

TACTICAL INCOME FUND

As at May 2021

Fund objective

The Fund seeks to achieve a total return after fees that exceeds the total return of the Benchmark, by investing in a diversified portfolio of predominantly Australian income producing assets.

Investment approach

The Fund is actively managed and designed to make tactical investment decisions between cash, longer duration fixed interest securities and higher yielding securities, through every step of the investment cycle.

Benchmark

Bloomberg AusBond Bank Bill Index and Bloomberg AusBond Composite 0+ Yr Index (equally weighted)

Risk profile

Low-medium

Suggested timeframe

3 years

Inception date[^]

30 June 2009

Fund size

\$4.2 billion

Minimum investment

\$25,000

Management cost (%)

0.45 p.a.

Buy/sell spread (%)

0.00/0.04^{^^}

Base currency

AUD

Distribution frequency

Quarterly

ARSN code

130 944 866

APIR code

IOF0145AU

ASX mFund

JHI02

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)	0.11	0.69	0.12	3.23	3.30	3.29	4.33	5.29
Fund (net)	0.08	0.59	-0.10	2.84	2.83	2.82	3.86	4.81
<i>Growth (Net)</i>	0.08	-0.33	-1.56	-1.92	0.19	0.04	0.02	0.78
<i>Distribution (Net)</i>	0.00	0.92	1.46	4.76	2.64	2.78	3.84	4.04
Benchmark	0.13	0.82	-1.33	-0.56	2.58	2.33	3.59	3.90
Excess return*	-0.05	-0.23	1.23	3.40	0.25	0.49	0.27	0.91

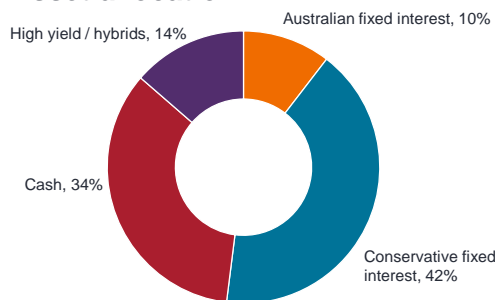
*Excess return is measured against net performance.

Gross performance is calculated gross of management costs and sell spread.

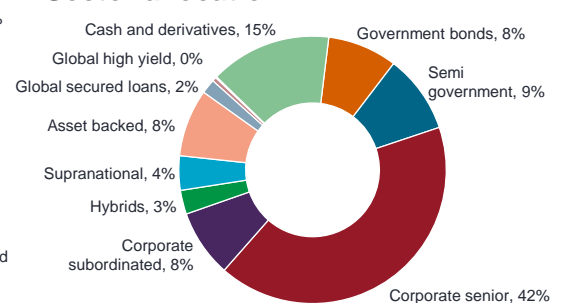
Past performance is not a reliable indicator of future performance.

[^] Fund inception for performance reporting purposes is at end of month, whereby the actual fund inception date may be earlier in the month.

Asset allocation*

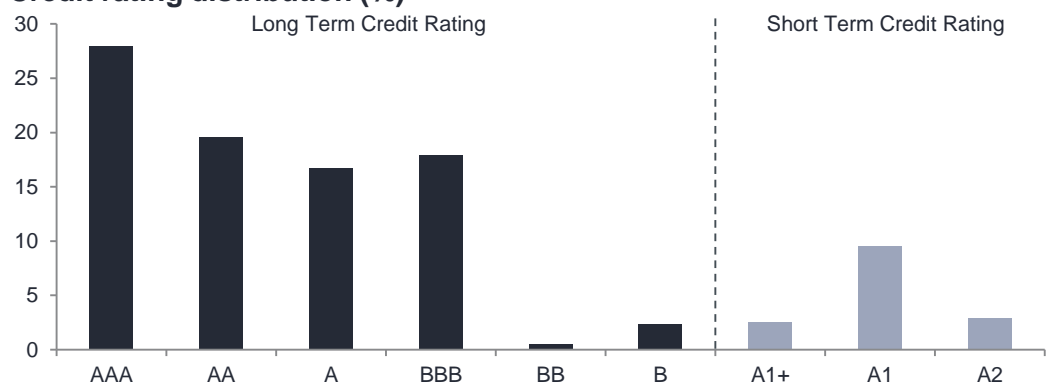


Sector allocation



*Asset allocation shown as effective exposure of asset classes. Rounding accounts for small +/- from 100%.

