



# UBS Diversified Fixed Income Fund

July 2021

## Fund description

The Fund is an actively managed, diversified portfolio of Australian and global fixed income assets.

## Investment strategy

The strategy is managed employing both top-down macroeconomic research and bottom-up security specific analysis to build a portfolio with the core defensive characteristics of the fixed interest asset class. Whilst the Fund seeks to be fully hedged to Australian dollars, we may invest in strategic foreign currency exposures that will not exceed 10% of the total portfolio.

## Investment return objective

The Fund is actively managed, based on fundamental research that draws upon the investment insights of our fixed income teams. The approach employs both "top-down" research, including analysis of economic factors, market data and macro credit themes and "bottom-up" research in respect of particular securities including analysis of earnings and cash flow stability, balance sheet strength, industry and valuation.

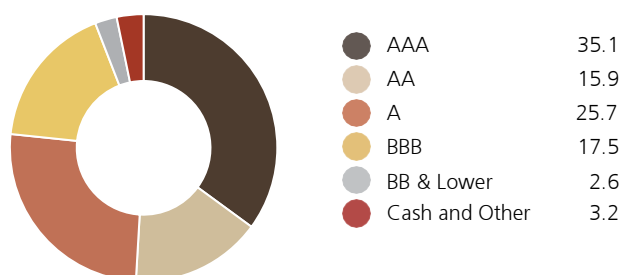
Key statistics	Fund	Benchmark <sup>1</sup>
Modified duration (yrs)	5.88	6.82
Spread duration <sup>2</sup> (yrs)	4.19	3.29
Weighted avg maturity (yrs)	6.96	7.81
Average credit quality	A1	Aa2
Yield to maturity <sup>3</sup> (%)	1.20	0.88

<sup>1</sup>Benchmark statistics do not reflect month end rebalancing for new issues and reinvestment of coupons.

<sup>2</sup>Option adjusted spread duration ex Treasury.

<sup>3</sup>Yield to Maturity (YTM) is the estimated annualised rate of return that would be received if the Fund's current securities were all held to maturity. Note that YTM does not account for fees or taxes. YTM is not a forecast, and is not a guarantee of the future return of the Fund.

## Credit quality (%)



Note: Credit ratings for physical holdings only, 'cash and other' includes the effect of derivatives.

## Fund information

Inception date	31 January 1997
Fund size	\$ 916.9 m
Management fee	0.55% pa
Minimum initial investment	\$10,000 (via mFund and online application \$5,000)
Distribution frequency	Quarterly
Buy/sell spread	+ 0.05% / - 0.15%
APIR code	SBC0007AU
mFund code	UAM06

## Fund positioning – modified duration contribution (yrs)

By sector	Fund	Benchmark
Government nominal <sup>4</sup>	2.59	4.24
Government inflation-linked	0.22	0.00
Semi-government	0.76	0.94
Government related	0.79	0.53
Corporates	1.24	0.82
Financials	0.40	0.25
Industrial	0.67	0.48
Utility	0.18	0.09
Securitised	0.28	0.29

## By Country

Australia	3.33	3.11
USA	0.45	1.38
Japan	0.49	0.63
Canada	-0.01	0.11
Euro area	0.84	0.92
UK	-0.13	0.30
New Zealand	0.13	0.00
China	0.73	0.20
Other	0.04	0.16

<sup>4</sup>Includes derivatives.

## Investment performance

Fund	1 month %	3 months %	1 year %	3 years % pa	5 years % pa	Since inception* % pa
Total return	1.31	2.17	(0.10)	3.84	2.94	5.86
Benchmark**	1.51	2.35	0.30	4.62	3.20	6.30
<b>Added value</b>	<b>(0.20)</b>	<b>(0.18)</b>	<b>(0.40)</b>	<b>(0.78)</b>	<b>(0.26)</b>	<b>(0.44)</b>

\*Inception date: 31 January 1997. \*\*50% Bloomberg AusBond Composite 0+ Yr Index / 50% Bloomberg Barclays Global Aggregate (hedged to \$A).

Performance figures are net of ongoing fees and expenses. The performance figures quoted are historical, calculated using end of month redemption prices, and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. Performance can be volatile and future returns can vary from past returns.

