Antares Income Fund

Monthly Investment Report
November 2022

antares

Fund Performance

Period Ended 30/11/2022	1 Mth %	3 Mths %	1 Yr %	3 Yrs %	5 Yrs %	7 Yrs %	Since Inception %pa[1]
Antares Income Fund	0.22	0.49	-0.16	0.70	1.30	1.76	2.00
Bloomberg AusBond Bank Bill Index	0.25	0.64	1.01	0.49	0.99	1.26	1.55
Difference	-0.03	-0.15	-1.16	0.21	0.31	0.50	0.45

Valuation at month end was $199,624,803.69
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 30/11/2022

	Fund	Benchmark
Interest Rate Duration (yrs)	0.14	0.13
Yield to Maturity*	4.73	2.99
Credit Spread Duration (yrs)	2.07	-
Average Credit Rating	A	-
Liquidity**	72%	100%

*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	14.69%
AA+	1.07%
AA	6.03%
AA-	21.37%
A+	3.89%
A	1.27%
A-	13.62%
BBB+	20.47%
BBB	17.61%
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	30-Sep-22
Distribution Amount	0.40 Cents Per Unit
Next Distribution Date	31-Dec-22

Portfolio Review

Key Drivers of Portfolio Performance:

- A curve flattening position at the front end of the curve added to returns, while a 3s10s steepener detracted
- Corporate spreads narrowed, contributing to returns
- Senior banks narrowed, contributing to returns
- Bank sub debt widened, detracting from returns
- CDS protection detracted 8bps as iTraxx tightened 40bps
- Yield enhancement and rolldown of quality investment grade bonds added to returns.

Portfolio Activity and Positioning

- Bought NAB 11/25 hedged with 3yr futures
- We have maintained the liquid structure of the Fund.

Portfolio Strategy

Strategy	Implementation
Duration and Yield Curve: Our scenario analysis points to an increasing probability of structurally higher inflation for longer with a potential bear steepening of yield curves if central banks are unable to contain longer term inflation expectations. However, aggressive tightening by central banks to contain inflation may have a significant impact on economic growth, creating a "stagflation" environment.	• The market has a strong assumption that inflation will return to pre covid levels of 2-3%. A key risk we see to this market expectation is that many of the structural drivers keeping inflation low during the post GFC (pre-COVID) period have potentially moved into reverse, supporting the case that the longer-term structural level of inflation is higher. • **Yield curve:** We think shorter bonds are still more sensibly priced than longer bonds on a relative basis and, therefore, we continue to favour a curve steepening strategy. With the 3-10yr curve currently trading in a 30/40 range, we will continue to monitor and may look to tactically reduce some steepening positions if levels trade above 50. • **Duration:** Given our outlook, we are positioned between neutral and short duration across mandates depending upon mandate objectives.
Credit exposure: Our scenario analysis points to rising risks of recession and stagflation risks that make us concerned about credit risks in portfolios.	• **Valuations:** After widening sharply this year, credit spreads have narrowed over the past few months, reflecting the resilience seen to date in the economy and labour market despite the most aggressive rate hiking cycle in four decades. We are focusing on high quality credit, targeting credits in the 3-5yr area. • **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 is back trading at below 90 after reaching highs of around 150 in October. We will continue to monitor credit protection and potentially buy protection opportunities for those portfolios that use CDS.
Optimising yield through carry and rolldown: Focusing on high quality credits and inflection points on steep curves.	• **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 still like the steepness of semis in 10-15yrs versus Commonwealth government bonds. NSW and TCV 2037s and the new TCV 36 are our preferences. • **Credit term premia:** Recent major bank issuance in the 5yr area has markedly steepened the bank curve and created attractive switch opportunities between 2yrs and 5yrs.
Liquidity: Where appropriate maintaining liquidity that can be realised in stressed conditions.	• **Portfolio construction:** Selective semis, major banks and government bonds are seen as core liquidity building blocks across portfolios.

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Market Review

In November, yield curves bull flattened due to lower than expected US inflation, some evidence of the economic impacts of rate hikes, and China's announcement of a property stimulus package and potential relaxation of aspects of its covid zero policy despite covid cases increasing. Bond markets saw strong positive returns from term and credit.

Globally, central bank rhetoric shifted to strike a more balanced tone with both hawkish and dovish messaging as they continue to navigate between containing inflation and rising recession risks. While the Fed continued with its 75bps hikes and the RBA delivered another 25bps hike, the main shift in market sentiment over the month was that central banks are getting closer to a stage in the hiking cycle where they may be able to moderate the pace of tightening. One consequence of this is that rates may need to stay higher for longer, remaining elevated throughout 2023, especially if inflation continues to surprise to the upside. This is inconsistent with current market pricing in the US which has rate cuts priced into the back end of 2023.

