

Altius Bond Fund

Fund Update 30 June 2021

Altius Asset Management employs a diversified strategy to fixed interest funds management that aims to take advantage of the mispricing of bonds in all market conditions.

Performance as at 30 June 2021

	1 mth %	3 mths %	1 yr %	3 yrs % p.a.	5 yrs % p.a.	7 yrs % p.a.	10 yrs % p.a.	Since inception % p.a.
Total return	(0.16)	0.38	(0.48)	1.53	1.66	2.27	3.53	3.54
Benchmark	0.35	0.77	(0.32)	2.49	2.13	2.73	3.45	3.46
Excess to benchmark	(0.51)	(0.39)	(0.16)	(0.96)	(0.47)	(0.46)	0.08	0.08

Inception date for performance calculations is 14 June 2011.

Total returns are calculated after fees and expenses and assume the reinvestment of distributions. Past performance is not a reliable indicator of future performance.

Effective 1 July 2016, Benchmark is 50% Reserve Bank of Australia Cash Rate and 50% Bloomberg AusBond Composite 0+Yr Index and applied retrospectively for all periods.

Excess to benchmark is calculated on Total return.

Portfolio Performance and Activity

The key themes over June were the significant flattening of both the domestic and US curves and the reduced fear of markets concerns about inflation risk. The domestic curve started the month at 1.43% and fell to 1.07%. Three year rates rose 0.25% to 0.465% following a significant change in the markets expectations that the Reserve Bank will commence tightening rates as early as 2022 while 10-year rates fell 0.11% to 1.47%, driven by reduced inflationary fears in both the US and domestic economy. The flattening of the curve was a key driver for the Fund's underperformance with our expectations that inflationary pressures will grow with improved economic data and employment numbers. At the end of the month the Fund maintained its short duration position of 1.91 years.

US inflation data and expectations continued to surprise on the upside but was offset by a poor employment report. While inflation data was high, markets become more comfortable with the Fed's view that inflationary pressures were only transitory. The US Federal Open Market Committee (FOMC) surprised markets with the Fed dots implying two rate hikes in 2023 while inflation forecasts were only 2.20%, well under market expectations. Immediately post this meeting, long end rates pushed lower while short rates rose.

Key data releases over the month were both the domestic and US employment numbers. While the US payrolls report disappointed with the 559,000 jobs created being well below expectations, it was the local employment numbers that surprised with 115,000 jobs versus expectation of 30,000, driving the unemployment rate to 5.1%, a pre-pandemic low. Following this report and coupled with the FOMC outcome, domestic banks began to change their RBA views, including the timing of the first-rate hike and the tapering of their QE program. The impact was the first leg of the significant curve flattening that occurred throughout June.

Credit spread tightened marginally over June with investor sentiment remaining strong. Financial spreads fell roughly 0.03%

while non-financials fell 0.01% to finish at 0.53% and 0.85% respectively. With many corporates taking the opportunity to issue several months ago, it meant primary markets were extremely quiet. REIT's and Financials dominated issuance with Charter Hall LWR returning to the market to issue \$267m of 8.5 years at a margin of 1.25% and LendLease International Towers Sydney issuing \$200m of 9 years at 1.40%. While on the financial side, Teachers Mutual issued \$100m for 5 years to refinance their July 2020 maturity at 0.68%. Teachers Mutual remains a preferred regional bank from our sustainability view, and as such we participated in the transaction. Bendigo Bank and Macquarie round out the month with a 5-year senior and 5-year subordinated deal at 0.65% and 1.55% respectively. Over the course of the month portfolio risk to corporates was largely unchanged.

Sustainable issuance continued to grow strongly through June. Of most interest was the inaugural Wesfarmers Sustainable Linked Bond (SLB), the first such transaction in the local market. Wesfarmers set two KPIs for the transaction. The first KPI focused on renewables and emission reductions with a commitment to source 100% of electricity requirements from renewables for its retail businesses by December 2025. The second KPI focused on nitrate production and limiting emission intensity to 0.25 tonnes of CO₂ of ammonium nitrate produced, or lower. If Wesfarmers fails to meet either target, the coupon on the bond increases by 0.125% for each KPI. We believed both KPIs meet the objectives of the SLB principles, and as such, an investment was made for the Fund. CPP Investment (Canadian Pension Fund) issued a 7-year green bond with a focus on renewables, sustainable water and green buildings. While IDB Invest, a member of the IADB Group which focuses on Latin America and the Caribbean, issued a 5-year social bond.

