

Antares Income Fund

Monthly Investment Report

February 2023



Fund Performance

Period Ended 28/02/2023	1 Mth %	3 Mths %	1 Yr %	3 Yrs %	5 Yrs %	7 Yrs %	Since Inception %pa ¹
Antares Income Fund	0.57	1.76	1.52	1.14	1.54	1.95	2.14
Bloomberg AusBond Bank Bill Index	0.24	0.76	1.76	0.66	1.05	1.29	1.59
Difference	0.33	1.00	-0.24	0.48	0.48	0.66	0.55

Valuation at month end was \$217,559,371.41

Antares Income Fund returns are expressed after investment management fees and before taxes; The difference in returns between the Fund and the benchmark may be out due to rounding; 1. Since Inception 31/01/2013

Key Characteristics at 28/02/2023

	Fund	Benchmark
Interest Rate Duration (yrs)	0.03	0.12
Yield to Maturity*	4.82	3.45
Credit Spread Duration (yrs)	2.12	-
Average Credit Rating	A	-
Liquidity**	69%	N/A

*Estimated return if held to maturity. Market yield for Fixed Rate Bonds whilst FRNs uses a swap assumption rate as an input.

**Liquidity deemed available within 24 hours. Consisting of: (1) Cash and short-term securities, government & semi government bonds that are expected to be able to be liquidated at mid-market yields and thus no transaction costs, and; (2) Unit holdings of other Antares managed sub funds for which there is no buy/sell spread and next day redemption facility if notified by 2pm.

Rating Exposure (by market value %)

Asset Type	MV %
AAA	15.03%
AA+	1.04%
AA	5.66%
AA-	25.51%
A+	5.53%
A	1.30%
A-	11.96%
BBB+	17.88%
BBB	16.10%
BBB-	0.00%

Investment Return Objective

The Antares Income Fund aims to provide investors with a regular income and a return (after fees) that exceeds the Bloomberg AusBond Bank Bill Index over rolling three-year periods.

Distribution History

Distribution Information	Date
Distribution Date	31-Dec-22
Distribution Amount	0.62 Cents Per Unit
Next Distribution Date	31-Mar-23

Portfolio Review

Key Drivers of Portfolio Performance:

- The 3-10 yield curve bear flattened as rates sold off, detracting from returns.
- Corporate spreads narrowed 5-10bps, contributing strongly to positive excess returns.
- Sub debt tightened 10bps, adding 3bps to excess returns.
- Yield enhancement and rolldown of quality investment grade bond holdings added to returns.

Portfolio Activity and Positioning

- Bought Westpac Feb 2028 new issue.
- We have maintained the liquid structure of the Fund.

