

Investment objective

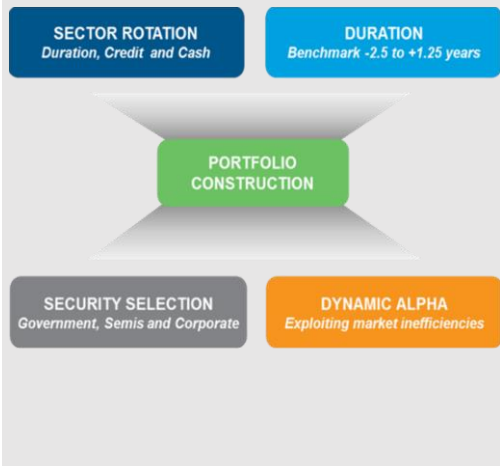
Aims to outperform the Bloomberg AusBond Composite 0+ Yr Index over the medium term (before fees) by using an active investment strategy. It aims to provide regular income and a moderate level of growth.

Key information

Fund details

APIR code	MAQ0061AU
Inception date	15 May 1995
Fund size	\$279.4m
Distribution frequency	Quarterly
Management fee*	0.390% pa
Minimum investment (Direct)	\$20,000
Unit prices and spreads	macquarie.com.au/unit_prices

*Read the Product Disclosure Statement for more details on fees and costs.



Fund performance to 31 July 2021

	Total Fund return (gross)	Total Fund return (net)	Benchmark return	Total excess return (net)
1 month (%)	1.79	1.76	1.76	0.00
3 months (%)	2.88	2.78	2.73	0.05
1 year (%)	1.12	0.69	0.53	0.16
2 years (% pa)	2.81	2.34	2.04	0.30
3 years (% pa)	5.42	4.93	4.77	0.16
5 years (% pa)	4.01	3.51	3.39	0.12

Past performance is not a reliable indicator of future performance.

Total returns are calculated based on changes in net asset values and assumes the reinvestment of distributions.

Total net Fund returns are quoted after the deduction of fees and expenses. Due to individual circumstances, your net returns may differ from the net returns quoted above.

The management fee was reduced to 0.390% pa from 8 January 2021.

Benchmark is Bloomberg AusBond Bank Bill Index

Asset allocation

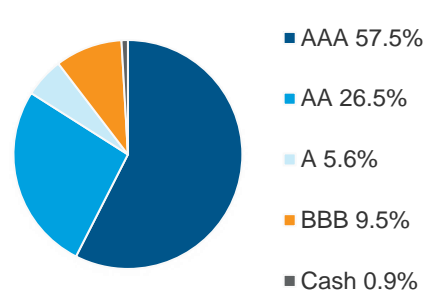
(based on physical exposure)

	Fund (%)
Government	45.9
Credit	27.0
Semi-Government	26.2
Cash and Equivalents	0.9

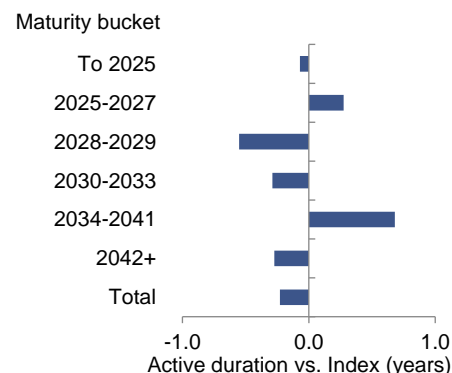
Fund statistics

Credit spread duration	0.9 years
Interest rate duration	5.8 years
Yield to maturity (% pa)	1.08%

Credit profile breakdown



Curve positioning breakdown



Macquarie Australian Fixed Interest Fund

Monthly report – 31 July 2021

Fund highlights

The Fund slightly outperformed the benchmark this month on a pre-fee basis, driven by sector rotation and security selection.

