

Investment objective

Aims to outperform the Bloomberg AusBond Bank Bill Index over the medium term (before fees). It aims to provide higher income returns than traditional cash investments at all stages of interest rate and economic cycles.

Key information

Fund details

APIR code	MAQ0277AU
Inception date	18 September 2003
Fund size	\$3,362.0m
Distribution frequency	Monthly
Management fee*	0.492% 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.

Sector limits (min/max)

Investment grade	0/100
High yield	0/20
Emerging markets debt	0/15
Cash	0/100

Fund statistics

Credit spread duration	2.7 years
Interest rate duration	1.2 years
Standard deviation ¹	1.8% pa
Yield to maturity ²	1.6% pa
Cash	15.8%
Cash exposure through credit hedges ³	5.3%

¹ Statistical measure of variance of Fund's post-fee monthly returns from average post-fee return since inception, used as gauge of volatility.

² Pre-fee returns Fund would earn over next year based on current market conditions if there were no changes to interest rates or holdings. It is not an actual or estimated return.

³ Credit hedges swap the return for underlying credit index for cash.

Fund performance to 31 May 2021

	Total Fund return (gross)	Total Fund return (net)	Benchmark return	Total excess return (net)
1 month (%)	0.19	0.14	0.00	0.14
3 months (%)	0.71	0.58	0.01	0.57
1 year (%)	4.18	3.67	0.06	3.61
3 years (% pa)	2.95	2.44	1.01	1.43
5 years (% pa)	3.41	2.91	1.33	1.58
10 years (% pa)	4.07	3.56	2.23	1.33
Since inception (% pa)	5.14	4.62	3.69	0.93

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.

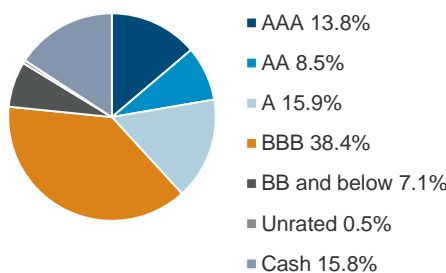
Asset allocation

Sector	Market value %
Investment grade corporates [^]	49.9
Investment grade government*	3.2
Asset-backed securities	21.3
High yield corporates [^]	3.6
Emerging markets corporates	5.5
Emerging markets government [^]	0.7
Cash and equivalents	15.8

Asset-backed securities include but are not limited to residential mortgage backed securities, bank loans and other credit related securities.

[^]Fund holds (0.0%) in investment grade, (5.3%) in high yield and (0.0%) in emerging markets credit hedges as synthetic cash (reduction in percentage of physical cash exposure).

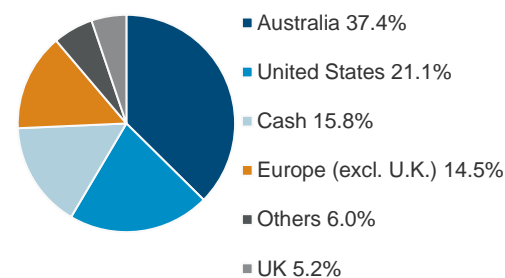
Credit profile breakdown



Average credit rating: A-

BB and below include direct holdings and residual exposure to issuers held through our investment grade and emerging markets allocation.

Region breakdown



Macquarie Income Opportunities Fund

Monthly report – 31 May 2021

Fund highlights

While society is discussing the evolving pandemic, vaccination rollouts and the re-opening of economies (or occasional lockdowns), fixed income investors are obsessing about inflation. During May, the data for April revealed that inflation was indeed rising, yet bond markets barely reacted. This was because the reasons behind the rise of inflation have been telegraphed. There are base effects, including the big declines in inflation at this time of 2020 now being reversed, logistical challenges as a result of supply chain disruption, and the impact of economic re-openings with a resultant surge in demand. It is also expected that these same forces will persist for the next few months. Over the past decade, fixed income markets have moved to fully embrace the theme of 'lower for longer', that is, persistently low interest rates. Therefore, inflation is a material threat to the current environment. We therefore expect the debate about inflation to rage for some time, which means that we are in a period of heightened sensitivity to inflation risk for fixed income markets.