Portfolio Strategy

Strategy	Implementation
<p>Duration and Yield Curve: Continued strong economic data and sticky inflation has pushed recession risks out to 2024 and increased terminal pricing.</p> <p>Looking forward, our scenario analysis continues to highlight risks to structurally higher long-term inflation and stagflation risks as the economy begins to reflect the impact of an aggressive rate hiking cycle.</p>	<ul style="list-style-type: none"> Yield curves bear flattened in February, driven by continued upside surprises in global economic data and sticky inflation, reiterating hawkish rhetoric from central banks of the need for higher rates for longer. Terminal rates moved 50bps higher in both the US and Australia in response and markets pared back rate cut expectations for 2023, extending the timeframe to reach a pivot in the rate cycle. Front end yields have moved higher with expectations of central banks continuing to tighten policy, giving confidence to market participants that central banks will bring inflation back down to 2%. This confidence has kept long term breakeven inflation rates anchored within target. Over the medium to long term, we see structural inflation risks which may challenge central bank's ability to maintain inflation within the 2-3% target band. Yield curve: With terminal cash rates rising and long-term inflation expectations remaining anchored for now, we continue to favour a strategic curve steepening view, reflecting the potential risks of structurally higher long-term inflation which is not currently being priced by markets. However, given the possibility of recession risks being pushed out into next year and beyond due to the continued resilience in the economy, we may look for opportunities to reduce curve steepening positions across portfolios that use derivatives. Duration: We are positioned between neutral and short duration across mandates depending upon mandate objectives. If bond yields continue to rise, we will look to reduce short duration positions opportunistically as we move closer to the end of the rate hiking cycle.
<p>Credit exposure: Our scenario analysis points to risks of recession and stagflation that make us more selective about credit exposure in portfolios.</p>	<ul style="list-style-type: none"> Valuations: Credit outperformed in February, reflecting decreased recession risks from ongoing resilience in the economy and the labour market. We are focusing on high quality credit, targeting credits in the 3-5yr area where yields are attractive, which has seen some recent new issuance from major banks. High quality issuers: We are targeting credits with low leverage, strong cashflows, some pricing power and robust balance sheets, i.e., issuers that are less exposed to inflation and recession risks. Synthetic credit: iTraxx traded below 90 in February after reaching highs of around 150 in October. We will continue to monitor credit protection and the broader macro-outlook to potentially buy protection for those portfolios that can use CDS.
<p>Optimising yield through carry and rolldown: Focusing on high quality credits and inflection points on steep curves.</p>	<ul style="list-style-type: none"> Portfolio construction: We are using our proprietary analytics to harvest attractive rolldown while maximising opportunities per unit of risk. Rate and swap term premia: For long maturity portfolios we see value in semi-government bonds in 8-15yrs versus Commonwealth government bonds. Credit term premia: Recent major bank issuance in the 3-5yr area has value in the major bank curve and created attractive switch opportunities between shorter bonds and newly issued 5-year bonds.
<p>Liquidity: Where appropriate, we are maintaining liquidity that can be realised in stressed conditions.</p>	<ul style="list-style-type: none"> Portfolio construction: Selective semis, major banks and government bonds are seen as core liquidity building blocks across portfolios. We have maintained the liquid structure of Funds where appropriate.

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Market Review

February was characterised by continued stronger than expected global economic data, sticker core and services inflation, strong labour markets and more hawkish higher rates for longer rhetoric from the Fed and other central banks. This has meant markets have pivoted from expecting that central banks were approaching the end of the hiking cycle, that peak inflation had past and a likely soft economic landing this year, to the prospect of reflation and an extended hiking cycle. As a result, markets repriced terminal rates higher and pulled back on rate cut expectations for this year.

In the US, unemployment reached a 50-year low, reiterating the strength of the labour market. After a spectacularly strong US payrolls print, markets also pushed out the timing of recession risks. Wages growth also remained strong, with the Fed acknowledging that the current level of wages growth is inconsistent with their 2% inflation target. This highlights the challenge central banks face in determining appropriate monetary policy settings to create a sufficient tightening in financial conditions to bring inflation back down to target while balancing the impact on the economy.

The Bank of England and European Central Bank both hiked 50bps in February and flagged further hikes after upgraded growth forecasts and higher than expected inflation across the Eurozone.

The RBA maintained its 25bps hike cadence after monthly CPI data suggested inflation had peaked, unemployment rose, tighter financial conditions impacted household consumption, and softer Wage Price Index (WPI) data suggested the risks of a wage price spiral remain low for now. However, it is recognised there was some seasonality in the unemployment data and limited scope of the monthly CPI and WPI metrics.

As at the end of February global and domestic credit spreads remained contained with recession risks being pushed out off the back of continued strong economic data over the month.

At the time of writing in March, bonds have become extremely well bid with global rates led by the US rallying aggressively. This follows reporting of at least two regional bank failures in the US and rising concerns of systemic contagion. With financial stability concerns dominating over economic and inflation risks, policy rates moved sharply lower. Fed fund expectations collapsed, and at one stage terminal fed funds were 100bps lower at 4.5%.

Moving largely in sympathy with the US, expectations for the RBA have also moderated lower in what was already a more dovish stance taken by the central bank at its March meeting. The rapid unwinding of policy rate expectations may point to a potential pause from the RBA at its coming meeting, but this is unlikely to be the end of the matter with important data ahead.

The situation in US banking remains fluid and the consequential repricing of risk globally is an evolving situation. Regulatory authorities have sought to get ahead of the situation by putting in stop-gap measures aimed at keeping deposits whole and preventing a broader run-on the banking system.

Macro Outlook

Central banks have reached a juncture after the most aggressive hiking cycle in decades have yielded limited impact on fighting spot inflation. The key question for monetary policy makers now is how much higher cash rates need to go to create sufficiently restrictive conditions to bring inflation down to 2%.