Credit rating distribution (%)



Portfolio characteristics

Estimated Weighted Average Yield to Maturity (EWAYTM) ¹	1.19
Running Yield	1.59
Benchmark EWAYTM	0.55
Weighted Average Credit Quality	AA
Number of Securities (on a look through basis)	438

¹Estimated Weighted Average Yield to Maturity is a measure of the average annual yield of all securities in the Fund (Grossed up for franking credits, where applicable)

Modified duration	Years
Fund	0.89
Benchmark	3.03
Active Position	-2.14

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

^{^^} For more information and most up to date buy/sell spread information visit

www.janushenderson.com/en-au/investor/buy-sell-spreads

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(continued)



**Head of Australian
Fixed Interest**
Jay Sivapalan

Fund performance

The Janus Henderson Tactical Income Fund delivered a stable positive return in May, returning 0.11% gross and 0.08% net. The Fund slightly underperformed the Bloomberg AusBond Bank Bill Index and Bloomberg AusBond Composite 0+ Yr Index (equally weighted) (Benchmark), which returned 0.13% over the month. Over the 12 months, the Fund has significantly outperformed its Benchmark by 3.40% net of fees, with the Fund delivering 2.84% to investors compared to the Benchmark which fell by -0.56%.

While the Fund is managed with an absolute return mindset, active interest rate management plays a significant role in its performance. Our base case on rates is that central banks and governments are looking to grow the economy, such that very low levels of unemployment are reached (effectively full employment with only friction remaining) which if left unbridled for long enough will tighten the labour market sufficiently to generate inflation. With this in mind, we think the markets have overpriced the likelihood of the RBA commencing a tightening cycle as markets look for a 2023 rate hike, balanced against the potential for bond yields to rise further as inflation expectations get further priced into markets. At current levels, we view nominal government bond duration reflecting close to fair value and have moved the Fund to a broadly neutral stance. In the last few months, we have pulled back the Fund's duration, taking profit after holding our highest overweight duration position at the turning point in yields. Our current duration position in the Fund sits appropriately with this fair value assessment of bonds and is designed to mitigate interest rate risk breaking out in either direction. We now await the next overshoot before we will apply a more meaningful position. The Fund generated a positive return in the month but performed slightly below the Benchmark which has a greater sensitivity to interest rate moves, in this case benefitting from the fall in longer dated bond yields.

Inflation expectations edged higher over the month, and we used the opportunity to trim some of our overweight position to inflation-linked notes. Overall, our holdings here have been a strong contributor to performance this month, as this sector benefitted from a rise in break-even inflation levels and a lowering in nominal bond yields.

Meanwhile, exposures to spread sectors including investment grade credit contributed to performance given income generation and slight spread tightening in credit markets. The Fund is currently allocated on an opportunistic basis with marginally above average exposure to higher yielding sectors, including hybrids, which overall were positive contributors in the month, despite the slight dip in performance from domestic hybrids. Finally, the Conservative Fixed Interest Fund, the Diversified Credit Fund and the Australian Fixed Interest Fund that the Tactical Income Fund invests in all outperformed their respective benchmarks, while the Cash Fund remained flat.

Market review

Massive fiscal and monetary stimulus boosted economic growth, both in Australia and abroad. Despite some volatility caused by a temporary surge in inflation expectations and the US Federal Reserve (Fed) raising the prospect of eventually tapering its Quantitative Easing (QE) program, risk appetite held up. Equity markets were firmer and credit markets remained well-supported. There was some further flattening in the domestic yield curve as longer-dated government bond yields edged lower. The Australian bond market, as measured by the Bloomberg AusBond Composite 0+ Yr Index, ended May 0.27% higher.