While bond yields broadly moved within narrow ranges during May, this masked another theme – the lack of 'global synchronisation'. COVID-19 had an uneven impact across countries in 2020, which resulted in differentiated economic outcomes. The vaccine rollouts are also inconsistent across countries, which is expected to have a differentiated economic impact on countries through 2021. This can be observed microscopically in relative spreads. For example, US Treasury yields peaked at the end of March and have been grinding lower in subsequent months, while European yields posted their highs in late May. The relative spread moves are still modest because central banks globally have maintained a consistent 'dovish' approach to their policy, but as this evolves in the months ahead we suspect that spread volatility can increase.

The Fund outperformed the benchmark in May, with excess carry earned in both duration and credit sectors positioning being the key driver. Overall, markets ended the month little changed, with modest spread compression in investment grade (IG) credit and an overall flat result in high yield credit. The strongest contributors came from low-IG corporate hybrids and subordinated financials, such as a hybrid issued by utility provider AusNet. The Fund's duration positions in the short-end of the AUD curves added value in a generally stable market, as they rolled down the yield curve and provided attractive running yield.

There were only modest changes to portfolio positioning during the month, mostly taking advantage of some offshore new issuance. The Fund added exposures to auto parts issuers and US financials via new issuance, with some value on offer in very selected new bonds. However, most new bonds were heavily subscribed with no new issuance premium or attractive value. The Fund maintained its barbell strategy, re-deploying cash levels into short-dated credit (for example, short-dated European bank subordinated financials, which offer some carry with very low duration risk) and maintaining higher-beta exposures.

Market review

Global and Australian credit markets

US credit markets finished May mixed. IG spreads tightened 4bps to 84bps, while US high yield (HY) spreads widened 5bps to 296bps. The tightening in IG spreads was driven by strong ongoing demand for high quality yield from both domestic and non-US issuers, and somewhat limited supply. Corporate earnings wrapped up in May, with the tail end of the season continuing to produce very strong results. Overall, over 70% of issuers in the S&P 500 positively surprised on revenues, and around 75% beat on earnings. In European IG and HY credit, the moves were also relatively benign over the month.

Outlook

In the debate over the outlook for inflation, our research guides our thought process to separate the drivers of 'cyclical' from 'structural' factors. The structural factors driving inflation lower over the past decade are now well known: the rising government debt level, aging demographics, digitalisation of the workforce, dependency on low interest rates, and the trend towards de-globalisation. An interesting observation we have made in the past year is that many of these trends have actually worsened during the pandemic. Thus, currently the structural trends supporting 'lower for longer' remain very much intact. Cyclical forces, by their nature, can be very strong but tend to be 'transitory' as most central bankers are describing. However, supply chain disruptions continue and many companies are reporting difficulties in re-hiring workers laid off during the pandemic. The fear amongst economists and fixed income markets is that these cyclical forces will become persistent.

A key factor that could turn the tide on low inflation could be active fiscal policy. US President Biden's twin infrastructure investment package provided substance to analysing this possibility, where we asked whether the spending package would be large, targeted and persistent enough to turn the tide of inflation? We assessed that it is indeed likely to be targeted and planned to be persistent, but may not be large enough – even in the size proposed. The risks are that politics can negotiate the actual spending to be much lower than the President hoped. We therefore concluded that while fiscal spending may extend the transitory period of higher inflation, it is unlikely to be large enough to turn the structural forces that is needed to end the 'lower for longer' environment.

That said, with cyclical forces 'in play' for a few months we are navigating a cautious path in terms of managing our duration positions, as well as our credit risk exposures. Overall, we expect a challenging investment climate to persist, where our intention is to maintain discipline and recognise that opportunities will present themselves.

Macquarie Income Opportunities Fund

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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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