

# AUSTRALIAN FIXED INTEREST FUND

## As at March 2022

### Fund objective

The Fund seeks to achieve a total return after fees that exceeds the total return of the Benchmark, over rolling three-year periods.

### Investment approach

The Fund is an actively managed portfolio of high quality interest bearing securities that seeks to provide a high level of capital protection. The Manager's investment approach is fundamentally driven and seeks to take advantage of situations where market pricing has become misaligned with economic and investment fundamentals. The Manager seeks to add value to the benchmark using a combination of active strategies including duration and yield curve management, sector allocation and security selection.

### Benchmark

Bloomberg AusBond Composite 0+ Yr Index

### Risk profile

Medium

### Suggested timeframe

3 years

### Inception date<sup>^</sup>

31 August 1994

### Fund size

\$726.2 million

### Minimum investment

\$25,000

### Management cost (%)

0.45 p.a.

### Buy/sell spread (%)

0.00/0.08<sup>^^</sup>

### Distribution frequency

(if any)  
Quarterly

### ARSN code

087 719 739

### APIR code

IOF0046AU

### ASX mFund

JHI05

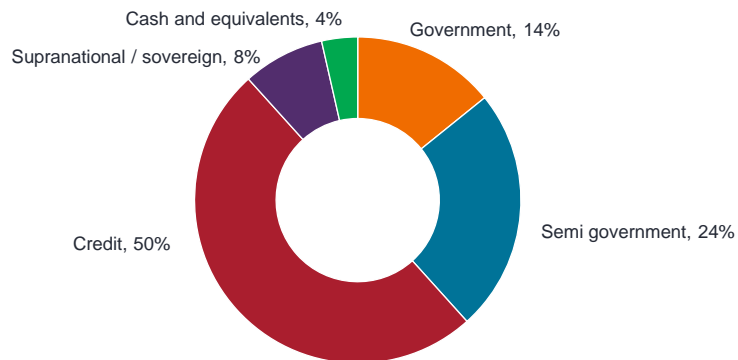
Performance	1 month (%)	3 months (%)	6 months (%)	1 year (%)	3 years (% p.a.)	5 years (% p.a.)	10 years (% p.a.)	Since inception (% p.a.)
Fund (gross)	-4.39	-6.90	-8.02	-5.48	0.52	2.37	4.11	6.78
Fund (net)	-4.43	-7.00	-8.22	-5.90	0.04	1.88	3.62	6.22
Benchmark	-3.75	-5.88	-7.25	-5.55	-0.32	1.86	3.44	6.02
Excess return*	-0.68	-1.12	-0.97	-0.35	0.36	0.02	0.18	0.20

\*Excess return is measured against net performance.

Gross return is gross of management costs and sell spread.

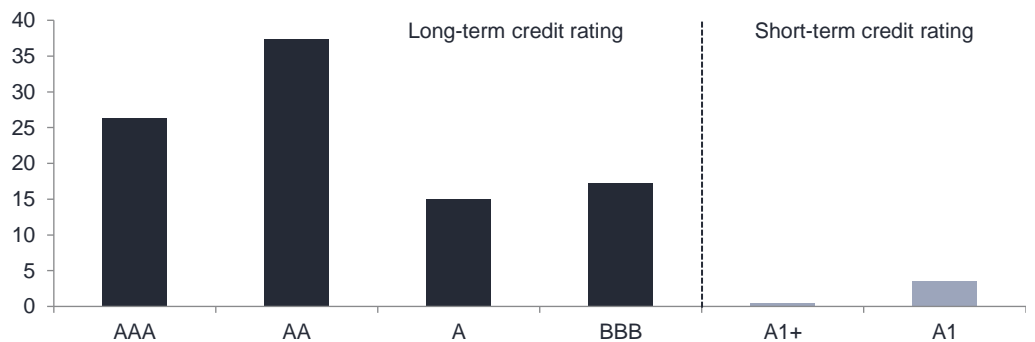
Past performance is not a reliable indicator of future performance.

## Sector allocation



Rounding accounts for small +/- from 100%.

