

Altius Sustainable Short Term Income Fund (Ordinary Units)

Fund Update
29 February 2024

The Fund invests in a combination of short-term money market instruments and medium-term floating securities that are investment-grade rated. The investment process is designed to maximise returns while balancing the risk and liquidity of the portfolio.

Performance as at 29 February 2024

	1 mth %	3 mths %	1 yr %	2 yrs % p.a.	3 yrs % p.a.	5 yrs % p.a.	Since inception % p.a.
Gross total return	0.58	1.65	5.69	3.86	2.65	2.34	2.43
Net total return	0.57	1.60	5.48	3.66	2.45	2.13	2.21
Benchmark	0.34	1.09	4.10	2.92	1.95	1.47	1.57
Excess to benchmark	0.23	0.51	1.38	0.74	0.50	0.66	0.64

Inception date for performance calculations is 13 June 2017.

Gross total returns are calculated before fees and expenses and assumes the reinvestment of distributions. Past performance is not a reliable indicator of future performance.

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

The benchmark is the Bloomberg AusBond BankBill Index.

Excess to benchmark is calculated on Net total return.

Portfolio Performance and Activity

Credit markets opened with a strong bid tone which was retained throughout February. Primary issuance volumes highlighted the strong technical backdrop driving credit spreads tighter over the month. Locally, Heritage and People's Choice kicked the month off with \$400m of 8/2/27 at a margin of 1.60%. The deal generated \$650m of support leading to a 0.05% price lowering. This was quickly followed by a \$2bn 10NC5 NAB deal with \$3.1bn of interest which pushed the initial margin from 2.10% to 1.95%. This strong support was a catalyst for bank-subordinated spreads to narrow around 0.15% over the month. Later in the month saw Macquarie Bank issued \$1.2bn of 10NC5 Tier 2 at a margin of 1.95% with a large book size of just under \$5bn, again highlighting the strength of markets. Other notable transactions included Newcastle Greater Mutual Groups \$400m 5-year and inaugural deals by the ASX, issuing \$275m to 2027 and Perth Airport \$300m 2031 transactions. The fund participated in a number of new deals including Heritage and Peoples Choice, Newcastle Greater Mutual, Macquarie Bank, and ASX. By the end of the month, senior financial and industrial spreads had contracted 0.04% and 0.03% to finish at 0.90% and 1.02% respectively.

The Australian earnings season concluded in February. Corporates (ex REIT's) reported moderately credit-negative to neutral results with financial leverage increasing year-on-year with most guiding a cautious and uncertain outlook. Key

themes included a soft consumer and higher cost across the board and the inability to pass on cost increases. REIT's remained under pressure reporting negative credit results driven by higher debt costs and further asset devaluations, resulting in a significant increase in leverage. Consistent themes were seen across the Banking sector with slowing credit growth and increased NIM pressure, driven by higher funding costs and mortgage competition. The positive for banks was that while non-performing loans have started to increase, they remain at historical lows.

Several key credit events occurred locally over the month. The Australian Competition Tribunal overruled the ACCC's decision and authorized ANZ's proposal to purchase Suncorp's banking division. The acquisition still remains subject to approval by the Federal Treasurer and an amendment to Queensland Parliament. The announcement saw Suncorp Bank securities compress towards ANZ Bank margins. Bank Australia announced merger talks with Qudos Bank with the member vote expected late 2024 and completion in early 2025.

The biggest global credit story of the month was the poor Q4 result from the regional US bank, New York Community Bancorp (NYCB). NYCB reported an unexpected \$252m loss, which reignited concerns about US regional banks exposure to commercial real estate. This saw Moody's cut the Group's rating by 2 notches. While the Regional Bank equity index only fell 1.7% on the announcement, the weakness continued to

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build through the month. The month closed with NYCB announcing a delayed release of its mandatory annual financial disclosure until March 15th. The delay led to a further 4-notch downgrade by Moody's from Baa2 to Ba3 and resulted in a 25% equity fall. The woes continued for NYCB in early March with Fitch also downgrading the bank and the equity price fell a further 30%. Over the past 12-month NYCB has fallen 73%. While uncertainty about NYCB's future continues the impact on the wider banking market has been minimal.