Despite the continued resilience and strength in the labour market, markets remain concerned about rising recession risks. The yield differential between the 10-year US Treasury and 2-year US Treasury ended the month at -78bps. Empirically, an inverted US Treasury curve has typically preceded a recessionary period in the US.

Macro Outlook

As central banks move further into restrictive territory and higher rates start to impact the economy, their steadfast commitment to prioritising inflation over growth and employment will be tested. It is anticipated that next year will see a decrease in the pace of hikes after the fastest rate hiking cycle in 40 years. Current market pricing sees the US terminal cash rate just under 5.0% and the Australian cash rate at 3.75%.

Domestically, the key to assessing the economic impact of rate hikes this year and into 2023 will depend on the sensitivity of the consumer. The more even keel approach recently touted by the RBA will be a challenge given the high level of household debt, the largely variable rate structure of Australia's mortgage market and the potential impacts on the economy of a slowdown in the global growth outlook.

To assess monetary policy's impact on inflation, the labour market and how wage inflation plays out next year will be critical. If the labour market remains resilient, it will continue to provide a buffer, increasing the likelihood of a soft economic landing. However, if the labour market starts to soften, then this will provide evidence of tighter financial conditions leading to increased recession risks.

A key focus of central banks is preventing inflation expectations becoming embedded in pricing structures. Embedded inflation could result in a stagflation scenario where rates remain structurally higher for longer.

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	AU 3YR Bond	AU 5YR Bond	AU 10YR Bond	AU 30YR Bond	US 10YR Bond	iTraxx
Strong Growth	5.00%	4.50%	5.00%	5.50%	6.00%	6.50%	7.25%	6.50%	150
Above Trend	4.00%	3.50%	4.50%	4.50%	4.25%	4.00%	4.00%	4.25%	110
Trend	3.00%	2.50%	3.25%	3.50%	3.75%	4.00%	4.50%	4.00%	75
Below Trend	1.50%	1.50%	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%	3.75%	4.25%	4.75%	5.25%	5.75%	5.50%	150
Stagflation - ve growth/high inflation	-1.50%	4.00%	2.00%	2.50%	3.50%	4.75%	5.75%	4.75%	150
Antares Latest Fair Value (FV)	1.51%	2.95%	3.06%	3.34%	3.68%	4.05%	4.54%	3.93%	129
Market Yield Latest			**3.09%**	**3.07%**	**3.17%**	**3.36%**	**3.68%**	**3.58%**	**99**
FV - Market (+ exp / - cheap)			**-0.03%**	**0.27%**	**0.52%**	**0.70%**	**0.86%**	**0.35%**	**30**

Antares' continues to have a greater than 42% probability weighting to structurally higher inflation outcomes; 55% probability being assigned to the stagflation scenario of higher inflation with weak/negative growth (Scen 6); and 13% probability of higher inflation with strong growth (Scen 1 & 2). The sustained rally in bonds has been driven by; a strong bearish consensus in investor positioning, the lower than expected October US inflation print, slowing economic indicators and central banks messaging a slowing in the pace of the tightening cycle. Current market yields look very expensive versus Antares' fair values (FVs) (25-80bps). 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

November saw the combination of partly weaker momentum in economic data, as well as increasing speculation of a tapering in the pace of rate hikes, both here and abroad. One of the data points to highlight the potential tempering in economic strength was the Australian October monthly CPI reading. This came in at 6.9% yoy versus the previous month of 7.3% yoy, with goods inflation noticeably slowing down. Both the equity and bond markets rallied on the release, taking it as a guide that inflation is cooling and potentially that peak inflation is behind us.

The impact from the monthly CPI reading was an immediate lowering of the terminal rate with OIS pricing shifting subsequently from 75bps of hikes to 45bps of hikes for 2023. This interpretation of the monthly report, however, is open to question given the current inflation backdrop. For instance, the report only captures 52% of the CPI basket and is skewed to goods inflation over services inflation where most of the inflation pressure remains.

While there is some valuable information within the monthly CPI data, the series is still not well understood by the market with respect to its compositional effects and monthly seasonality. The October CPI reading, for instance, revealed little inflationary pressure in travel and rents, while other data sources show clear signs of strength in both categories.

BEIs showed a notable bounce into month end, although this may have had more to do with strong index related flows for the month, driving the performance of the mid and ultra parts of the real yield curve. Nevertheless, the RBA continues to project inflation to peak at near 8% by year end 2022 and remain outside the 2-3% band into 2025. In this context, another 25bps hike from the RBA is reasonably assured for December, with more work likely required for the RBA in 2023.

Credit Outlook

Credit spreads rallied across global markets in November amid signs that inflation may be easing in the US. US investment grade credit ended the month 30bps lower, while European Investment grade credit tightened by 35bps. Australian credit underperformed its global peers with the investment grade spread narrowing 11bps over the month.