Outlook

Australia is well advanced in its recovery. Successful virus containment has allowed the economy to open more quickly than anticipated, but we expect virus mutations and the nature of the

pandemic to be with us for some time. Virus outbreaks and related restrictions are definitionally unpredictable, thus providing a backdrop of some volatility.

Central banks are universally supportive, but keen to ensure a recovery lifts inflation to target levels not seen over the last decade. This biases cash rates to remain low until inflation actually appears, but markets will be more forward-looking, meaning longer dated interest rates can drift higher, albeit dampened by the ongoing central bank bond buying programs.

Despite the rise in underlying inflation expected to be temporary, the US has seen a larger lift than expected. The narrative of the Federal Reserve has evolved to suggest the lift may be a little more persistent.

Australia's position is rather more idiosyncratic. Closed borders mean virtually no workers coming from overseas combined with the historically high participation rate, there are pockets of wage pressure emerging. Although no widespread wage lift has been seen in official data, anecdotal evidence suggests that the labour market is tightening a little quicker than the RBA has forecast. The RBA has significantly revised up expected growth rates for 2021 to 4.75%. Unemployment is expected to fall to 5% by year end.

The RBA is embarking on the slow process of unwinding its emergency settings, whilst hoping to spark a healthy measure of inflation. So as not to allow an unhelpfully high Australian dollar, official cash rates are unlikely to lift ahead of the US increasing cash rates. However, reflecting the improved backdrop, the RBA has decided to not extend its Yield Curve Control point beyond the current maturity (April 2024 Government Bond) at 0.1%. Given smaller government budget deficits, the RBA has been able to trim the volume of its bond purchases. Consequently, we expect some upward recalibration to interest rates, with 10-year yields moving higher to around 1.9% by year end.

The Fund's exposure to inflation-linked bonds caters to the likely lift in headline inflation from the rebasing effect of the depths of "COVID-19 shutdown" passing, and as a hedge against expectations of wage increases.

Intermediate maturity semi-government and corporate bonds continue to have attraction given the "roll down" of their very steep yield curves. The global "hunt for yield" born of ultra-low cash rates continues to support the high grade corporate and semi sectors.

Sector Profile

Asset Class	Portfolio %	Benchmark %
Australian Commonwealth Government	6.44	28.65
Supranationals	15.06	4.63
Industrials	17.06	2.08
Financials	18.63	1.50
Asset Backed	9.62	0.00
Agencies	10.59	0.14
11am	0.97	0.00
Cash at Bank	0.69	0.00
RBA Cash	0.00	50.00
Semi Government	20.95	13.00

Ratings Exposure

Rating	Portfolio %	Benchmark %
AAA	44.39	33.13
AA+ to AA-	27.90	14.31
A+ to A-	13.65	1.39
BBB+ to BBB-	14.06	1.17
RBA Cash	0.00	50.00

Maturity Profile

Term	Portfolio %	Benchmark %
0 - 1 year	5.59	52.70
1 - 3 years	28.23	10.17
3 - 5 years	22.40	9.66
5 - 7 years	17.67	9.66
7+ years	26.11	17.81

Top 10 Issuers

Issuer	Portfolio %	Benchmark %
NSW Treasury Corp	11.13	3.09
Nationl Housing Fin Invt	10.60	0.05
Australian Government	6.44	28.25
Asian Development Bank	4.94	0.40
Treasury Corp Victoria	4.34	2.78
Queensland Treasury Corp	3.28	3.09
Inter-American Devel Bank	3.22	0.33
UBS Ag Australia	2.92	0.04
Intl Bank Reconstruction & Development	2.21	0.35
McDonalds Corp	1.89	0.00

Portfolio Summary Statistics

	Portfolio	Benchmark
Yield to maturity (%)	1.17	0.58
Modified duration (years)	1.91	3.02

Fund snapshot

APIR code	WFS0486AU
Inception date	14 Jun 2011
Distribution frequency	Quarterly
Minimum initial investment	\$5,000
Fund size (net asset value)	\$133.39m
Management fee*	0.46% p.a.
Buy/Sell spread	0.00%/0.10%
Advice fee	Available

*Refer to the Fund's Product Disclosure Statement for more details on the Fund's management costs which also include recoverable expenses and indirect costs. Total management costs may vary.

Ratings / Awards



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