Socially Responsible Investments in Focus

January 2024 was the warmest January in the ERA5 data record, going back to 1940. The global surface air temperature was 13.14°C, which is 0.70°C above the 1991–2020 average for January and 0.12°C above the previous warmest January, in 2020. Considering the average of the last twelve months, the global mean temperature was the highest on record at 0.64°C above the 1991–2020 average and 1.52°C above the 1850–1900 pre-industrial average.

Samantha Burgess, Deputy Director of the Copernicus Climate Change Service (C3S) noted: "2024 starts with another record-breaking month – not only is it the warmest January on record but we have also just experienced a 12-month period [with a mean global average temperature] more than 1.5°C above the pre-industrial reference period. Rapid reductions in greenhouse gas emissions are the only way to stop global temperatures increasing."

The average global sea surface temperature (SST) for January outside the polar regions reached 20.97°C, the highest recorded for January and the second highest monthly temperature in the ERA5 dataset for any month, only 0.01°C below the highest, reached in August 2023.

(<https://climate.copernicus.eu/warmest-january-record-12-month-average-over-15degc-above-preindustrial>)

The International Capital Market Association (ICMA) is exploring the possibility of developing market guidance for 'avoided emissions' (estimated savings from low-carbon projects or products), to include in principles for sustainability bonds and loans. These are separate to an entity's scope 1, 2 and 3 GHG emissions, and not usually counted towards decarbonization targets.

A key impediment to growing the use of 'avoided emissions' as an impact measure is the lack of a standardized accounting method for calculating 'avoided emissions', to ensure there is no overstatement of climate impact claims. The development of a guidance together with standardized calculations will help improve the credibility around this concept and orientate financial flows to activities to enable the decarbonization of the economy.

(https://www.icmagroup.org/assets/documents/Sustainable-finance/ToR/TF-Green-enabling-ToR_-2023-2024_Member-List-Jan-2024-080124.pdf).

Despite global macroeconomic uncertainty in some key regions, S&P anticipate that GSSSB (Green, social, sustainability, and sustainability-linked bonds) issuance will increase modestly in 2024, building on the near US 1 trillion seen in 2023. Green bonds will continue their dominance, buoyed by increased demand for environmental projects across all geographies, while transition and blue bonds may also gain traction in the GSSSB market in 2024. S&P also see the spread of issuers growing as middle- and low-income countries strive to increase their share of GSSSB issuance given their large unmet

funding needs.

Outlook

Global goods inflation has retreated but the tension between activity and employment data, and the trajectory of services inflation is expected to manifest in oscillating market reactions. The lags in the effect of interest rate adjustments, timing of data, and of wage responses ensure a degree of volatility. The slow but nonlinear fall in inflation biases yields lower though with reasonably wide ranges.

Late last year, oil fell 28% as OPEC and non-OPEC (largely Russia) increased production. The effects of this flow, with a lag, provided a disinflationary pulse that hit official inflation data. This contributed to financial markets factoring in the expectation of significant rate cuts, starting in the US and Europe as early as June.

Attacks on container ships passing through the Red Sea have contributed to a 35% lift in shipping container costs over the first quarter. Key trade routes have extended by up to three weeks and specific shipping insurance costs have increased up to ten-fold. If this is ongoing, estimates suggest a 0.4% to 2% lift inflation, depending on jurisdiction.

Growth is expected to be uneven and weaker in sectors reliant on discretionary consumer activity. But as long as unemployment remains toward 50-year lows, and inflation is above target, the RBA's inflation mandate remains the greater focus for monetary conditions.

In Australia, housing makes up 22.25 percent of the CPI, with the big ticket items being rents, new dwelling purchases, and maintenance. Australian "asking rents" are tracking at 8.4 percent – higher than measured rents currently in the CPI. The significant population growth and shortage of housing supply mean rents will have an upward bias to the CPI going forward, noting the rental subsidy effect was temporary.

Domestically, the Commonwealth Rental Assistance program added to the disinflationary pulse by temporarily dampening rents; an otherwise consistent source of Australian inflationary pressure. This allowed the RBA to resist the need for a follow-up rate increase. Moreover, it translated into markets factoring in RBA rate cuts as early as the second quarter.