Sector rotation

Within sector positioning, the Fund has held an underweight to the semi-government sector, though this position was reduced in size over the month. There have been a number of primary deals launched this month with attractive new issue concession and this, when combined with the widening of spreads, has meant that we have been set at attractive levels. Semi-government spreads were previously tight and we had viewed the yield pick-up in certain parts of the curve as insufficient, but spreads have drifted wider following the announcements of the state government's bigger-than-expected funding tasks and the Reserve Bank of Australia's (RBA) reduction in weekly semi-government purchases.

The Fund's credit positioning contributed positively to its performance relative to the benchmark in July despite the Australian credit market moved broadly sideways. The Fund benefitted from the bull-steepening of the credit curve as the overweight credit positioning was tilted towards the front to mid part of the curve, despite the slight underperformance of some of the COVID-impacted sectors. The Fund's credit positioning also continued to benefit from higher carry than the benchmark. Given credit spreads continuing to hover around historically tight levels and with major banks likely to start issuing senior unsecured bonds in the foreseeable future, the Fund took the opportunity in this relatively low-volatility environment to establish a small amount of credit default swap protection position, which allows the Fund to continue to participate in issues at higher spreads.

Security selection

Within security selection, the Fund has been positioned overweight to the belly versus the wings in the Australian Commonwealth Government Bond portion of the Fund and bar-belled in the semi-government portion. The RBA's Yield Curve Control policy and bond purchasing program have anchored yields at the front end of the curve, before sharply steepening to reflect a rate hiking cycle, which we believe is unlikely to be realised in practice, and we have been overweight to the ultra-long bonds given the steepness relative to global curves and attractiveness to foreign investors on a hedged yield basis. We have had a preference for the 10-12 year semi-government maturities, as spread curves have remained steep due to a supply-demand mismatch for different tenors, with regulatory demand focused on shorter maturities while issuers have preferred to term out their debt.

The Fund's credit security selection marginally outperformed the benchmark despite slight widening in some of the high-beta industrial names such as Qantas, Brisbane Airport and Pacific National. Further compression of spreads in financial subordinated bonds was one of the main contributors to the Fund's performance in July. Over the month, the Fund participated in primary transactions from issuers such as CNH Industrial Capital, Banco Santander, Dexu Wholesale Property Fund, Triton 2021-2, Puma 2021-2 and Metro 2021-1.

Duration and curve

The Fund's duration positioning has been tactically underweight whilst the curve positioning has favoured the belly of the curve. The underweight duration position detracted from performance this month but given the sharpness of the move is in part driven by positioning, there has been a big clean-out of positioning and we believe most of the move is done. Option structures in place cover the short if yields were to move higher and have offset some of the losses on duration this month. The Fund has been overweight to the 4-6 year tenors, offset by an underweight to the benchmark out to the 3-year point, given the RBA has anchored yields at the very front end of the curve. The curve steepened into the 4-6 year tenors, implying a rate hiking cycle, which we do not believe can be realised, and this offers attractive rolldown.

Market review

The US Federal Reserve (Fed) surprised markets by shifting its tone and forecast for the outlook of rate hikes, whilst the US Administration disappointed with the progress of its fiscal strategy. The Federal Open Market Committee continued to emphasise that the recent rise of inflation is transitory, yet markets viewed the upward shift in rate expectations as validation of their speculation. This caused shorter-term yields to push higher, and longer-dated bond yields went the other way with a flatter yield curve the result. The debate amongst market participants was not only interpreting the Fed's signal, but also why the bond market rallied. There is merit in the view that earlier-than-expected Fed tightening could put a lid on the recovery and hence cap inflation, but there were also more subtle technical forces at play, which combined to squeeze many 'short' positions that further fuelled the rally in Treasury yields. Whilst these events were unique to the US, the impact rippled across countries, and curve flattening was a common theme.

Risk assets were mixed in July amid concerns around the Delta variant and the impact on growth. Equities hit new highs, but credit markets were moderately softer and bonds continued to rally. Emerging markets debt underperformed as the US dollar reversed its downward trend, but also because the pandemic has had a differentiated but significant impact on many countries.