## Market highlights

- Australian government bonds rallied across the curve over the month.
- Australian credit spreads were broadly stable, trading in a tight range.
- The RBA maintained the cash rate at 0.10%.

## Performance review

The 10-year US Treasury rallied in July, with yields falling from 1.47% to finish the month at 1.23% and the curve flattened. European rates followed a similar pattern, with the 10-year yield on German Bunds decreasing by 25bps to end the month at -0.46%. Global bond market returns were broadly positive, driven by spread tightening in most credit markets and falling US Treasury yields. US and EUR HY eked out small gains in July. EM Sovereign bonds were also slightly up for the month, however spreads on Asia HY widened by 106bps due to ongoing negative news flow around the Chinese property developer Evergrande.

In the US, second quarter annualised GDP growth of 6.5% fell short of an 8.5% forecast, with the difference mainly due greater-than-anticipated pandemic-related disruptions and inventory drawdowns. Leaving this aside, consumer spending was strong with growth accelerating to 11.8% annualised, from 11.4% in the first quarter. Forward-looking indicators were also positive, with the ISM manufacturing and services survey readings both above 60 for June, well above the 50 level that separates expansion from contraction. Net job creation for the month was the strongest since last August at 850,000. With an improving economic outlook, the Federal Reserve concluded its July policy meeting by saying for the first time that “the US economy has made progress toward” the Fed’s goal. That marked another step towards a tapering of bond purchases, though the Fed has set a high economic bar for a withdrawal of stimulus.

The Australian bond market delivered positive return in July as the Australian Government Bonds rallied across the curve over the month. Credit spreads were broadly, trading in a tight range over the month. The Bloomberg AusBond Composite 0+Yr Index returned 1.76% in July. The Australian 3 year government bond yields rallied 17bps to 0.24% while 10 year bonds were 34bps lower in yield, to 1.18% - as the ongoing outbreak of the delta variant resulted in lockdowns across Australia weighing on near-term expectations of the RBA’s tapering plans. The spread between Australian and US 10 year government bond yields flipped negative again, ending the month at a spread of -4bps (from +5bps at the end of the prior month).

Our overall short duration positioning detracted from relative performance as global yields fell. Within duration management, underweight positioning in the US and UK markets was a detractor, while the overweight to Chinese sovereign bonds contributed positively. Elsewhere, our exposure to New Zealand made a positive contribution, with inflation linked bonds rallying, and the NZD appreciating relative to the AUD. Our overweight position in corporate credit detracted slightly from relative performance, as spreads widened in global credit markets, outweighing the extra yield (“carry”) generated.

## Outlook

While we remain broadly optimistic on the outlook for global growth given easy fiscal and monetary policy settings, the economic risks resulting from outbreaks of the more contagious delta strain of COVID-19 suggests recovery will continue to be uneven across both global economies. In this regards the varied pace of rollout of COVID-19 vaccines across countries, and the impacts emanating from any further genetic mutations, will continue to be a headwind to more robust growth and inflationary pulses.

Although we expect inflation to move higher on stronger growth and ongoing supply bottlenecks, it is not expected to be sufficiently strong to warrant most central banks changing course in the near-term. Monetary policy settings globally remain highly accommodative, and central banks will retain these settings for some time in order to support their economies. However, we expect to see some central banks – with the US Federal Reserve in particular – discussing on a more consistent basis about when they will taper and ultimately begin to raise rates. Indeed, in NZ the RBNZ has already halted their QE program and are expected to begin hiking rates and introducing macroprudential measures in the near term. While removing excess stimulus is still some way off for other central banks, markets may become skittish if they try to get too far ahead of the expectations they have fed to markets over the past year.

In contrast to changes in messaging from the US Fed, the RBA continues to be quite resolute in signalling that it will continue to pursue an accommodative monetary stance for some time. The excess liquidity that is being generated should continue to support the local bond market and act as a counterbalance to currency strength.

Risk assets across-the-board continue to perform well. Within credit, we expect investor demand to remain strong in an environment where official cash rates are at or close to zero and investors globally continue their reach for yield. Explicit support for high quality credit from central banks in the US and Europe will also underpin demand and is likely to help keep a ceiling on any spread widening episodes. Based on this backdrop, we expect the Australian corporate credit market will continue to perform reasonably well.

## Client Services

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