

Ardea Real Outcome Fund

ARSN 158 996 699 APIR Code HOW0098AU

Monthly Performance Report November 2022

| Performance ¹ | 1 month | 3 months | 1 year | 2 year | 3 year | 5 year | Inception |
|--------------------------|---------|----------|--------|--------|--------|--------|-----------|
| Fund | -1.87 | 1.15 | 0.90 | -0.12 | 1.85 | 3.44 | 3.53 |
| Benchmark ² | 0.63 | 1.37 | 7.14 | 5.22 | 3.73 | 2.95 | 2.45 |
| Excess Return | -2.50 | -0.22 | -6.23 | -5.34 | -1.87 | 0.49 | 1.08 |

¹ Performance figures are calculated after fees have been deducted and assume distributions have been reinvested. No allowance is made for tax when calculating these figures. Past performance is not a reliable indicator of future performance.

² The Fund benchmark is the Australian Consumer Price Index.

Source: Fidante Partners Limited, 30 November 2022.

Fund Features

Unique 'relative value' investment strategy: The Fund adopts a relative value investment strategy to access a range of fixed income return sources that are independent of interest rates.

Tight risk control: The Fund specifically targets low volatility returns by using a range of risk management strategies.

Diversification benefits: The Fund offers significant diversification benefits when combined with conventional bond, credit and equity investments in an investment portfolio.

Capital preservation: The Fund prioritises capital preservation by only investing in high quality government bonds, related derivatives and cash like investments. However, the Fund is not guaranteed.

Protect long term purchasing power: The Fund explicitly targets a return exceeding Australian inflation rates to protect long term purchasing power.

Daily liquidity: The Fund only invests in the most liquid segments of global fixed income markets.

Experienced and stable investment team: Ardea's investment team has decades of experience across global fixed income markets. Majority employee ownership of the Ardea business fosters team stability.

Fund Facts

| | |
|-------------------------------|--|
| Portfolio Manager | Ardea Investment Management |
| Investment Objective | The Fund targets low volatility returns exceeding cash rates and inflation, by investing in a global portfolio of high quality government bonds that prioritises capital preservation and liquidity. |
| Investment Horizon | Recommended min. 2 years |
| Inception Date | 20 July 2012 |
| Fund Size | \$8.4bn |
| Management Fee | 0.50% p.a. |
| Buy/Sell Spread | +0.05% / -0.05% |
| Distribution Frequency | Quarterly |

| Sector Exposure | | Rating Exposure | | Risk Contribution by Currency | |
|------------------------------|------|-----------------|------|-------------------------------|------|
| Government – National | 71% | AAA | 58% | AUD | 42% |
| Government - State | 29% | AA | 36% | CAD | 15% |
| Total | 100% | A | 6% | EUR | 20% |
| | | Total | 100% | JPY | 1% |
| | | | | NZD | 1% |
| | | | | GBP | 2% |
| | | | | USD | 18% |
| | | | | Total | 100% |

Source: Ardea Investment Management, S&P Ratings

Portfolio Commentary

Performance for the month of November was -1.87% (after fees).

The main driver of the negative return in November is a reversal of outsized gains in the prior few months from the Fund's structural long position in interest rate options.

It's important to note the high starting point for option valuations. Global interest rate market volatility had reached historically high levels prior to November. Markets were braced for a continuation of one of the most aggressive and synchronised rate hike cycles on record. However, through November, markets quickly shifted course. Bond yields fell sharply amid signs that inflation momentum is slowing. Despite still high macro uncertainty, in the current context this repricing compressed the perceived distribution of future rate outcomes causing option-implied volatility to fall sharply. The decline in volatility was among the largest one month falls in a decade or longer (depending on measure).

The Fund was impacted by the fall in implied volatility through option holdings (-1.4%). This impact was spread across multiple markets but was most notable in EUR and GBP, where the decline in volatility was most pronounced.

Option positions serve an important portfolio risk balancing role and tend to provide protection in stressed market environments, which can adversely impact other RV positions. While this portfolio construction approach works reliably over the medium term, there are infrequent short-term periods such as November where options decline significantly in value and are not offset by gains in other RV positions.

Within non-option risk factors, there are a large number of underlying positions and mixed performance between markets over the month. Overall, these exposures were modest detractors, summarised as RV curve (-0.4%) and bond vs derivative (-0.2%) in the portfolio attribution. For example, RV positions in the front part of the CAD curve - targeting the relative expensiveness of 3-4y rates - were a detraction. In terms of bond vs derivative exposures, long positions in 10-30y AUD government bonds vs swaps detracted this month, after driving positive performance in the prior months. These spreads had widened well beyond supply/demand factors due to positioning and liquidity and this impact faded in November.

We remain positive on the opportunity set in RV brought about by recent extraordinary stress in interest rate markets. Over time we expect improved performance in non-option RV positions to more than offset any prospective decline in volatility.

Market Commentary

Please see the Insights section of the [Ardea website](#) for our latest thoughts on markets and investment themes.

Understanding Performance

Performance is evaluated over rolling 2 year periods for consistency with the recommended minimum investment horizon of 2 years. Over short-term horizons it is expected that portfolio performance will fluctuate in a range around the expected long-term investment outcome, including periods of negative returns. This is because the Fund's targeted return is not expected to materialise evenly over the investment horizon.

We use the concept of 'expected performance variability' to objectively define a range of short-term performance fluctuation that is consistent with the investment strategy operating as expected. This range is based on the Fund's volatility target of 2% p.a. and translates to an expectation for monthly performance to commonly fluctuate in a range of -0.4% to +0.7%.

The Fund's highly differentiated investment approach generates returns exclusively from capturing RV mispricing opportunities across global interest rate markets. This approach is intentionally independent of the level of bond yields, the direction of interest rates and broader bond market themes.

The Fund's portfolio construction process intentionally diversifies risk across many different types of independent and modestly sized RV trades. Therefore, performance is the cumulative result of interactions between hundreds of trades entered, exited, and held over the preceding months.

For these reasons, the Fund's performance is ordinarily not driven by a few key trades, nor can it be mapped to broader market fluctuations or macro themes. This is intentional, because the Fund aims to deliver volatility controlled returns that exhibit low correlation to the performance of government bond, credit, and equity markets. This is precisely why the Fund can offer compelling diversification benefits when combined with conventional investments.

Please note that monthly performance attribution is heavily influenced by short-term 'noise' and ordinarily offers little genuine information value.

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The Morningstar Analyst Rating™ for
Ardea Real Outcome Fund is
'Bronze' as of 7/9/2022



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