## Credit rating distribution (%)



## Portfolio characteristics

Estimated Weighted Average Yield to Maturity (EWAYTM) <sup>1</sup>	3.22
Benchmark EWAYTM	2.59
Running Yield	2.64
Weighted Average Credit Quality	AA-

<sup>1</sup> Estimated Weighted Average Yield to Maturity is a measure of the average annual yield of all securities in the Fund.

Modified duration	Years
Fund	6.50
Benchmark	5.46
Active Position	1.04

Benchmark duration is as at month end and therefore does not include rebalancing.

<sup>^</sup> Fund inception for performance reporting purposes is at end of month, whereby the actual fund inception date may be earlier in the month.

<sup>^^</sup> For more information and most up to date buy/sell spread information visit

[www.janushenderson.com/en-au/investor/buy-sell-spreads](http://www.janushenderson.com/en-au/investor/buy-sell-spreads)

# AUSTRALIAN FIXED INTEREST FUND

(continued)



**Head of Australian Fixed Interest**  
Jay Sivapalan

## Fund performance

The Janus Henderson Australian Fixed Interest Fund (Fund) returned -4.43% (net) and -4.39% (gross) in March. The Fund underperformed the Bloomberg AusBond Composite 0+ Yr Index (Benchmark) by -0.68% (net), which fell by -3.75%, one of the largest monthly falls in nearly four decades. However, the Fund continues its outperformance by 0.20% (net) per annum since inception.

Rates strategies are actively managed in the Fund and performance was impacted by the large movement upwards in bond yields. Markets have, in our assessment, overshot fair value and we've therefore leaned against current pricing, meaning near-term underperformance. Seeing the opportunity to lock in what we assess as attractive 'all-in yields' caused by dislocated markets reflecting a cash rate profile that is unlikely to be delivered by the RBA over the next couple of years, we started adding meaningful duration to the Fund. Implementing this strategy while bond yields continued to rise detracted from performance over the month. However, bond investing is rarely about the direction of cash rates, but rather about what's already priced in relative to how fundamentals may eventuate. As opportunities became clearer, we continued to add duration, looking to lock in the current yields for investors.

While zero (or 0.1% to be precise) cash rate settings are no longer appropriate for the Australian economy and given that the first 100 basis points (bps) of tightening can occur quite briskly with consumers absorbing the lift, we question the subsequent 200bps without a pause. We believe there is a very real prospect that the full extent of current market pricing of the future path of cash rates isn't fully realised. Further, the risks of another 100bps of tightening to a cash rate of 4.25% inside the next 36 months is remote. Much of the capital loss in bond markets from rising yields occur before the first cash rate tightening. Where markets overshoot or get it wrong, bond yields can fall more sharply, delivering capital gains.

The Fund holds good exposure to inflation linked bonds, bought cheaply when inflation was low. As inflation expectations rose over the month, so did inflation break even rates, resulting in these bonds outperforming nominals and aiding performance.

In terms of credit, the Fund had a good level of credit protection going into 2022 through CDS as the tide that supported risk assets was likely to go out. Having initially employed an effective credit hedge, this was reduced, taking profit as CDS spreads widened earlier in the month. However, physical credit spreads continued to widen over the month, contributing to negative performance. During March we were highly active in markets, switching from 'capital preservation mode' to actively seeking yield enhancement, with high levels of asset acquisition.

While noting the negative performance this month, we have boosted our running yield advantage significantly by utilising the opportunities available from market pricing. For example, the Fund's yield to maturity is approximately 96bps higher than the Benchmark. This is one of the highest advantages we have had over the Benchmark in around 10 years. We believe this sets us up for a strong period ahead, with high levels of conviction.

