

# Macquarie Real Return Opportunities Fund

(formerly Macquarie Multi-Asset Opportunities Fund)

Monthly report – 28 February 2023

## Investment objective

Aims to provide positive returns of 3% to 5% per annum above Australian inflation<sup>1</sup> over the medium term (before fees). It also seeks to provide regular income.

<sup>1</sup> Defined as the Consumer Price Index (CPI) as measured by the Reserve Bank of Australia Trimmed Mean and as published by the Australian Bureau of Statistics.

## Key information

### Fund details

APIR code	MAQ3069AU
Inception date	30 September 2013
Fund size	\$495.3m
Distribution frequency	Monthly
Management fee*	0.70% pa
Minimum investment (Direct)	\$20,000
Unit prices and spreads	<a href="https://www.macquarie.com.au/unit_prices">macquarie.com.au/unit_prices</a>

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

## Fund statistics

Credit duration	1.5 years
Interest rate duration	4.2 years

## Fund performance to 28 February 2023

	Total Fund return (gross)	Total Fund return (net)	Benchmark return	Total excess return (net)	Australian inflation
<b>1 month (%)</b>	-1.21	-1.26	0.24	-1.50	0.56
<b>3 months (%)</b>	-0.48	-0.66	0.76	-1.42	1.70
<b>1 year (%)</b>	-2.79	-3.47	1.76	-5.23	6.98
<b>3 years (% pa)</b>	3.08	2.36	0.66	1.70	3.61
<b>5 years (% pa)</b>	5.06	4.31	1.05	3.26	2.80
<b>Since inception (% pa)</b>	4.81	4.02	1.60	2.42	2.47

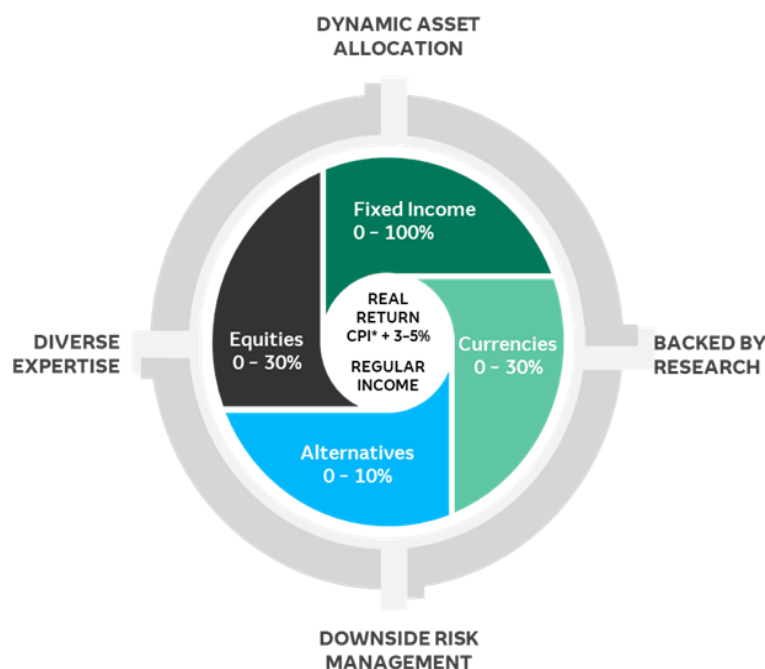
**Past performance is not a reliable indicator of future performance.**

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.

Benchmark is Bloomberg AusBond Bank Bill Index.

## Asset allocation



Sector	Security Type	Fund (%)
Fixed income and cash	Investment grade credit	38.8
	Structured securities	3.6
	High yield credit / Emerging markets debt	10.9
	Cash and government bonds	34.1
Listed equities	Australian equities	2.4
	International equities	0.5
Alternatives	Alternative assets	9.7

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## Fund performance and positioning

The Fund delivered a negative return over the month, which was driven by the Fund's allocation to both growth and defensive assets.

## Asset allocation changes

In February, hedged international and Australian equities performed negatively with volatility increase significantly, detracting -1.6% and -2.6% respectively. With regard to fixed interest, the sector also delivered a negative result, detracting -1.4% domestically and -1.7% offshore. Finally, our global real estate and global infrastructure asset also delivered negative result, both detracted -3.6%. Markets were driven by inflation surprises to the upside during the month, which markedly increased the terminal cash rate in both the US and Australia.

Our Model Portfolio maintained a defensive stance close to the maximum allowable level. Given the market conditions, we continue to anticipate the possibility of increased volatility and plan to maintain this position for the time being. However, if growth assets show significant improvement in valuation or global monetary policy becomes less aggressive, we will re-evaluate and adjust our focus to seize upside opportunities within growth assets.

