



February 2023

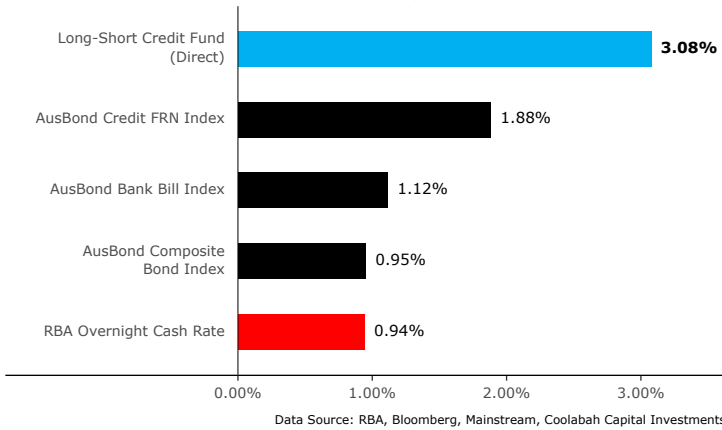
Objective: An absolute return fixed-income strategy focused on exploiting long and short mispricings in credit markets that targets high-yield like returns above the Reserve Bank of Australia (RBA) cash rate plus 4% to 6% p.a. over rolling 3 year periods with volatility of less than 5% p.a. after Management Fees, Administration Fees and Performance Fees.

Strategy: We add value via active asset-selection using a range of valuation models with the aim of delivering superior risk-adjusted returns, or alpha, to traditional hedge funds. We primarily invest in senior and subordinated debt securities, hybrids and derivatives issued by Australian entities domestically, although we can invest in these securities when they are issued overseas, or by overseas entities (into Australia or offshore). The Fund can use gearing and targets holding the majority of its portfolio in investment-grade securities. It is managed by Coolabah Capital Investments.

Period Ending 2023-02-28	Gross Return (Direct)	Net Return (Direct) [†]	RBA Cash Rate	Gross Excess Return [‡]	Net Excess Return (Direct) ^{†‡}
1 month	2.17%	2.09%	0.25%	1.93%	1.85%
3 months	4.98%	4.72%	0.76%	4.22%	3.97%
6 months	3.72%	3.21%	1.38%	2.34%	1.82%
1 year	1.66%	0.67%	1.73%	-0.07%	-1.06%
2 years pa	0.22%	-0.71%	0.88%	-0.66%	-1.59%
3 years pa	3.76%	2.10%	0.63%	3.13%	1.47%
4 years pa	4.76%	2.91%	0.73%	4.03%	2.18%
5 years pa	4.65%	2.88%	0.89%	3.76%	2.00%
Inception pa Sep. 2017	4.87%	3.08%	0.94%	3.93%	2.14%

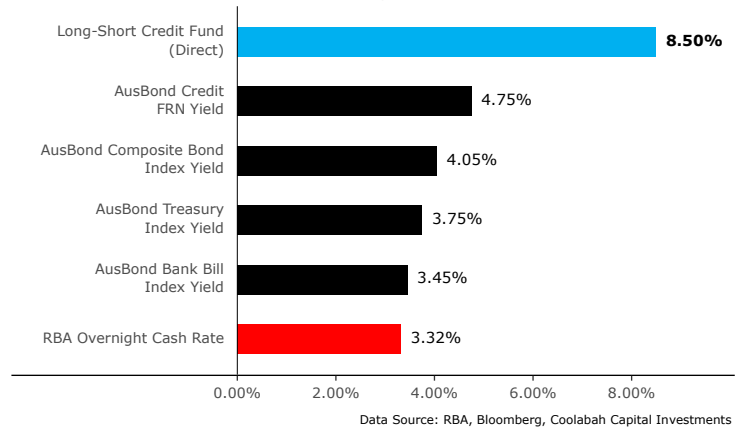
Long Short Credit Fund Returns (Net) vs Comparisons

Annualized Total Returns Since Inception in September 2017 to February 2023



Annualised Yield to Call/Maturity

28 February 2023



[†] Net returns are calculated from the historic gross returns using the current fee structure as displayed in the Product Disclosure Statement. [‡] The Excess Return columns represent the gross and net return above the RBA cash rate.

Disclaimer: Past performance does not assure future returns. Returns are shown net of all Management and Performance fees unless otherwise stated. All investments carry risks, including that the value of investments may vary, future returns may differ from past returns, and that your capital is not guaranteed. To understand Fund's risks better, please refer to the Product Disclosure Statement available at Coolabah Capital Investments' website.