Given continued strong economic data, the current hiking cycle has some way to go to take the heat out of a resilient labour market, contain wages pressures and reign in services spending, driving core inflation. Hawkish Fed rhetoric over February reiterates that a more protracted hiking cycle is required to mitigate the risk of inflation becoming structurally embedded. The RBA has taken a less clear path with its recent dovish tones.

Antares Scenario Analysis

The Antares Scenarios table below reflects the interplay between growth, inflation, and bond yields, and how they will drive the level and shape of yield curves in the different scenarios.

Scenarios	AU GDP	AU Inflation	1YR Bond	AU 3YR Bond	AU 5YR Bond	AU 10YR Bond	AU 30YR Bond	US 10YR Bond	iTraxx
Strong Growth	5.00%	4.50%	5.50%	5.75%	6.00%	6.50%	7.25%	6.50%	150
Above Trend	4.00%	3.50%	4.75%	4.50%	4.25%	4.25%	4.50%	4.50%	110
Trend	3.00%	2.50%	3.50%	3.50%	3.50%	3.75%	4.00%	3.75%	75
Below Trend	1.50%	2.00%	2.50%	2.50%	2.50%	2.50%	2.75%	2.00%	100
Recession	-2.00%	0.50%	0.25%	0.50%	1.00%	1.50%	2.25%	1.25%	250
Stagflation low growth/high inflation	1.50%	4.00%	4.00%	4.25%	4.75%	5.25%	5.75%	5.50%	150
Stagflation -ve growth/high inflation	-1.50%	3.50%	2.75%	3.25%	4.00%	4.75%	5.75%	4.75%	150
MK Latest Fair Value (FV)	1.90%	3.25%	3.65%	3.78%	4.03%	4.38%	4.80%	4.45%	119
Market Yield Latest			3.53%	3.23%	3.30%	3.52%	3.94%	3.74%	97.90
FV - Market (+ exp / - cheap)			0.12%	0.55%	0.73%	0.86%	0.87%	0.71%	21

Antares continues to have a greater than 50% probability weighting to structurally higher inflation outcomes; 40% probability being assigned to the stagflation scenario of higher inflation with weak/negative growth (Scen 6); and 15% probability of higher inflation with strong growth (Scen 1 & 2). After the 20-35bp rally in March (post SVB collapse), current market yields are looking very expensive versus Antares' Fair Values (FVs) +55bps to +85bps, with 3yr bonds still looking the best value. The aforementioned are weighted average FVs and it should be noted that there is a wide dispersion of potential yield levels under the various scenarios.

Interest Rate & Inflation Outlook

The rally in bonds seen in January gave way to an almost complete round-trip in yields selling off over February and early March. Expectations for both the Fed and RBA policy rates ratcheted up materially over the month. The RBA raised the cash rate at the February meeting by 25bps to 3.35%, signaling further rate hikes over coming months. This marked a hawkish turn in the policy stance of the RBA relative to more qualified statements made in December.

While the pivot appeared to be driven by a solid Q4 CPI report, a soft path of data followed and appeared once again to change the narrative. Subsequent to the February decision, the Q4 GDP report, wage price index, January labour report and January CPI pointed to some cooling in the economy. As a result, forward cash expectations were pared back to 4.10% and following a dovish statement from the RBA's March meeting (and another 25bps hike to 3.60%), cash rate expectations were pared back further, to remain below 4% at the time of writing.

The contrast with the Fed could not be more stark, with the Fed looking to hike further and more aggressively, considering a return to 50bp increments. The resurgence of headline inflation and the strength in the labour market underpin the Fed's renewed concern.

In the interim, inflation expectations have lifted globally, although Australian BEIs have struggled to pierce through 2.50%. US BEIs have performed strongly with 10 year BEIs rising 13bps to 2.43% only to be eclipsed by shorter tenor BEIs. 2yr inflation expectations rallied from 2.33% up to 3.18% over February, underscoring the challenge facing the Fed.

Credit Outlook

Credit markets were resilient in February despite hawkish central bank messaging. US IG spreads widened 5bps, European IG spreads remained unchanged, and Australian credit spreads tightened 7bps. High yield continues to perform with US high yield remaining unchanged and European high yield tightening 25bps. Synthetic credit moved 10bps wider for IG and 30bps wider for high yield, but has since rallied back to the level similar to the beginning of February.

