

# REALM GLOBAL HIGH INCOME FUND AUD

JULY 2024

## FUND OBJECTIVE

The Realm Global High Income Fund AUD is a fixed income strategy, that invests in global asset backed securities, bank-issued securities and corporate bonds. The objective of the Fund is to deliver investors a consistent return (net of fees and gross of franking) of 2.5 - 3.5% over the RBA cash rate through a market cycle.

## FUND DETAILS

### Distribution Frequency:

Monthly

**Liquidity:** Daily

**Buy/Sell:** 0.05% / 0.05%

**Inception Date:** 16.11.2023

**Fund size:** AUD \$76.7 million

**Management Fees (Net of GST):**

0.7175%

**Direct Minimum**

**Investment:**

Ordinary Units - \$25,000



## NET PERFORMANCE

Period	Global High Income Fund AUD	RBA Cash Rate Return
1 Month	1.17%	0.35%
3 Month	3.13%	1.06%
6 Month	6.22%	2.13%
Since Inception	12.75%	3.04%

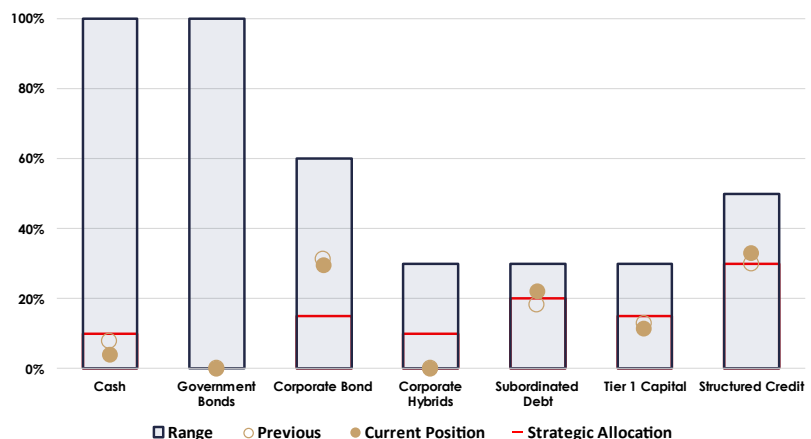
\* Past performance is not indicative of future performance.  
Inception 16 November 2023.

## FUND STATISTICS

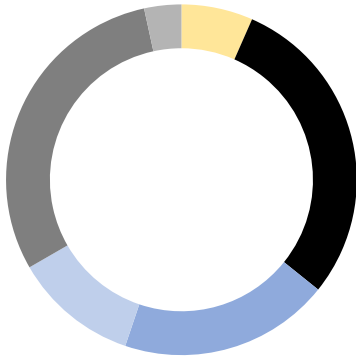
Running Yield	7.23%
Yield to Maturity	7.50%
Volatility†	N/A
Interest rate duration	0.19
Credit duration	4.02
Average Credit Rating	BBB
Number of positions	84
Average position exposure	0.39%
Worst Month*	0.58%
Best Month*	2.22%

†Trailing 12 Months Calculated on Daily observations. \*Since Inception Calculated on Daily observations

## SECTOR ALLOCATION

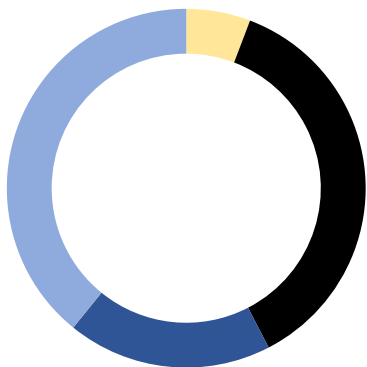


## PORTFOLIO COMPOSITION



- Cash (6.60%)
- Corporate Bond (29.17%)
- Corporate Hybrid (0.00%)
- Subordinated Debt (19.42%)
- Tier 1 Capital (11.49%)
- ABS Public (29.90%)
- ABS Private (3.42%)

## CREDIT DURATION PROFILE



- At Call to 6 Months (5.79%)
- 6 Months to 3 Years (36.61%)
- 3 Years to 5 Years (18.44%)
- 5 Years to 10 Years (39.16%)
- 10 Years + (0.00%)

## FUND UPDATE

**Cash and Short-Term Liquidity:** ↓ The allocation to highly liquid assets (cash and government bonds) decreased from 7.78% to 6.60%. This mainly reflected higher allocations to T2 capital which was slightly offset by lower allocations to Corporates Bonds and T1 Capital. The fund also increased its allocation to ABS Private.