Synthetic credit spreads outperformed cash bonds as rumours of China's reopening, prompted a sharp market response which saw the Asian Ex-Japan iTraxx rally 90bps and the Australian iTraxx tighten 40bps over the month.

US high yield credit tightened 15bps in November, less than investment grade credit as it had already rallied ~110bps since Septembers wide.

Looking ahead, the supportive macro backdrop which credit has enjoyed so far is showing signs of weakening with global financial conditions continuing to be tightened further. With the rising risk of a stagflationary or recessionary environment next year we remain cautious on further performance from credit spreads and have a preference to hold shorter-dated and high-quality credit.

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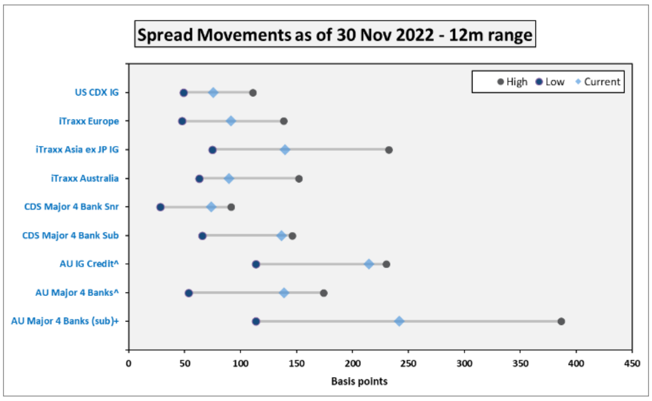
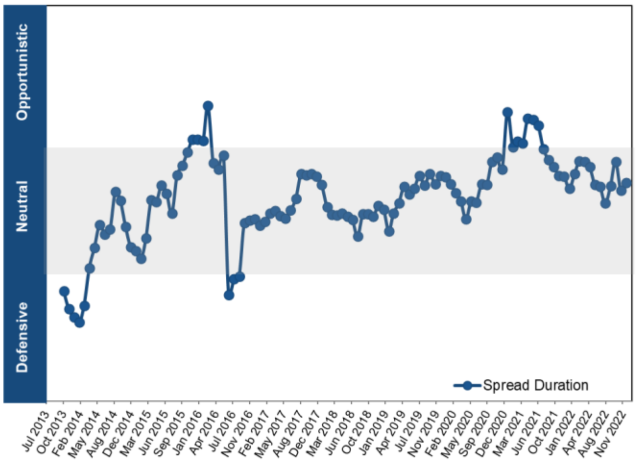
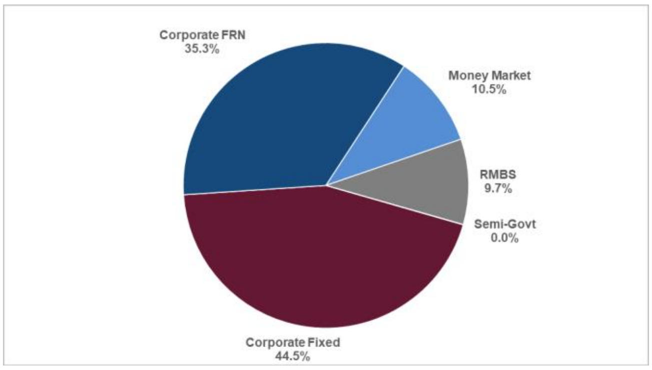


Defensive to Opportunistic



Sector Breakdown (Market Value %)



ESG

Cyber security risk is becoming increasingly entrenched in societies and a key focus for our Social risk analysis. The recent high-profile data breach incidents by several Australian corporates highlight the vulnerabilities of Australian companies in managing cyber risks. Whilst these incidents do not have any meaningful impact on our credit exposures, we have increased our engagements on this issue to get a better understanding of which part of our portfolios are most exposed to cyber risks. We have identified that our exposure to Australian banks is likely to be the most exposed to cyber risk, given the banks host large quantities of sensitive consumer information and their operations are heavily digitalized. During the month, we engaged with one of the Australian major banks to get an understanding of how banks are managing such risks – the takeout was that the four major banks are perhaps the most sophisticated in managing cyber risks amongst the Australian corporates and they invest the most in their IT systems. However, the challenges of defending cyber-attacks are constantly evolving as attackers are becoming increasingly sophisticated, which requires constant investment in systems, collaboration amongst industry groups and working with the Australian government. In this aspect, we believe the four major banks are relatively well positioned to absorb potential costs in dealing with cyber risks given their large balance sheets. As such, we assign a Moderate ESG credit impact score to banks' cyber security risk.

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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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Important information