | 1.48 |
| Average Credit Rating | A |
| Number of positions | 267 |
| Average position exp. | 0.30% |
| Worst Month* | -0.26% |
| Best Month* | 0.58% |
| Sharpe ratio∂ | 4.40 |

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

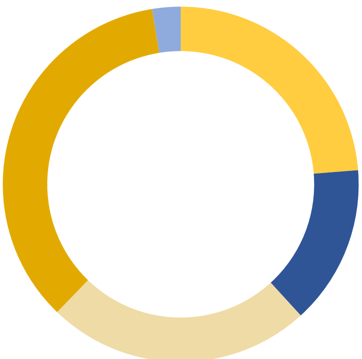


## PORTFOLIO COMPOSITION



- Cash (13.45%)
- Short Dated Liquidity (12.32%)
- Sub Debt (19.90%)
- Corporate Bond (24.72%)
- RMBS & ABS (29.62%)

## MATURITY PROFILE



- At Call to 6 Months (23.73%)
- 6 Months to 1 Years (14.49%)
- 1 Years to 2 Years (24.00%)
- 2 Years to 3 Years (35.21%)
- 3 Years to 3.5 Years (2.57%)

## FUND UPDATE

**Cash and Short-Term Liquidity Weighting:** ↑ Cash and Short dated liquidity increased from 24.45% to 25.77%.

**Interest Rate Duration Position:** → 0.09 years. The strategy will maintain interest rate duration of approximately 3 months as an average. Having a low IRD number limited the realised volatility and losses in the fund from government bond volatility over the month (51 basis point trading range for AU 3-year bonds). The strategy will, as a rule, only take modest interest rate risk.

**Corporate & Subordinated Debt Allocation:** ↑ Decreased from 45.61% to 44.62%. Optimisation within the corporate bond sector was balanced. Corporate bonds, traditionally, present modest relative value over bank senior bonds due to the rating differential; and this relative value was maintained over the month due to relatively stable credit spreads. Corporate bond volatility, albeit small, was driven partly by swap spreads. The short, conservative nature of the sector and diversification aided in cushioning the market volatility over the month.

**Residential Mortgage-Backed Securities (RMBS) & ABS:** → Allocation to structured credit securities remained in line with last month at 29.62%. As at month end, the portfolio maintained an A- average credit rating and a relatively short weighted credit duration of 1.76 years.

Public structured credit market yields began to tighten over the month of July, with reports of a strong offshore bid returning to the market. This was especially prevalent in the senior portions of the capital structure in prime transactions, with the bid tightening credit margins across the sector. Tighter yields continue to make transaction more economic for issuers, leading to a substantial amount of primary deal flow looking to price in markets over the next month, including several regional bank trades, along with both prime and non-conforming RMBS.

With respect to market performance, Prime arrears as reported by S&P's SPIN index improved 3bps over the month of June to 0.97%. Nonconforming arrears also improved, tightening 16bps to 3.47%. Both results remain very strong in comparison to both market expectations and historic index levels.

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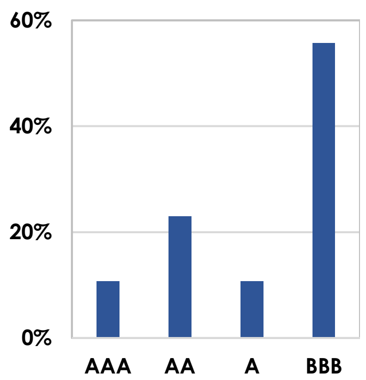
**JULY 2023**

## 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% | 0.15% | 2.5% |
| Gambling | 0.0% | 0.0% | 0.0% | 2.5% |

## 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/realm-short-term-income-fund/

**Targeted risk across the Fund:** ↑ Targeted risk increased from 0.89% to 0.90%, reflecting the increase in market volatility and optimisation within portfolio limits. Meanwhile, realised standard deviation is at 0.44%. This has risen over the short term 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 4.85% 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.

## FUND OUTLOOK

Credit markets remain favourably priced, on a risk adjusted basis, despite having rallied materially since the US regional banking crisis erupted. Spreads continue to reflect a higher-than-average risk aversion as monetary policy settings are restrictive in aggregate and the possibility of recession is elevated.

Hopes of a soft landing in the US and Australia are improving. Staff at the Fed have revised their prior expectations and no longer expect a recession to emerge in the coming year. The RBA continues to expect that inflation can be managed back to the target band within a reasonable timeframe, whilst preserving employment gains.

Energy prices are rising again, which may complicate the inflation outlook. Labour markets remain remarkably tight with many showing only early signs that wage inflation can expect to abate. Pockets of sub-investment grade markets are experiencing a material deterioration of fundamentals associated with a slowing economy and higher interest burden. The upcoming wall of maturity for high yield debt is a source of concern. Issuance of sub-IG corporate debt has been relatively low, as borrowers attempt to strengthen balance sheets, and this is producing scarcity effects which are creating a rally in spreads that cannot be fully attributed to an improving economic backdrop.

The core of the banking systems we invest in remains very sound. An exceptionally favourable issuance of senior debt by US regional Fifth Third Bancorp signalled that concerns in this part of the market are receding despite the outlook for CRE not having improved.