**Corporate Bond, Corporate Hybrids & Subordinated Debt:** ↓ Weighting to corporate bonds, corporate hybrids and subordinated debt decreased from 49.36% to 48.59%. Global credit spreads recovered as concerns eased around France's snap election in June. Notably, European bank T2 capital snapped back strongly, supporting the fund's meaningful re-allocation to the sector. Further investments into European bank T2 capital were made during the month, including in a new offering from ABN AMRO. Corporate issuance resumed globally in July as market sentiment improved.

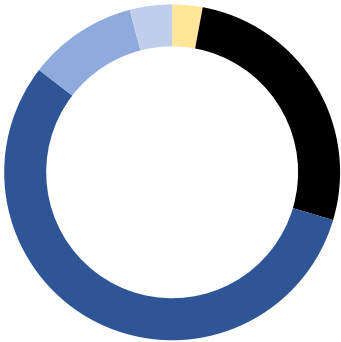
**Tier 1 Capital:** ↓ Weighting to T1 capital reduced from 12.94% to 11.49%. Global T1's rallied over the month in sympathy with French election risk abating and was also supported by solid 2Q24 bank earnings where the fundamental outlook for European banks continues to be positive. This provided the opportunity to take profits after increasing our allocation in the previous month. AT1 issuance continued with deals from Citi, Santander, Bank of Montreal and Wells Fargo, which the fund did not participate in as valuations were rich.

**Structured Credit (ABS/CLO):** ↓ ABS/CLO weighting reduced over the month from 34.70% to 33.32%. CLO spreads continued their path tighter and the fund continued to optimise holdings, particularly to recycle into new issues opportunities if they arose. AAA spreads did edge a little wider at the end of the month, perhaps some indigestion at the sheer quantity of new issue, again largely driven by resets and refinances. US CLO CCC concentrations continue to track at around 5.8% in the US, and in Europe at around 3.9%. The Morningstar LSTA US Leveraged Loan index was 1c higher over the month at 96.60; in Europe the index was up 34c to 97.95 over July. \$82bn of loans priced in July, comprised of 86% repricing/refinances and 12% M&A related, down in size from June, but with the M&A component increasing from 4% in June.

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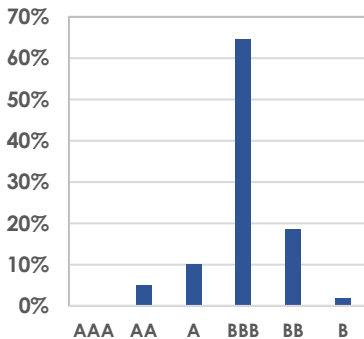
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## GEOGRAPHIC EXPOSURE



- Australian/NZ Domiciled Issuer (2.92%)
- North America Domiciled Issuer (26.67%)
- Europe Domiciled Issuer (55.84%)
- United Kingdom Domiciled Issuer (10.51%)
- Cash (4.06%)

## CREDIT QUALITY



## PORTFOLIO ESG RISK LIMITS

Sector	Portfolio Exposure	Portfolio Limit
Fossil Fuels	1.00%	10%
Non-Renewable & Nuclear Energy	0.00%	10%
Alcohol	0.00%	10%
Gambling	0.00%	10%

**Interest Rate Duration Position:** → IRD positioning remained stable at 0.19 years. The US core inflation softened for the second time in a row, which caused the rates market to bull steepen. Additional dovish commentary from FED chairman Powell supported further fall in yields and an increased expectation of rate cuts by December 2024 – from 45bps to 72bps. Conversely, expectations in Australia were for a higher likelihood of a rate hike; however, the less-than-expected CPI statistics moderated the rhetoric, leading to a domestic rate rally. The Bank of Japan hiked rates by 15 basis points, which caused the Yen carry trade to unravel, while central banks around the world continued to speak in dovish terms. Mid-month volatility was caused by geo-political events including the failed assassination attempt on Trump. US and AUS bond yields ended the month 36bps and 35bps lower respectively. The term premium and relative value on offer from credit instruments outweigh those offered by global government bonds, and as a result, the IRD of the portfolio was maintained at a minimum level.

**Targeted risk across the Fund:** ↓ Targeted portfolio risk decreased from 1.99% to 1.95%. This partially reflected the reduction in T1 capital. Credit duration increased (from 3.74 years to 4.02 years). Interest rate duration decreased slightly over the month (from 0.20 years to 0.19 years).