Yields at the shorter end of the yield curve remained anchored around the Reserve Bank of Australia's (RBA) 0.10% cash rate and three-year government bond yield target. Further out along the curve, markets are still discounting future tightening, with the November 2024 government bond yield ending the month 2 basis points (bps) lower at 0.28%.

Longer-dated government bond yields spiked to mid-month highs on concerns that strong growth, supply bottlenecks and massive stimulus, particularly in the US, could lead to a breakout in inflation. After peaking at 1.81%, the 10-year government bond yield then fell to end the month 6bps lower at 1.69% as inflation fears ebbed. The 30-year government bond also finished 6bps lower at 2.61%.

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(continued)

Partial demand indicators point to an ongoing vigorous rebound in activity.

Partial demand indicators point to an ongoing vigorous rebound in activity. Encouragingly, strong business conditions and high levels of confidence are starting to translate into a lift in animal spirits. Business capital investment intentions have lifted across a range of surveys and if realised, will add to the longevity and broadness of the current rebound. We look for the Australian economy to expand by around 1.0% to 1.25% over the March quarter in the upcoming national accounts release.

The rapid recovery in the labour market took a breather in April with the end of JobKeeper and an early Easter driving a fall in hours worked and labour force participation. The number of jobs fell by 30,600, while the unemployment rate edged lower to 5.5%. Forward labour demand indicators remain strong and we expect to see jobs growth resume over the months ahead, even after allowing for the Victorian COVID-19 circuit-breaker lockdown.

The improvement in labour market conditions has yet to translate into a lift in wages, one of the pre-conditions for a tightening in monetary conditions. The March quarter Wage Price Index rose by 0.6% and by 1.5% over a year ago.

Money market rates remained very low given the 0.10% official cash rate and RBA forward guidance for an extended period of highly accommodative policy. Three-month bank bills ended the month largely unchanged at 3.6bps, while six-month bank bills ended 1bps lower at 8.5bps.

After the ebb and flow in bond yields and primary supply since February, the credit market enjoyed a period of relative calm in May. iTraxx Australia CDS traded in a fairly tight 2bps range over the month, settling 2bps tighter at 59bps to end May. The additional income available from credit was complemented by a very modest tightening in spreads and assisted positive excess returns. In Australia, bank floating rate note (FRN) spreads tightened by 3bps, while corporate credit spreads rallied 3bps. Higher yielding floating rate spread sectors, like global loans performed well, returning 0.6%, while subordinated bank notes also performed well locally, returning 0.5%, outpacing listed hybrids which gave back some of the very strong late April rally, returning -0.2% for May.

From an Environmental, Social and Governance (ESG) perspective, the government guaranteed National Housing Finance Investment Corporation issued their first Sustainability bond, which has both social and environmental impact features, providing for the renewal of social housing with energy and water efficient buildings, including solar installations and social support initiatives. We were glad to support the transaction which will assist the local community, while investors were also able to access an attractive 0.3% yield advantage above similar government bonds.

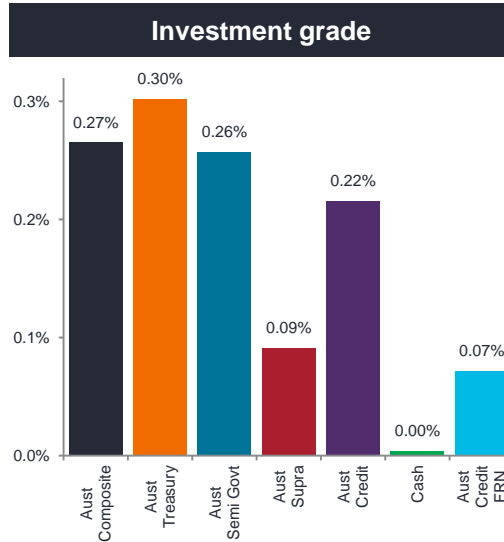
Corporate supply was light, with Paccar issuing a 3.5-year and NBN Co issuing a 7-year at swap spread +100bps, both appeared reasonably good value in our view. The major banks were active after reporting their half year results, with Westpac issuing a Tier 2 green bond in Euro, then NAB issuing a Tier 2 in US dollars. The issuance of Tier 2 into offshore markets allowed the local market to perform well as local supply fears abated. Later in May Westpac was the first major bank since early 2020 to issue a long-term senior bond. They chose the US dollar market to issue A\$3.15bn across both 5- and 10-year maturities, extending their maturity profile beyond the 3-year Term Funding Facility (TFF) window.