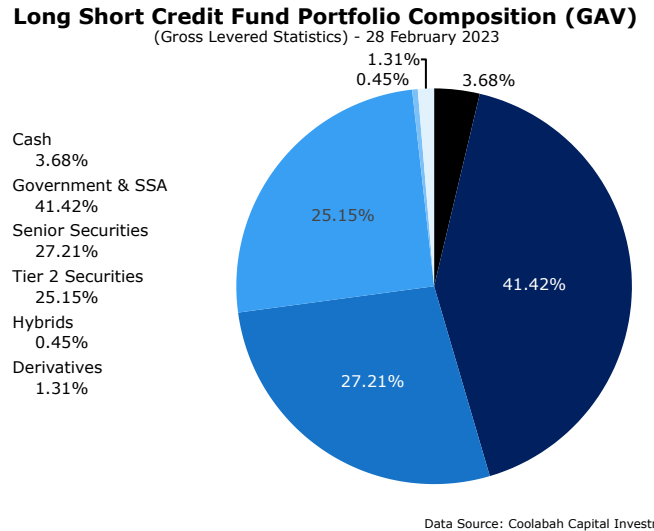
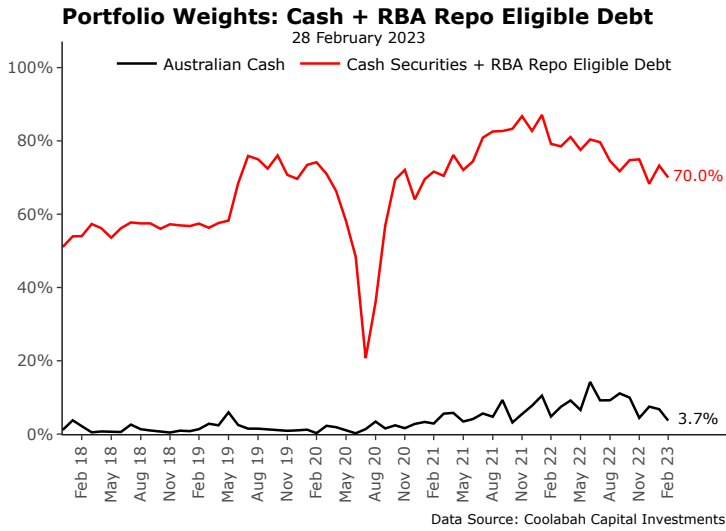
Note: all portfolio statistics other than running yield reported on gross levered value

Net Monthly Returns > RBA Overnight Cash Rate	73%	Av. Interest Rate (Gross Running Yield)	4.97%
Gross Portfolio Weight to Cash Securities	3.7%	Modified Interest Rate Duration	0.36 years
Gross Portfolio Weight to Bonds	95.0%	Gearing Permitted?	Yes
Av. Portfolio Credit Rating	AA-	1 Year Av. Gross Portfolio Weight to Cash	8.3%
Portfolio MSCI ESG Rating	A	Gross Portfolio Weight to AT1 Hybrids	0.5%
No. Cash Securities	17	Gross Cash Securities + RBA Repo-Eligible Debt	70.0%
No. Notes and Bonds	106	Net Annual Volatility (since incep.)	3.48%

Awards: FE Alpha Manager 2019: Christopher Joye; **Ratings:** Lonsec available to advisers; Recommended (Atchison); 'Superior More Complex' (Foresight Analytics)