## FUND OVERVIEW

The Fund benefited from the recovery in spreads following an outcome in the French elections which settled the market. The return of 1.17% exceeded the return on cash of 0.35%. This extends the strong performance of the portfolio since inception where the Fund's return of 12.75% is comfortably ahead of the cash return of 3.06% over the period since 16 November 2023.

There were minor asset allocation shifts over the month. Key positions include a zero weight to corporate hybrids and an underweight to cash. This funded an overweight position in corporate bonds where the portfolio exhibits high credit quality. With an average credit rating of BBB+ the exposures are largely robustly capitalized financials, high quality REIT and infrastructure assets. The portfolio's sub-IG exposures are primarily housed in CLOs managed by top tier investment houses where the risk of permanent capital loss is remote. The portfolio also holds sub-IG AT1 positions in a selection of banks, most of which are systemically important.

Whilst credit markets are generally unattractive in an aggregate sense, the portfolio is concentrated into a selection of names whose prospects are more favourable. The probability of a negative return over a 12-month period is modest given the current yield to maturity of 7.50% and other settings. The Fund remains capable of generating its target return objectives despite tight margins in the market, although the inferred risks from derivative markets suggests near-term drawdowns may be a feature.

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## PLATFORM AVAILABILITY

- Australian Money Market (AMM)
- HUB24
- Netwealth IDPS & Super
- Powerwrap
- Praemium

## 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/our-products/realm-global-high-income-fund/>

## OVERALL DEVELOPMENTS

Investors entered the month in a bullish state, confident that the US would experience a soft landing. Inflation concerns softened and geopolitical matters became the most front-of-mind risk. The outcomes of the French elections calmed markets when the far-right National Rally party came third in a surprising result. Later in the month, Middle East hostilities escalated when a rocket explosion in the Golan Heights risked involving Hezbollah more completely in the conflict. Subsequent assassinations of senior Hezbollah and Hamas leadership has the world waiting for a significant Iranian response.

US President Biden ceded his re-election ambitions in favour of VP Harris and former President Trump survived an assassination attempt. The Harris campaign has proved competitive although her policy positions have yet to be clarified in depth. Her previous policy positions included adding a racial equity element to the Fed's mandate.

The Yen carry trade began to unwind following the BoJ's move to tighten rates. Earnings reports were generally well received. Global banks reported limited signs of credit deterioration on the whole. The strong run for AI-related stocks took breath as the market considered the prospects for securing a suitable return on capex. Consumer facing companies reported ongoing cost of living pressures and weak Chinese demand, including for luxury goods.

## MARKET DEVELOPMENTS

Equities performed well overall with the ASX 200 +4.2% although the Nikkei 225 fell -1.3% as the Yen carry trade began unwinding. Major bond markets generally rallied outside of Japan, where 10 yr bonds closed unchanged at 1.05%. US 10-year Treasuries rallied 35bps to 4.02% on flight to safety from rising tensions in the Middle East and a lower-than-expected borrowing requirement announced by Treasury. Middle-East tensions drove gold prices up (+3.9%) and also the VIX (+4 to 16.4). The 3rd Plenum meeting in China produced no material stimulus measures which disappointed the market as well, sending WTI (-3.4%), Copper (-3.9%) and the AUD (-1.9% vs USD to 65.4) lower. The Yen rallied an enormous +6.8%.

Credit synthetics rallied overall as the outcomes of the French elections eased concerns. Some of these gains were unwound later in the month as weaker European economic outcomes combined with disappointment in the 3rd Plenum and rising geopolitical concerns.

Credit spreads remained tight. The Bloomberg USD Baa Option Adjusted Spread closed unchanged at 1.14%. This remains very tight by historical standards which is attributed to less discriminate buying due to high all-in yields, a Fed commitment to protect against a disorderly slowing of the economy and general optimism for a successful normalization of inflation without any material disruption to growth. The tight spreads make the markets prone to material sell-offs and this was visible in the period following the European Parliamentary elections and, in early August, a surprisingly weak US NFP outcome which followed shortly after the BoJ tightened cash rates.

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The tight market is also visible in the spreads between US BB and BBB-rated corporate bonds which remained stable through the month and are towards the low end of the historical range.

The dispersion of spreads in the high-yield markets remains near historical highs as the prospect of defaults is elevated. Dispersion amongst sub-IG credit spreads is similar to levels during other times of distress like the European fragmentation (2012), distress following the oil price correction (2016) and Covid (2020). Credit concerns are focused on the TMT and healthcare sectors. These concerns do not transfer to the IG rated securities where spreads are tight overall and trade within a narrow range as underlying fundamentals remain sound. Nonetheless, credit derivative markets are anticipating a higher than usual risk of a tail event.