The market had been eagerly awaiting confirmation of the pricing of 5-year bank senior debt and after such a long hiatus from primary markets, the new 5-year deal swapped to a local equivalent of swap spread +48bps, in line with secondary levels. At the time of writing, banks still have access to A\$81bn of 3-year TFF funding at a cost of 0.10%. Westpac's activity suggests the combination of slowing deposit growth, rising credit growth and the desire to smooth out maturity profiles will keep bank treasurers at the ready as the TFF winds down.

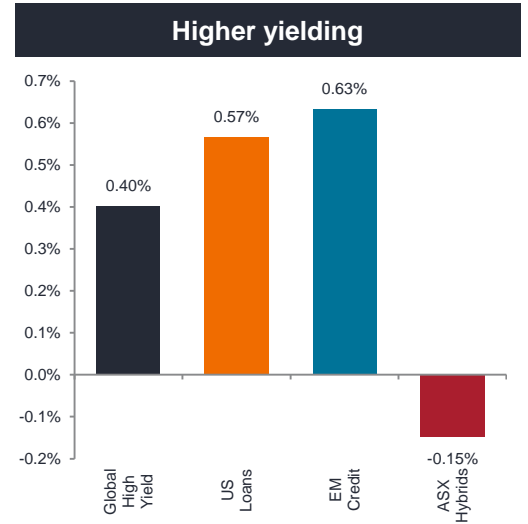
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Both the RBA and Treasury look for a period of above trend economic growth sufficiently strong enough to push the unemployment rate down towards 4.75% by mid-2023.



Source: Bloomberg AusBond Indices
Period of 1 May 2021 – 31 May 2021



Source: ICE BoAML Global High Yield Index A\$ Hedged, S&P/LSTA Leveraged Loan Index AUD TR Hedged, JPMorgan CEMBI Broad Diversified A\$ Hedged, Solactive Australian Hybrid Securities Index (Gross).
Period of 1 May 2021 – 31 May 2021

Market outlook

Both the RBA and Treasury look for a period of above trend economic growth sufficiently strong enough to push the unemployment rate down towards 4.75% by mid-2023. The focus of fiscal and monetary policy remains outcome based, with full employment the primary goal.

While output gaps caused by COVID lockdowns are expected to be closed, neither the RBA nor Treasury see an inflation break out, with both looking for inflation to settle in the 2.00% to 2.25% range by mid-2023. The Budget is only expected to go into the repair phase once full employment levels have been reached, thus avoiding the risk of premature austerity.

While the RBA upgraded their economic forecasts in the latest Statement on Monetary Policy, we believe there has been no material change to their reaction function.

In our view, the stance of monetary policy will only change once the tightening trifecta conditions have been met. These are:

1. an unemployment rate close to 4%;
2. actual inflation at 2% or above on a sustainable basis; and,
3. wages growth of at least 3%.

The RBA continued to signal that it doesn't see the conditions in place for tightening until 2024 at the earliest. Nevertheless, markets are still looking for a tightening cycle to commence early 2023, with the cash rate to get to over 2% by late 2026, above our estimates of the neutral cash rate. This implies restrictive policy settings over the second half of the decade and can only be validated by a sustained breakout in inflation. Given the inertia in wages setting, we believe the market is premature in fully pricing in restrictive policy settings.