The disinflation pulse is unlikely to be repeated in the current quarter. This is consistent with Altius view that fall in inflation to central bank targets will be elongated and non-linear. We expect mini-cycles that reflect the uneven nature of the global economy and reaction functions.

The crude oil spot price is about 18% higher in Australian dollar terms than where it was at end of December and the average only a little below the average price of the previous quarter.

We expect lower headline inflation and a less supply-constrained labour market to allow more modest wage growth in aggregate compared to last year. The cumulative negative 7.5% real wage growth of the last three years likely sees wage negotiations attempt to claw back the loss of disposable income. Wage increase pressures should remain elevated – though not acute – over a longer time horizon.

Fed Governor Powell articulated that the Fed won't wait until inflation reaches 2% before easing interest rates. Real cash rates are as tight as any time over the last 30 years. As long as there is sufficient evidence that the expected immediate bounce in inflation is temporary and modest, the trimming of cash

rates can occur while keeping monetary settings slightly restrictive. The one hundred basis points fall in long-dated US Treasuries has already eased monetary conditions.

Australia's real cash rate is not tight by historical standards. We expect Australian cash rates to be eased during the fourth quarter,. This reflects the higher starting point and more gradual decline of inflation. The commencement of a gradual US easing cycle in the middle off the year introduces a disinflationary bias through the currency channel and has influence on the RBA's reaction function.

The range on Australian long-dated bonds is expected to oscillate around a midpoint in 10-year Australian sovereign bonds of 4.0% with the expected evolution of inflation to allow long bonds to move lower to around 3.75%. The portfolio strategy is to actively manage duration settings; incrementally increasing duration above 4.0% or decreasing duration accordingly.

With cash rates above 4% over the immediate investment horizon, there is a significant benefit of attractive accrual across the yield curve and capital gains from roll down on fixed-rate corporate bonds. The expected low volatility environment correlates bullishly with higher-yielding corporate bonds converging with sovereign bonds.

The portfolio maintains overweight credit exposure with a preference for financials, including senior and subordinated securities.

A further measure of value that we find in the high-grade corporate market is related to the yield on the Australian Corporate Index is higher than the dividend yield of Australian stocks as defined by the ASX 200. To illustrate at the time of writing, the CBA dividend yield is around 3.8%. By comparison, the higher ranking CBA (10 year) subordinated bond yields above 6%.

Fund snapshot

APIR code	AUS0079AU
Inception date	13 Jun 2017
Distribution frequency	Monthly
Minimum initial investment	\$100,000
Fund size (net asset value)	\$411.27m
Management fee*	0.20% p.a.
Buy/Sell spread	0.05%/0.05%

*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.

Sector Profile

Asset Class	Portfolio %
Industrials	5.70
Financials	66.55
Asset Backed	21.31
Money Market	2.40
11AM	3.69
Cash at Bank	0.34

Portfolio Summary Statistics

Asset Class	Portfolio	Benchmark
Yield to maturity (%)	5.16	4.32
Credit duration (years)	1.98	N/A
Modified duration (days)	31.45	45.83

Interest Rate Profile

Term	Portfolio %
0 - 30 Days	6.09
1 - 3 Years	44.86
3 - 5 Years	36.48
30 - 90 Days	0.71
90 Days - 1 Year	11.85

Top 10 Holdings

Issuer	Senior Rating	Portfolio %
Australia and New Zealand Banking Group Limited	AA-	8.63
Westpac Banking Corporation	AA-	7.22
Commonwealth Bank of Australia	AA-	5.00
National Australia Bank Limited	AA-	4.77
Bank Australia Limited	BBB	4.05
Bank of Queensland Limited	BBB+	3.94
Macquarie Bank Limited	A+	3.92
UBS AG (Australia Branch)	A+	3.51
Teachers Mutual Bank Ltd.	BBB+	3.34
Bendigo and Adelaide Bank Limited	BBB+	2.96

Ratings Exposure

Rating	Portfolio %
A	17.44
AA	12.42
AAA	29.87
BBB	40.26

Ratings / Awards



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