Flows into bonds continue with IG having seen a 13 week inflow streak since Oct 2021. However, money is flowing out of the riskier part of the market with high yield and EM debt having all experienced outflows during February.

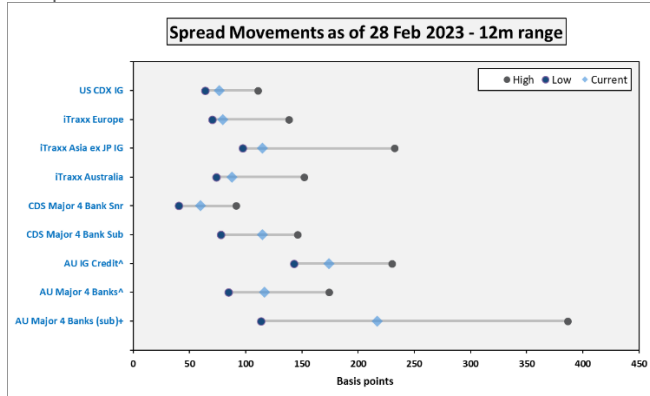
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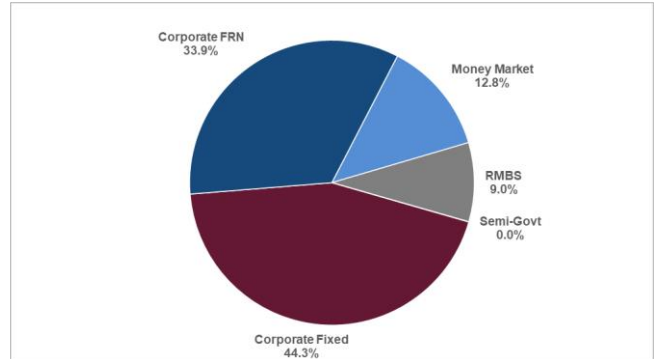
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The latest reporting season showed that, in aggregate, corporates in Australia and the US are still experiencing positive revenue growth. However, their earnings have turned negative, indicating companies are starting to feel the pinch of a tightening profit margin as they struggle to fully pass on the cost of inflation to end consumers.

Currently, although fundamentals and flows are still constructive on credit (for now) we see valuations becoming less attractive whilst financial conditions tighten with central banks continuing on their rate hike path.



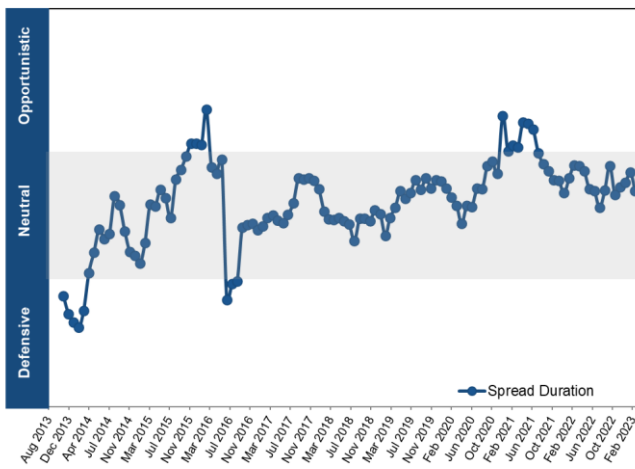
Sector Breakdown (Market Value %)



ESG

ESG analysis is reviewed regularly for material changes to the issuer's credit profile, as well as the effectiveness of the risk mitigants in place to manage such risk. For the month of February, our fundamental credit assessment process did not uncover any concerns around an individual issuer's ESG risk. Therefore, no action was required.

Defensive to Opportunistic





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About Antares Fixed Income

Antares Fixed Income (Antares) is a specialist fixed interest manager covering a range of domestic and international securities. Antares has managed fixed interest and cash portfolios for investors since 1990 and currently has over A\$25.41 billion* in funds under management across a range of cash management, fixed income and liability driven investment strategies. Antares is focused on delivering performance objectives for its clients within a carefully managed and defined risk framework.

*as at 30 June 2022

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