While we acknowledge that expansionary fiscal policy, particularly in the US, carries the risk of overstimulating economies, we see investors compensated for this risk by current yield curve steepness with the 10-year government bond yield 17 times higher than the prevailing cash rate. Our view is that the current 10-year government bond yield at 1.70% (at the time of writing) is fairly valued.

Spread sectors are likely to remain well-supported, with corporates in particular, benefiting from the tail winds of a cyclical recovery and persistent accommodative policy settings. Nevertheless, with the spread cushion for investors within pockets of credit having narrowed substantially, we remain very active and selective in this environment. While the market searches for any yield advantage, we remain discriminate, avoiding lower quality borrowers. The need for inflation protection has diminished, with breakeven inflation rates moving back into the lower end of the RBA's 2% to 3% target band.

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(continued)

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Investment strategy

Our north stars for investing are:

- Zero to ultra-low risk-free cash rates
- Navigate the range within bond yields, adding duration when they overshoot to the upside and taking profit when yields retreat
- Inflation protection when its cheap
- Income bid (spread sectors, including credit)
- Invest with a cautious mindset – managing ESG/stranded asset risk and deploying capital to positive impact opportunities
- Aim to participate in any cyclical growth uplift

The following is a summary of the key strategies in the Fund (at the time of writing):

Interest rates:

We see government bond yields, at the time of writing, as fairly valued. We will look for overshoots, in either direction, away from our current neutral view on rates to alter our duration position. As we patiently wait for the next overshoot in rates, the Fund is positioned to benefit from the market pricing of term premium and steepness in the curve, which offers good roll down.

Sector allocation:

Inflation-linked bonds: The cheapness of inflation protection has diminished, with breakeven inflation rates moving back into the lower end of the RBA's 2% to 3% target band. That said, we continue to maintain some allocation to inflation-linked notes to participate in further upside, albeit recognising the big shift in break-even inflation levels has already occurred in the last 12 months.

Semi-government bonds: After benefitting from holding a meaningful overweight to semi-government (semi's) position for much of the last year, we have now trimmed this exposure, taking our position close to neutral. The reward for semi's has diminished greatly, and while these securities are still supported by RBA under the QE program, spreads have contracted to levels where we view valuations as unconvincing. We will wait for the next opportunity to add to this position.

Investment grade credit: In an expected backdrop of strong corporate profits, tight labour conditions, employment income aiding serviceability for mortgages holders, low delinquencies for banks, good liquidity and funding conditions for companies (including those that are challenged) should bode well for credit spreads but nuancing where to invest is still paramount. Lessons learned from the pandemic and trade with China is that there will be winners and losers. The sub-sector themes we like in credit are those assets that are not priced consistent with a recovering economy. These include universities, property trust, airports and consumer finance, and companies that will benefit from an improvement in unemployment. We have reduced our overall credit exposure in the Fund over recent months, taking it to a lower level that provides spare capacity for when opportunities arise. Until then, we remain active in switching into industries and sectors that we view as under-priced but should be winners over the cycle.

Higher yielding credit: The Fund took profit on selective sectors of the higher yielding market in the last few months after a strong run of spread tightening. We maintain a modest exposure, which the Fund accesses via the Janus Henderson Diversified Credit Fund. We complement this exposure with domestic hybrids, which offer good income in a yield-deprived landscape.

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(continued)

With supply lagging demand for ESG labelled bonds, there is a strong return argument that these types of bonds will enjoy capital appreciation.

Environmental, Social and Governance:

With supply lagging demand for ESG labelled bonds, there is a strong return argument that these types of bonds will enjoy capital appreciation. While only investing in approved issuers, our Fund has appetite for more of these green and social bonds given their positive impact attributes and our view on outperformance capabilities.

We continue to carefully analyse issuers on their ESG risks and seek to deploy capital to positive impact opportunities.

Important information

A new Product Disclosure Statement and Additional Information Guide for the Fund dated 30 September 2020 is available at 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, before making a decision about the Fund. Dollar figures shown are in Australian Dollars (AUD), unless otherwise stated.