## Market review

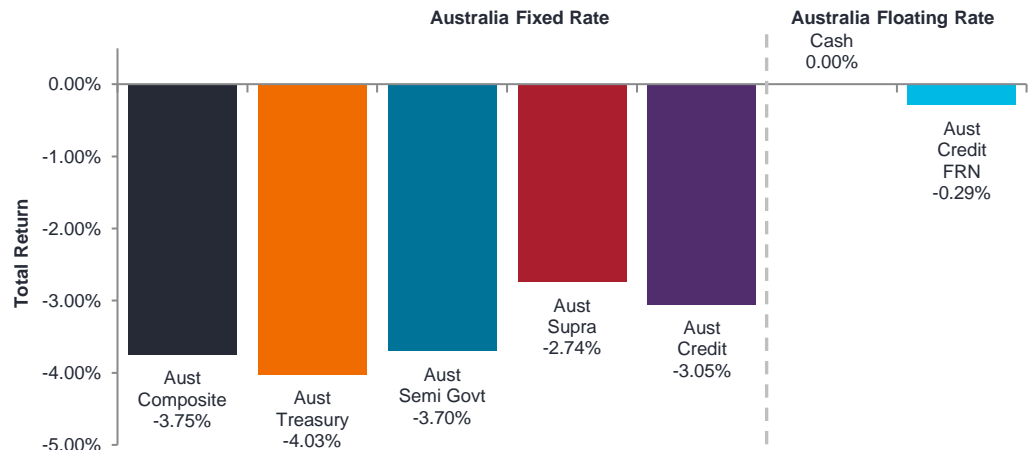
- Bond investors endured another near-record monthly sell-off in bond markets in March. The market, as measured by the Bloomberg AusBond Composite 0+ Yr Index was down -3.75%, one of the largest monthly falls in nearly four decades.
- Offshore and domestic yields rose sharply following hawkish commentary from the US Federal Reserve (Fed) after its first tightening. Inflation expectations rose as the impact of Russia's invasion of Ukraine on global supply chains, commodities and energy prices became more apparent.
- Markets have now fully priced in a 1.75% cash rate by year end and a 3.25% cash rate by the end of next year. To put this into context, a tightening cycle of 3% in such a short period of time has never occurred in Australia. Current pricing for this 300bps of tightening implies a mortgage rate by late next year of around 6%.
- Credit markets were volatile against the backdrop of shifting rate and inflation expectations, and the implications of a flatter-to-inverse US yield curve for the medium-term growth outlook and potential for future recession.

# AUSTRALIAN FIXED INTEREST FUND

(continued)

We suspect the most likely scenario is one where the Reserve Bank of Australia (RBA) removes policy accommodation steadily with the goal to extend, not end, the current cycle.

- Credit spreads on high quality financials (such as major banks) had been widening due to a combination of needing to find natural market pricing following the ceasing of the RBA's term funding facility (TFF) last year, other policy withdrawal and the more recent 'risk-off' episode driven by the Russian invasion.



Source: Bloomberg AusBond Indices  
Period of 1 March 2022 – 31 March 2022

## Market outlook

- We suspect the most likely scenario is one where the Reserve Bank of Australia (RBA) removes policy accommodation steadily with the goal to extend, not end, the current cycle. Our base case view has the cash rate lifting from 1% at the end of this year to 1.75% by the end of 2023 and to 2% by the end of 2024.
- While we still look for policy normalisation, we remain sceptical of the speed and quantum of tightening currently priced in.
- We continue to expect further bouts of volatility caused by geo-political events, pandemic machinations, and central bank actions to roil credit markets. These periods can provide opportunities when spread widening is in excess of fundamentals.

For in-depth economic analysis and the Australian Fixed Interest Team's outlook, visit [go.janushenderson.com/Viewpoint-Apr22](https://go.janushenderson.com/Viewpoint-Apr22).

## Investment strategy

In terms of positioning, combining the above two developments of elevated bond yield / swap rates and elevated high quality senior debt spreads has allowed the Fund to access yields of around 3% with a carry, rolldown and potentially move (lower all-in yields) benefit, suggesting the potential for total returns of 3-4.5% in a relatively safe manner over a 12-month period. The same combination of high-quality credit and swap rates just 18 months ago was yielding around 0.5%, with heavy investor demand at that time. While the potential exists for risk-free yields and credit spreads to rise further, our assessment is that the risks are asymmetric at present and provide investors some defence over a 12-month investment period.

This has manifested in the estimated weighted average yield to maturity of the Fund reaching a healthy 3.55% by month end.