Domestic issuance of public structured credit remains very elevated. This is driven by increased funding of auto and personal loans from non-bank lenders. Additionally, favourable relative pricing between public markets and private warehouse financing has encouraged issuers to bring their lending books to the public markets. Strong demand for IG risk is visible through historically tight spreads (now towards recent QE tightens for BBB-rated notes). The premium between BBB-rated notes and AAA-rated notes is very low.

Demand for CLO's has been strong with spreads for tranches compressing relative to spreads on the underlying loans. Although there has been strong reset and refinance activity as CLO issuers seek to improve returns to equity, net issuance has not been strong enough to satisfy investor demand. Underlying credit quality is supported by loan default rates declining off recent peaks which were not extreme. This is a trend which is likely to continue as cash rates decline. Underlying loans are generally floating-rate and borrowers will service these loans more readily as the Fed easing cycle begins and the European easing cycle continues.

In aggregate, we believe credit markets are tight and offer lower than average value.

## ECONOMIC AND OTHER DEVELOPMENTS

Key Western markets are expected to normalize towards trend growth rates and target inflation levels without undue economic turbulence. Whilst these economies are seeking to reduce inflation by loosening the labour market, China's inflation is very low and faces challenges to their economic growth. Japan's post-Covid wage increases, which have broken from the pattern of near zero movements over the prior 25 years, raises the possibility that it will enter a virtuous cycle of rising wages and prices and help address weak economic growth. Overall, economic surprises were to the negative side over the month and Western central banks are expected to cut rates (further) in the coming months. Services inflation remains sticky.



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The market outlook for the United States is for a gentle moderation in growth which will lead to a further softening in the labour market and inflation normalisation. This is expected to be achieved without experiencing net job losses and the path to a soft landing is supported by commitments from the Fed to protect against sudden downside risk. The market is sensitive to a sudden decline in labour market conditions as employers shift their mentality away from one of labour scarcity, which led to workforce hoarding. For these reasons, a weak headline NFP outcome in early August led to significant market volatility. This was despite a less dire underlying assessment as the figures were affected by one-off transient factors like Hurricane Beryl. Inflation expectations remain well-anchored, and the market is expecting 100bps of easing in cash rates over the rest of 2024.

Consumer sentiment remains weak (UMich 66.4, prior 68.2, expected 68.5) with Republicans far more pessimistic than Democrats. Financial distress is visible via anecdotes like car repossessions rising by 23% over the year. Nonetheless core retail sales produced an upside surprise (ex Auto 0.4% MoM p0.1% e0.1%). Existing home sales remained moribund with limited appetite amongst homeowners to reset their long-dated mortgages to current rates. House prices rose 1% on the month. Corporate activity improved with the ISM Manufacturing and Services PMI readings both higher than last month. The outlook for services is stronger than for manufacturing and price inflation remains a concern. Core durable orders (Non-defense ex-air 1.0% MoM p-0.9% e0.2%) surprised to the upside.

The labour market softened with job growth (NFP 206k p218k e190k), hourly earnings and the unemployment rate (4.1% p4.0 e4.0) all pointing to reduced wage growth rates ahead. The soft NFP result published in August (114k e175k) shocked the market, but Fed speakers played down the details of the headline reading and its influence on the immediate outlook for policy. Core PCE was stronger than anticipated (June 0.2% MoM p0.1% e0.1%).

The Fed left rates unchanged. Commentary from FOMC members welcomed a reduction in observed inflation rates and indicated caution was required as policy settings were adjusted. Their commentary seemed far less dovish than the market path of 100bps of easing for the balance of 2024.

The expected trajectory of the Australian economy is a complex mix of recovering growth, softening inflation and looser labour market conditions. This is possible if labour productivity improves and household spending is supported by higher real wages and positive wealth effects. The RBA has revised its estimates of economic slack in the direction of requiring tighter monetary conditions. The timeline for inflation normalization has been extended. Addressing inflation is challenged by a strong pipeline of infrastructure developments. This draws economic resources away from addressing high housing-related inflation. The markets are pricing a single rate cut for the rest of the year, but RBA commentary is skeptical of this prospect.

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Households remain deeply pessimistic (Westpac Cons. Conf. 82.7 p83.6) as ongoing cost of living and interest rates pressure finances. Early indications are that most of the Stage 3 tax cuts are being saved. Whilst current conditions for business have weakened (NAB Business Conditions 4 p6) the outlook has improved. The PMI releases suggest no growth in activity occurred during the month. Supply of new housing remains impaired as construction costs are elevated and significantly hampering projected profits to developers. Transaction activity remains orderly in the market for existing homes. House prices rose 0.5%. Trimmed Mean inflation for Q2 was better than expected (0.8% p1.0% e0.9%).

