Sustainable Short Term Income Fund - Ordinary Units

Fund Update
30 June 2021

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 30 June 2021

	1 mth %	3 mths %	1 yr %	2 yrs % p.a.	Since inception % p.a.
Gross return	0.06	0.20	1.45	1.51	2.15
Net return	0.05	0.15	1.34	1.28	1.92
Benchmark	0.00	0.01	0.06	0.45	1.17
Excess to benchmark	0.05	0.14	1.28	0.83	0.75

Inception date for performance calculations is 13 June 2017.
Gross returns are calculated before fees and expenses and assumes the reinvestment of distributions. Past performance is not a reliable indicator of future performance.
Net 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 Bank Bill Index.
Excess to benchmark is calculated on Net return.

Portfolio Performance and Activity

Over the course of the month, portfolio credit risk increased to 2.15 years from 1.98 years. Corporate risk grew to 1.74 years while asset-backed security risk was unchanged at 0.41 years. Credit spread tightened marginally over June with investor sentiment remaining strong. Financial spreads fell roughly 0.03% while non-financials fell 0.01% to finish at 0.53% and 0.85% respectively. With many corporates taking the opportunity to issue several months ago, it meant primary markets were extremely quiet. REIT's and Financials dominated issuance with Charter Hall LWR returning to the market to issue $267m of 8.5 years at a margin of 1.25% and LendLease International Towers Sydney issuing $200m of 9 years at 1.40%. While on the financial side, Teachers Mutual issued $100m for 5 years to refinance their July 2020 maturity at 0.68%. Teachers Mutual remains a preferred regional bank from our sustainability view, and as such we participated in the transaction. Bendigo Bank and Macquarie round out the month with a 5-year senior and 5-year subordinated deal at 0.65% and 1.55% respectively with the Fund making investments in both transactions.

Sustainable issuance continued to grow strongly through June. Of most interest was the inaugural Wesfarmers Sustainable Linked Bond (SLB), the first such transaction in the local market. Wesfarmers set two KPI's for the transaction. The first KPI focused on renewables and emission reductions with a commitment to source 100% of electricity requirements from renewables for its retail businesses by December 2025. The second KPI focused on nitrate production and limiting emission intensity to 0.25 tonnes of CO_2 of ammonium nitrate produced, or lower. If Wesfarmers fails to meet either target, the coupon on the bond increases by 0.125% for each KPI. We believed both KPI's meet the objectivities of the SLB principles, and as such, an investment was made for the Fund. CPP Investment (Canadian Pension Fund) issued a 7-year green bond with a focus on renewables, sustainable water and green buildings. While IDB Invest, a member of the IADB Group which focuses on Latin America and the Caribbean, issued a 5-year social bond.

Socially Responsible Investments in Focus

The Queensland government has announced an increase of a further $1.5 billion to their clean energy fund, on top of an existing $500 million renewable energy fund committed in last year's budget. The expanded Queensland Renewable Energy and Hydrogen Jobs Fund will be used to invest directly in new renewable electricity, hydrogen production and clean energy resources project.

It was a big month for zero emission transport with the NSW government announcing ambitious plans to electrify the state's train network within the next four years, and retrofit some harbour ferries with electric engines, as well as funding to speed up adoption of passenger electric vehicle (EV) use in the state. The government has also announced a new scheme to retrain motor mechanics so they can work on electric vehicles, as it ramps up the electrification of its bus network. Over the next decade, the NSW government plans to replace its entire network of 8,000 buses with zero emissions vehicles. The scheme to retrain mechanics on these new buses will be run as a partnership with Volvo Australia and TAFE NSW. NSW will waive stamp duty on new EVs under $78,000, give cash rebate of $3,000 for 25,000 new EV buyers and spend $171 million on chargers throughout the state. The government is aiming to increase EV sales to more than 50% of new cars sold in NSW by 2030 and the vast majority of sales by 2035.

In another win for the environment, the NSW government has announced plans to cut single-use plastics by 2025. The move has been lauded by different environmental groups as NSW was the only state in Australia without a ban on plastic bags. Straws, stirrers, cotton buds and polystyrene cups will be phased out 12 months after legislation is passed, with a review on plastic cups, heavy bags and fruit stickers to be carried out within three years.