Australian bond market

There was a sharp rally in rates and curve flattening over July, with the increasing spread of the Delta variant a significant drag on global sentiment, and the implications of more lockdowns and extended border closures a pull on growth. Australian rates outperformed given New South Wales's outbreak and, when the situation failed to improve, expectations began to build that the Reserve Bank of Australia (RBA) would postpone their proposed taper of quantitative easing (QE) purchases in September, though at their meeting in early August they announced they would stay the course for the time being. US inflation beat expectations as did the Australian inflation print, but for the most part data was not a significant immediate drag on yields, which saw Treasuries reach a low mid-month and trade broadly sideways, though Australian Commonwealth Government Bonds (ACGBs) continued to outperform. The Australian Office of Financial Management issued \$1.5bn of bonds most weeks and \$2bn of T-notes, bringing the total in July to \$6.5bn, whilst the states continued their issuance with a moderate uptick in NSW Treasury Corporation issuance, resulting in most states drifting slightly wider in spread to ACGB over the month.

Macquarie Australian Fixed Interest Fund

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Global credit market

US credit markets were modestly weaker. The investment grade (IG) credit index widened 6bps to finish at 86bps, though still close to post-financial crisis tightness. Performance across the IG index was broadly consistent, with minimal differentiations between ratings and curves – higher quality (single A) corporates were 5bps wider, which mirrored moves in BBB corporates. High yield credit was weaker, with CCC credit almost 50bps wider, though this simply reversed some of the strong rally from previous months. The earnings season began and approximately 60% of the S&P 500 reported by month end. Overall, earnings and revenues were strong and well above expectations, with almost 90% of reported companies beating earnings expectations. The European IG market had a benign month, with spreads closing 1bp wider at 83bps and low issuance volume in primary markets. The airline sector was the main mover this month as concerns around the Delta variant initially caused underperformance of the sector. IG airline names widened 10-30bps intra month, only to recover the majority of the moves in the latter half of July, and names such as Ryanair in fact closed at new tightness.

Australian credit market

The Australian IG market experienced little volatility in July. Despite the Term Funding Facility now in the rear-view mirror, still ample liquidity in the market, evidenced by the lack of switching activities into new issues, kept spreads broadly in check. However, this masked the underperformance in a number of COVID-impacted sectors such as airlines, airports and industrials, which widened 3-8bps over the month. Financial subordinated paper outperformed, with spreads tightening 4-11bps. The IG curve bull-steepened given some profit-taking activities occurring in the long end. There were \$A1.8bn of primary IG issuance in July, with corporates making up well over half of total IG issuance during the month.

Outlook

As we move into the second half of 2021, attention is on the shape of economic recovery, and whether the current inflation pulse will prove transitory as expected by policy makers or persistent. A key feature of the pandemic was massive government support to workers and businesses, but this is nearing its end and many states in the US are deciding to withdraw the federal support early in the hope that this encourages people back to work. The speed at which furloughed/unemployed workers return to work will be key in determining the shape of the recovery, but businesses trying to re-open have reported difficulty in hiring and many have offered financial incentives, including higher wages. This has fuelled concerns that inflation will become persistent, yet the data has shown that the majority of government transfers to these workers during the pandemic was saved, suggesting that persistent uncertainty will hold back consumption. While supply chain disruption is likely to continue to pressure inflation, in our opinion, the evolution of consumer income and demand will prove the decisive determinant of inflation longer-term.

There are still many unanswered questions on the future such as: when will normal activity resume; when will international travel resume; and what will the post-virus workplace look like? These vital but unanswered questions, combined with low bond yields and tight valuations, guide to a cautious approach to investment. However, we also recognise the ferocious insatiable need for yield. We balance these forces by maintaining discipline and 'doing the work' to determine the best risk-adjusted positioning for portfolios.

For more information speak to your financial adviser, call us on 1800 814 523, email mim.clientservice@macquarie.com or visit macquarie.com

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