The labour market remains tighter than is consistent with returning inflation to the target band. More jobs were created (50.2k p39.5k e20.0k) and drew in higher participation (66.9% p66.8 e66.8). Unemployment is presently at 4.1% and expected to reach 4.5% in 2025.

The RBA kept rates unchanged at 4.35%. Commentary was towards the hawkish side overall. Prior estimates of household spending strength for overseas holidays were understated. As a result, the strength of household spending capacity is greater than previously believed. APRA decided to retain the existing counter cyclical buffer requirements for banks and also serviceability buffers for loans.

In Europe, an ongoing recovery from near zero growth in H2 2023 is expected. However, economic surprises have been particularly negative in recent months. The ECB is expected to cut rates by 50-75bps over the remainder of the year.

Although consumer confidence continues to recover from the lows of September 2022 (UK mini-budget), retail sales remain sluggish (0.1% p-0.2% e0.2%). The PMI readings are consistent with modest growth in services (51.9 p52.8) whilst manufacturing activity is slowing at the same significant rate (45.8 p45.8). Tarriff policies to overcome China's push to export significant amounts of EVs and other products complicates the outlook for Germany. Any generalized trade war would have a significant adverse impact on Europe.

Unemployment was stable at 6.4% (e6.4%), but the flash inflation reading for July was higher than expected (2.9% yoy p2.9% e2.8%).

The ECB kept the deposit rate at 3.75%. Commentary focused on the need for data dependence for future moves and there being no predetermined path.

The UK General Elections saw an overwhelming swing to Labour. Chancellor Reeves identified GBP 22bn of previously undisclosed and unfunded spending. The PMIs are consistent with modest growth. Inflation and labour market conditions were unchanged but consistent with the need for ongoing tight monetary conditions. Nonetheless, sufficient progress towards the inflation goal had been made to convince the majority of BoE members to cut rates to 5% from 5.25%. UK house prices rose by 0.3%.

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China's economic growth is expected to fall to the low side of its "around 5%" target. The proposed composition of this growth, with its significant export component, is likely to be challenged with tariffs. Household consumption and property developers remain impaired. Unlike the West, inflation readings in China are weak and highlight a pattern of over-saving and investment. The 3rd Plenum, historically a key forum to develop and announce significant economic policies, disappointed the market with key pronouncements focusing more on governance reforms which ultimately centralize more power into President Xi.

The official PMIs showed near flat economic conditions (Manufacturing 49.4, Non-manufacturing 50.2). GDP disappointed (Q2 4.7% YoY p5.3% e5.1%). Loan growth and Total Social Financing grew at the slowest rates on record (both 8.1% YoY). Housing prices have fallen -4.5% YoY.

The PBoC has been attempting to support the currency and manage the yield curve. Key interest rates were cut over the month to support the economy. However, long dated yields on government bonds rallied more than desired. The PBoC intervened in bond trading to try and steepen the yield curve, which helps to protect bank profitability. Foreign Direct Investment into China continues to decline and is nearly 30% lower than last year. Examinations on the pattern of trade increasingly suggest geographic segmentation away from Western nations, possibly as a way to circumvent tariffs on direct trade.

China's coastguard ships clashed with Philippine vessels in disputed waters in the South China Sea. President Xi met with President Putin in Kazakhstan where he said the relationship with Russia had unique value.

Japan's key economic goal is to establish a virtuous circle of wage and price inflation. If properly constituted, this can help to generate investment and ongoing growth. Whilst growth in the near term is likely to be robust, the market does not expect that this will remain above a modest 1% next year.

Manufacturing activity is relatively weak (Manu PMI 49.1 p50 e49.2) and the broader Industrial Production figure was lower, but not as bad as expected (-3.6% MoM p3.6% e-4.8%) but core machinery orders pointed to a weak outlook. Retail sales surprised to the upside (3.7% YoY p2.8% e3.3%) which may provide some indication of the promise of the virtuous cycle, as real wage growth was finally positive in June (YoY) for the first time since March 2022.

Strong labour markets (u/e 2.5% e2.6%), a favourable services PMI (53.7 p49.4 e53.9) and solid core inflation (2.6% YoY p2.5% e2.7%) supported the BoJ's decision to raise the cash rate from 0.1 to 0.25%, and announce a reduction in bond purchases related to ordinary government financing from next year. The market had been finely balanced on expectations.



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