As Australian banks report their earnings and additional arrears activity statistics are released, it is clear that distress amongst mortgagees remains generally well contained. Mortgagees rolling off fixed interest arrangements to higher variable rates are not showing unusual arrears performance. Given the rebound in property prices in recent months, any reasonable forecast for arrears does not produce projected losses within our structured credit exposures that concern us. Indeed, the foreign bid for private and public Australian structured credit has returned.

## REALM INVESTMENT HOUSE CONTACTS

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## PLATFORM AVAILABILITY

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

Portfolio activity remained focused on maximizing expected return within tight boundaries. Australian credit remains adequately priced and the portfolio is providing a well-diversified exposure supported by the unquestionably strong financial system and significant tangible asset backing. Following revisions to the investment parameters disclosed in recently released fund documents, the portfolio will introduce foreign issuers in the coming weeks. This is expected to improve portfolio outcomes by providing more scope to identify mispricing and also deliver greater portfolio diversification.

The possibility of credit losses on the RMBS exposures within the portfolio remains remote. Property prices continue to rise. We anticipate a further rise in arrears but the magnitude is not of the order that raises any concern. The portfolio remains capable of withstanding significant liquidity stress.

The portfolio offers a yield to maturity of close to 6% per annum. With an average credit rating of A, no sub-investment grade exposures and a credit duration of close to 1.5 years, the likelihood of a negative quarterly return is towards the lowest end of the portfolio's history. As the portfolio has negligible interest rate duration, it has also largely avoided any impact from the heightened volatility in bond yields.

## MARKET DEVELOPMENTS

Markets were stronger over July as the peak of the cash rate cycle appears close to hand. Receding concerns for the US regional banking sector and the increasing likelihood of a soft landing helped to draw spreads lower. Equities markets were generally stronger. The VIX finished the month below 14, near lows recorded since the covid period. The index jumped during the month following the release of somewhat hawkish Fed minutes relating to the June meeting. Whilst bond yields subsequently rallied again, they generally finished wider. Notably, the Bank of Japan revised the management of the yield curve control policy relating to 10-year bonds and will allow yields there to trade as high as 1%. Yields rose immediately. As concerns for risk abated, the USD weakened. Whilst this contributed to higher commodity prices (which are quoted in USD), oil prices rose as the global economy remained resilient and industrial commodities benefited from rising expectations for further stimulus in China.

## OTHER DEVELOPMENTS

The Fed hiked in July with the key rate lifted by 25bps to a target range between 5.25% and 5.50%. A soft landing was seen as likelier than recession. A weaker than expected non-farm payrolls figure was reported and well received. The ISM survey and Beige Book point to expectations for normalisation of wage growth. Inflation outcomes were favourable. Used car prices declined and both CPI and PPI readings surprised to the low side. The Advanced GDP estimate for Q2 was 2.4% SAAR which was higher than the 1.8% expected. Consumer sentiment improved and house prices recorded their fourth consecutive positive monthly return.

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Fitch downgraded US sovereign debt to AA+ (stable), matching S&P's rating. This has refocused attention on the lack of sustainability of the US budget trajectory as the interest burden accelerates.

RBA Governor Lowe will depart having contributed to the best employment outcomes Australia has seen for many decades whilst expecting a soft landing. Michele Bulloch's appointment to the role was warmly received. The RBA held rates unchanged, citing the need to be patient to observe incoming data. It held again in August and mentioned evidence of easing labour market conditions. Rent inflation is becoming a complicating factor. The labour force grew by 32.6k jobs vs expectations of 15k and unemployment stayed low at 3.5%. There are limited signs that a wage-inflation spiral will become entrenched. The trimmed mean inflation reading and subsequent PPI were softer than expected. The outlook for consumer spending remains a key source of uncertainty. NAB transaction data suggests nominal spending remains robust yet consumer confidence did not improve materially despite the rate pauses. The NAB business survey continues to suggest that activity will moderate in an orderly manner. The CoreLogic property series recorded its fifth consecutive positive monthly return. Supply-side inflation now appears close to being fully resolved.

High inflation is absent in the Chinese economic setting. The economic performance continues to underwhelm and the preparedness to create targeted stimulus has been announced, avoiding a big bang approach. Some attention is being directed towards the fragility of the financial system which, given its importance to the property market, presents a challenge as the property sector is a drag on growth. The labour market here is weak, with youth unemployment a significant social issue and low wage growth indicating that slack remains. GDP growth expectations for 2023 are being pared back.

The European outlook remains challenging. Core inflation for June accelerated although the PPI reading came in below expectations at -1.9% for the month. The economic growth outlook continues to be for modest growth in the coming year which is likely to avoid recession. The ECB raised rates a further 25bps to bring the Main Refinancing Operations rate to 4.25%. The post meeting communications were decidedly less hawkish.

Although inflation challenges in the UK imply that the Bank of England still has some way to run before concluding its tightening cycle, most other major central banks appear to have reached their terminal rate or will shortly do so. As central bank balance sheets (other than Japan) are being wound down, we expect the possibility of active quantitative tightening will be discussed further. The RBA's holdings of government bonds have a relatively extended maturity schedule making active QT a greater possibility.

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