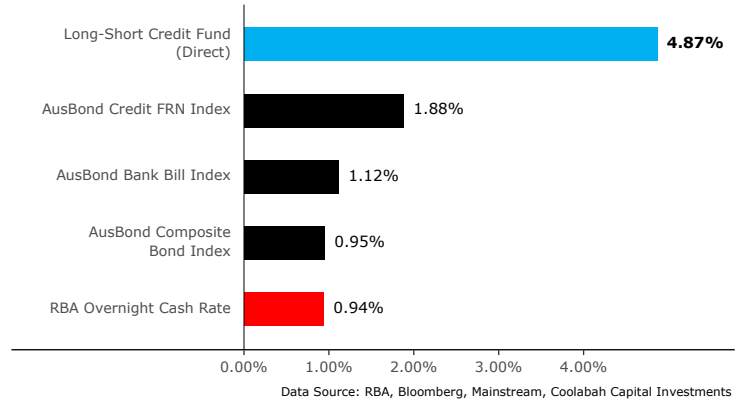


Asset weighted average rating



Long Short Credit Fund Returns (Gross) vs Comparisons

Annualized Total Returns Since Inception in September 2017 to February 2023



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The since inception gross (net) return of **4.87% pa gross (3.08% pa net)** is the total annual return earned by the fund since Sep. 2017, including interest income and movements in the price of the bond portfolio after all fund fees (assuming net returns are calculated from the historic gross returns using the current fee structure as displayed in the Product Disclosure Statement). The net return quoted applies to the Smarter Money Long-Short Credit Fund - Direct Investor Class, with quarterly distributions reinvested. Each investor's return will vary depending upon their own investment date and any top-ups and withdrawals they make. The **annualised volatility estimate of 3.48% pa** is based on the standard deviation of net daily returns since inception, which are then annualised, attributable to the Smarter Money Long-Short Credit Fund - Direct Investor Class.

Portfolio Managers	Christopher Joye, Ashley Kabel, Roger Douglas, Dr Nick Campregher (Coolabah Capital Investments)		
APIR Code	SLT2562AU	Fund Inception	31-Aug-17
ISIN	AU60SLT25623	Distributions	Quarterly
Morningstar Ticker	41597	Unit Pricing	Daily (earnings accrue daily)
Asset-Class	Alternatives/Hedge Funds	Min. Investment	\$1,000
Target Return	Net 4.0%-6.0% pa over RBA cash rate	Withdrawals	Daily Requests (funds normally in 3 days)
Investment Manager	Coolabah Capital Investments (Retail)	Buy/Sell Spread	0.00%/0.05%
Responsible Entity	Equity Trustees	Mgt. & Admin Fee	1.00% pa
Custodian	APEX Fund Services	Perf. Fee	20.5% of returns over RBA cash rate + 1.00% pa

Portfolio commentary: The zero-duration daily liquidity Long-Short Credit Fund (LSCF) ended February with a yield to call/maturity of 8.50% (assuming current funding costs), a weighted-average credit rating of AA-, and a portfolio weighted average MSCI ESG rating of A. In February, LSCF returned 2.17% gross (2.09% net), outperforming the AusBond Composite Bond Index (-1.32%), the AusBond Bank Bill Index (0.24%), the RBA Overnight Cash Rate (0.25%), and the AusBond Credit FRN Index (0.43%). Over the previous 3 months, LSCF returned 4.98% gross (4.72% net), outperforming the AusBond Composite Bond Index (-0.69%), the AusBond Bank Bill Index (0.76%), the RBA Overnight Cash Rate (0.76%), and the AusBond Credit FRN Index (1.20%).

Since the inception of LSCF 5.5 years ago in September 2017, it has returned 4.87% pa gross (3.08% pa net), outperforming the RBA Overnight Cash Rate (0.94% pa), the AusBond Composite Bond Index (0.95% pa), the AusBond Bank Bill Index (1.12% pa), and the AusBond Credit FRN Index (1.88% pa). While LSCF's return volatility since inception has been low at around 3.48% pa (measured using daily returns), as a daily liquidity product with assets that are marked-to-market using executable prices, volatility does exist. This contrasts with illiquid credit (eg, loans and high yield bonds) wherein assets that have very high risk can appear to have remarkably low volatility, which is, in fact, just a mirage explained by the inability to properly value these assets using executable prices.

Strategy commentary: In February, all of Coolabah's strategies generated substantial alpha or outperformance, as has been the case for the last 6-9 months. This has been driven by a diverse range of factors, including:

- 1. Mispriced new global bank bond issues that have come with large new issue concessions in AUD, USD, and EUR.** Since the end of October 2022, we have invested \$2.1 billion into new primary market bond issues. We have been focussed on finding cheap senior and Tier 2 bond issues in AUD, USD, and EUR. We have also allocated capital to new sovereign bond issues that have offered demonstrable new issue concessions. We think this will remain an ongoing source of alpha as issuance requirements are high amongst banks and sovereigns around the world.
- 2. Very active secondary market trading.** Over the past 4 months, we have executed \$12.5 billion of cash bond trades in global secondary markets. This has involved taking profits on existing positions and switching from lower yielding and comparatively more expensive assets into secondary opportunities with larger mispricings across the high-grade and liquid credit spectrum.
- 3. Further improvement in our underlying yields.** Central banks continue to lift cash rates and expected terminal cash rates have drifted higher. The US Federal Reserve is projected by bond markets to now increase its Fed Funds Rate to almost 5.5%. The RBA's expected terminal rate has recently increased from 3.5% to 4.2%. In the US, the 10-year government bond yield jumped from 3.50% at the start of February to finish the month at 4.0%. Over the same period, the Australian 10-year government bond yield rose from 3.55% to 3.79%. Higher cash rates and long-term yields are enhancing the yields on Coolabah's portfolios. Our RBA cash + 1.5% strategies are currently carrying annual yields to maturity of about 5.3% pa with a weighted-average A+ rating, zero duration, and daily liquidity. Our more aggressive long/short credit strategies are offering annual yields to maturity of between 9-10% pa with a weighted-average AA- rating, zero duration, and daily liquidity.

What are the big ideas that we are ruminating on right now? There are a few...

- 1. Since January 2022, we have forecast a US/global recession, and our models continue to imply that is likely in late 2023/early 2024.** Central banks are singularly focussed on demand destruction and crushing inflation back to their ~2% targets. They are actively hiking while forecasting recessions in countries like the UK and NZ. This is an existential battle for central bank credibility, and we do not think policymakers are worried about downside economic risks: they have to secure these downside scenarios to in turn deliver price stability. The Powell Put Option is well and truly dead. We do not think that a serious recession is priced into risk assets, and into equity earnings in particular. Equities have priced in the discount rate changes, but not recessionary risks, in our view.

Strategy commentary cont'd: 2. We believe that illiquidity is creating cognitive dissonance in asset pricing for the time being. With global cash rates rising above 4-5%, bank deposits paying 4-6%, many highly rated government bonds offering 4-5%, and highly rated bank bonds paying as much as 6-7%, the hurdle rates for all other asset classes have soared. Yet valuations in illiquid markets have yet to fully adjust. We are particularly focussed on commercial property, high yield bonds, and private credit. But other markets like residential property, private equity, and venture capital are also responding to this cash rate shock with a delay. If bank bonds are paying 6-7% pa with almost zero default risk and strong liquidity, how can one justify allocating to other asset-classes trading on inferior yields, or much riskier segments, like high yield and private credit, that offer very poor risk premiums. Historically, US B-rated high yield bonds have paid a risk premium of 3.5% above BBB rated investment-grade bonds. That risk premium is currently only 3.0%. And during default cycles, the risk premium normally rises to 6.0% or more. There remains much downside risk in the high yield and private loan markets.

3. We believe that the global economy is about to be subject to a very serious default cycle. Interest rates have risen by a record margin. Households are carrying record levels of debt. The economy is about to go into recession or sharp retrenchment. And scores of businesses and families had predicated their finances on the assumption of the “low rates for long” paradigm persisting.

We now face the spectre of high rates for a very long time. Central banks are scarred by missing this inflation crisis, which was fuelled as much by excess demand as supply-side frictions. While they should pause this year, there is real risk that there is a second phase to this hiking cycle if core inflation rates do not promptly move back to their 2% targets. Markets are not pricing in **any possibility** of a second phase to this monetary cycle: they universally assume rates peak this year and then drift lower.

When central banks do come to cutting, they will be slow, and eager to avoid over-stimulating again. None of them know where the true normal/neutral cash rate is, and they will be careful as they approach it. Most central banks do not expect to cut until 2024 or 2025, and the cuts may be modest when they come.

Our systems show that the share of listed companies that don't have sufficient profits to pay the interest bill on their debts almost doubled in the US, UK, Europe, and Australia over the last decade. And this is based on FY21 financial data - before rates started rising.

These zombie companies will be wiped out. That is what the central banks want: they are actively seeking job losses, higher unemployment, lower wage growth and the demand destruction required to get inflation under control.

Since the GFC and the advent of TINA and the search for yield, many business models and asset-classes were predicated on the persistence of uber-cheap money. The pervasive search for yield saw demand for income rich equities, commercial property, high yield debt, and private loans explode.

In the period after 2008, this dynamic was amplified by global regulators forcing banks to reduce lending to the sectors that had historically accounted for huge balance-sheet problems and bank blow-ups. Regulators made it very difficult for banks to provide finance to residential property developers, commercial property owners, and zombie companies.