The put-option protection in Australia equities we acquired last month provided reasonable protection as the market began to decline. We also increased Australian duration exposure, as the 10-year yield climbed sharply over the month to close to 4%. Over the next few months, we will continue to focus on managing downside risks while remaining alert to growth asset valuations.

## Asset allocation strategy and outlook

Investment sentiment and market volatility continues to be driven by developments in inflation, labour markets and the trajectory of monetary policy. In the US, higher than expected inflation as well as the very strong labour report pushed up market expectations of the terminal federal funds rate from 4.8% to 5.3% in July 2023.

In Australia, the strong consumer price index (CPI) print at +7.8% also led to a more hawkish Reserve Bank of Australia (RBA). Market pricing for the terminal RBA cash rate increased sharply from 3.6% to 4.3%, with expectations for the tightening cycle to peak in August 2023. This resulted in negative impacts on valuations across asset classes. Over the coming months, we expect to see elevated volatility across both defensive and growth assets driven by volatility in the inflation report, as well as a possible deterioration in consumption, the labour market, and weaker corporate earnings.

Over the past 6 months, a large portion of the disinflationary force in the US was driven by falling prices for goods. Goods account for a quarter of the Personal Consumption Expenditures (PCE) Price Index, the US Federal Reserve's (Fed) preferred inflation measure. Housing, which accounts for approximately a quarter of the PCE, continued to rise. However, there is relief on the horizon as rental prices for new leases are resetting lower, in the US. As a result, we expect the housing component will be a disinflationary force in coming months. Importantly, core services excluding housing, which accounts for just over half of total inflation (PCE), remains uncomfortably high at circa 4%. Given the strength in the labour market, we think wage pressure will remain high, supporting service sector inflation to remain sticky at high levels. Subsequently, if the price of goods stops falling, and/or the price of housing does not fall as much as the market anticipates, the inflation series will see volatility. These 'surprises' may have significant implications for cash rates and asset prices.

In terms of consumption, we continue to witness increasing credit card debt and declines in the savings rate in the US. Credit card delinquencies are rising albeit still below their pre-pandemic levels. A record level of credit card debt (at over \$1 trillion) and declining savings suggests that the current level of consumption cannot be maintained for long. Given how tight the labour market is, with a portion of workers who yet to return to the workforce since the Covid19 pandemic, we struggle to see much room for aggregate income to improve. In an environment where income is capped, interest costs are rising, savings are falling and credit card balances are growing, it would be logical to conclude that consumption will need to fall to bring household budgets back into balance. With expectations for the current cash rate in the US to rise further, coupled with declining consumption, cost-cutting measures may be the most probable path forward to stabilise and/or improve corporate earnings. However, this approach may also lead to higher levels of unemployment and a recession.

Furthermore, there is a clear disconnect between the Fed's stated intention to increase interest rates and market participants' expectations for a cut in rates in H2 2023. This disconnection is likely to result in sustained market volatility throughout the year in both growth and defensive assets.

In terms of tail-risks, we have previously highlighted that sustained high level of interest rates increases the probability of such events. We have observed continued stress in the crypto space, a significant valuation gap between listed and unlisted assets, leading to large redemptions for unlisted asset managers seeking to price arbitrage on the revaluation lag for unlisted assets. Additionally, banks and financial institutions, such as Discover Financial Services, one of the largest credit card issuers in the US, are increasing their provisions in anticipation of higher credit losses as the US economy weakens.

To sum up, the current market conditions have demonstrated a significant level of volatility across major asset markets, and we anticipate this trend to persist in the future. Our analysis suggests that while the risk of continued increases in the rate of inflation has reduced, inflation will likely remain elevated above central banks' price stability targets. The disconnect between the Fed's interest rate policy and market expectations, as well as the rise of tail risks, all pose significant downside risks to growth assets. Additionally, we have seen a decline in corporate earnings and an increase in expected credit loss provisions. We believe that in the coming months, market participants will increasingly focus on recession risks rather than inflation risks. Although the recent strength of economic data in the US suggests that the recession timeline has been pushed out further, it also implies that the duration for which our portfolio remain at a maximum defensive level could be longer. This may also mean that our investors need to endure a higher level of volatility as well as uncertainty for a longer period of time.

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**For more information speak to your financial adviser, call us on 1800 814 523, email [mam.clientservice@macquarie.com](mailto:mam.clientservice@macquarie.com) or visit [macquarieim.com](http://macquarieim.com)**

## Important information

Macquarie Investment Management Australia Limited ABN 55 092 552 611 AFSL Licence 238321 is the issuer of units in, and responsible entity of the Fund. Macquarie Investment Management Global Limited ABN 90 086 159 060 AFSL 237843 is the investment manager of the Fund.

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