This forward-looking yield of the Fund, as well as capturing this value in our positioning from an overshot of market pricing, provides us with high levels of conviction for investment outcomes over the coming year for investors.

# AUSTRALIAN FIXED INTEREST FUND

(continued)

**Our base case view has the cash rate lifting from 1% at the end of this year to 1.75% by the end of 2023 and to 2% by the end of 2024, which is slower than what the market is pricing.**

Our investment focuses are:

- A 'normalising' in cash rates with 'lift off', not 'blast off'.
- Navigate the range within bond yields, adding duration when they overshoot to the upside and taking profit when yields retreat.
- Inflation protection when it's cheap.
- Targeted income bid (spread sectors, including credit), but wary of the policy support tide going out;
- Using credit protection for left field events and policy mistakes;
- Investing with a cautious mindset – managing ESG/stranded asset risk and deploying capital to positive impact opportunities;
- Aiming to fully participate in the cyclical growth uplift;
- Remaining active and able to pivot should a derailment to the recovery unfold;
- Aiming to 'lock in' attractive yields for investors.

### Interest rates:

Our base case view has the cash rate lifting from 1% at the end of this year to 1.75% by the end of 2023 and to 2% by the end of 2024, which is slower than what the market is pricing. With this in mind, we see some value at the shorter end of the yield curve. We see 10-year government bond yields at month end levels of 2.84% as beginning to offer value, providing investors with term premia at a time of heightened inflation risk.

### Sector allocation:

**Inflation-linked bonds:** We hold onto our inflation protection strategies, especially as the Russian invasion elevates oil prices and exacerbates supply chain pressures. Furthermore, there remains the tail risk that the RBA allows the labour market to overheat and lead to an upward wage/price spiral.

**Semi-government bonds:** remain attracted to semi-government securities, particularly those issued by NSW, as market pricing has adjusted to the removal of formal quantitative easing from the RBA. We hold a positive longer-term macro outlook for the state and the strong fiscal position of the NSW government. These are AA+ rated liquid government securities.

**Investment grade credit:** Recent spread widening has allowed us to access high quality names at attractive levels. As macro policy settings transition from accommodative to more neutral levels, we remain very active and selective, favouring relative value within sub-sectors, whilst being judicious on overall credit beta.

### Environmental, Social and Governance (ESG)

From an ESG perspective, we continue to engage with intermediaries and issuers on growing Australia's positive impact bond market. We seek to participate where valuations make sense.

### Important information

A Product Disclosure Statement and Additional Information Guide for the Fund dated 30 September 2021 is available at [www.janushenderson.com/australia](http://www.janushenderson.com/australia).

Past performance is not a reliable indicator of future performance. Performance source: Morningstar, Janus Henderson. Performance figures are calculated using the exit price net of fees and assume distributions are reinvested. The Gross performance methodology was updated at the end of March 2020 to reflect the Gross return to be Gross of Management costs and Sell Spread. Due to rounding the figures in the holdings, breakdowns may not add up to 100%. The information in this monthly report was prepared by Janus Henderson Investors (Australia) Funds Management Limited ABN 43 164 177 244, AFS Licence 444268 and should not be considered a recommendation to purchase, sell or hold any particular security. Securities and sectors mentioned in this monthly report are presented to illustrate companies and sectors in which the Fund has invested. Holdings are subject to change daily. This monthly report contains general information only and does not take account of your individual objectives, financial situation or needs. The value of an investment and the income from it can fall as well as rise and you may not get back the amount originally invested. None of Janus Henderson Investors (Australia) Funds Management Limited nor any of the Janus Henderson group entities nor their respective related bodies corporate, associates, affiliates, officers, employees, agents or any other person are, to the extent permitted by law, responsible for any loss or damage suffered as a result of any reliance by any reader or prospective investor. You should consider the current PDS, available at [www.janushenderson.com/australia](http://www.janushenderson.com/australia), before making a decision about the Fund. Target Market Determinations for funds issued by Janus Henderson are available here: [www.janushenderson.com/TMD](http://www.janushenderson.com/TMD). Dollar figures shown are in Australian Dollars (AUD), unless otherwise stated.