This sub-prime corporate finance has shifted into the rapidly growing “non-bank” sector, which sits outside of the regulatory net, as represented most visibly by the (1) high yield bond market, (2) the private loan market, and (3) crypto and the crypto lending industry. Investors wanted yield or the allure of super-normal returns. Asset managers wanted to raise capital to lend. And borrowers wanted crazy cheap money.

The huge growth in high yield issuance, private credit lending and crypto finance outside of the conventional bank regulatory net was fine for as long as credit default risks remained contained. This in turn required interest rates to stay very low.

That cycle has now turned. Lenders will not want to acknowledge loans going into formal default, and will be desperately restructuring them to extend terms, reduce interest repayments, and/or swap debt for equity in the name of not having to report defaults and/or foreclose.

Strategy commentary cont'd: But one way or another, a massive default and restructuring cycle is utterly inevitable. And in contrast to every other shock since the GFC when risky borrowers were bailed out by zero interest rates and endless money printing, this time around many will face insolvency.

The history of the financial world teaches us two key lessons from every single crisis: (1) most of the non-banks die and (2) the banking system has to be backed by government guarantees and the availability of central bank loans/liquidity.

What makes this very different to the GFC is that in this episode the credit risks have shifted out of the banking system, which has been aggressively de-levered and de-risked since 2008, into the non-bank domain...

4. We think the huge increase in the yields on liquid and high-grade bonds will see an inevitable shift of asset-allocation away from equities, property, infrastructure, and high risk debt back to conventional, liquid and highly-rated fixed-income. We are seeing this in record book-builds for new bond issues. And this process will be amplified by the regime change for defined-benefit pension funds globally, which for decades have run large funding gaps/deficits that have recently transformed into funding surpluses as a result of the huge spike in interest rates slashing the present value of their current liabilities.

When defined benefit pension funds in Australia, the US, UK, Europe, and Asia previously faced enormous funding gaps, they were forced into chasing risk/yield to try to close these gaps via allocation to public and private equities and other racy sectors, such as commercial property and high-yield debt. But with the sudden emergence of funding surpluses, they are looking to lock in this security by reallocating back to high-grade bonds paying lofty fixed interest rates.

We are seeing an unprecedented (in recent history) increase in the demand for fixed-rate as opposed to floating-rate paper. These yield buyers could in turn compress credit spreads sharply for as long as overall yields remain high and alternative investments fail to compete in risk, return, and liquidity terms. This has been evident in recent fixed-rate bond transactions that have experienced enormous spread compression for as long as they continue to pay an attractive total yield.

5. Don't expect the classic post-GFC boom in asset prices once the correction has passed. After every shock since 2008, central banks flooded rates and ran QE-to-infinity. They could only do this as long as inflation remained very low. This time around the structure of interest rates is fundamentally shifting higher. Central banks are all revising their estimates of both the NAIKU and the neutral cash rate back up to more normal levels after experimenting with the idea that NAIKUs had fallen and neutral cash rates might be much lower than they have been in the past. It is possible that we will see this unwind some of the shifts in portfolio construction and asset-allocation that flowed from the secular decline in interest rates, and the advent of very benign price stability, since the adoption of inflation targets in the early 1990s (i.e., the huge equity and illiquid assets binge over the 1990s and 2000s).

High-grade bonds are likely to become much more fashionable again. The risk is that central banks struggle to get inflation rates back to their ~2% policy targets, and have to precipitate very deep economic downturns, in order to secure their goal of price stability. This is likely to be bad for all asset-classes, except cash and very high-grade fixed-income. Asset prices have to adjust permanently lower in response to permanently higher discount rates, and potentially a period of permanently lower growth as household and business balance-sheets deleverage further. Rather than the big post-GFC bounce that many have hoped for when they buy the dip, you are likely better off selling the rip when we get these bear market rallies until you are sure that asset prices have properly adjusted.

We set Coolabah up in 2011 to specialise in running zero duration floating-rate strategies that would outperform during a rising interest rate climate. We did this because we believed that the emergent policy reflexes at the time of zero rates and QE-to-infinity would ineluctably propagate a very big inflation shock, which would prevent central banks from lower rates and/or printing money. It turned out that we needed a supply shock to initiate the demand shock that gave us the biggest inflation crisis in 40 years.



Don't forget to listen to Coolabah Capital's popular Complexity Premia podcast. You can listen on your favourite podcast app, or you can find it on [Apple Podcasts](#) or [Podbean](#).

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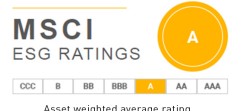
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