UNESCO has recommended that that Great Barrier Reef be placed on a list of world heritage sites that are "in danger" urging Australia to take accelerated action at all possible levels on climate change. The United Nations committee has also called on the Tasmanian government to halt tourism development in the Tasmanian Wilderness World Heritage Area (TWWHA) until a cultural assessment is completed (https://www.abc.net.au/news/2021-06-23/unesco-tasmanian-wilderness-world-heritage-area/100236044) . The G7 summit in Cornwall in June saw G7 leaders make new pledges to combat climate change. Although the G7 leaders have agreed to stop financing coal projects by the end of 2021, their climate pledge were criticised for not going far enough.

A draft of the Intergovernmental Panel on Climate Change report said crushing climate impacts will hit sooner than feared. With 1.1°C warming clocked, the climate is already changing. Earlier models predicted we were not likely to see Earth-altering climate change before 2100 but dangerous thresholds are closer than once thought with the report outlining the danger of compound and cascading impacts, along with point-of-no-return thresholds in the climate system known as tipping points. Warming of 2°C could push the melting of ice sheets past a point of no return. Other tipping points could see Amazon basin morph from tropical forest to savannah and billions of tonnes of carbon leech from Siberia's permafrost, fueling further warming.

Outlook

Australia is well advanced in its recovery. Successful virus containment has allowed the economy to open more quickly than anticipated, but we expect virus mutations and the nature of the pandemic to be with us for some time. Virus outbreaks and related restrictions are definitionally unpredictable, thus providing a backdrop of some volatility.

Central banks are universally supportive, but keen to ensure a recovery lifts inflation to target levels not seen over the last decade. This biases cash rates to remain low until inflation actually appears, but markets will be more forward-looking, meaning longer dated interest rates can drift higher, albeit dampened by the ongoing central bank bond buying programs.

Despite the rise in underlying inflation expected to be temporary, the US has seen a larger lift than expected. The narrative of the Federal Reserve has evolved to suggest the lift may be a little more persistent.

Australia's position is rather more idiosyncratic. Closed borders mean virtually no workers coming from overseas combined with the historically high participation rate, there are pockets of wage pressure emerging. Although no widespread wage lift has been seen in official data, anecdotal evidence suggests that the labour market is tightening a little quicker than the RBA has forecast. The RBA has significantly revised up expected growth rates for 2021 to 4.75%. Unemployment is expected to fall to 5% by year end.

The RBA is embarking on the slow process of unwinding its emergency settings, whilst hoping to spark a healthy measure of inflation. So as not to allow an unhelpfully high Australian dollar, official cash rates are unlikely to lift ahead of the US increasing cash rates. However, reflecting the improved backdrop, the RBA has decided to not extend its Yield Curve Control point beyond the current maturity (April 2024 Government Bond) at 0.1%. Given smaller government budget deficits, the RBA has been able to trim the volume of its bond purchases. Consequently, we expect some upward recalibration to interest rates, with 10-year yields moving higher to around 1.9% by year end.

The Fund's exposure to inflation-linked bonds caters to the likely lift in headline inflation from the rebasing effect of the depths of "COVID-19 shutdown" passing, and as a hedge against expectations of wage increases.

Intermediate maturity semi-government and corporate bonds continue to have attraction given the "roll down" of their very steep yield curves. The global "hunt for yield" born of ultra-low cash rates continues to support the high grade corporate and semi sectors.

Sector Profile

Asset Class	Portfolio %
Supranationals	8.40
Industrials	9.44
Financials	60.11
Asset Backed	14.56
Money Market	4.38
Agencies	0.76
11am	2.08
Cash at Bank	0.26

Portfolio Summary Statistics

Asset Class	Portfolio	Benchmark
Yield to maturity (%)	0.79	0.03
Modified duration (days)	235.87	48.18
Credit duration (years)	2.31	N/A

Interest Rate Profile

Term	Portfolio %
0 - 30 days	44.76
30 - 90 days	38.54
90 days - 1 year	0.00
1 - 3 years	4.98
3 - 5 years	11.72

Top 10 Holdings

Issuer	Senior Rating	Portfolio %
Bank Of Queensland	BBB+	5.21
Teachers Mutual Bank	BBB	4.55
Canadian Imperial Bank Comm (Syd)	A+	4.04
ANZ Banking Group	AA-	4.03
Bendigo And Adelaide Bank	BBB+	3.97
Macquarie Bank	A	3.61
Toronto-Dominion Bank	AA-	3.30
Suncorp-Metway	A+	3.25
UBS Ag Australia	A+	2.65
National Australia Bank	AA-	2.64

Ratings Exposure

Rating	Portfolio %
AAA	24.53
AA+ to AA-	19.56
A+ to A-	26.31
BBB+ to BBB-	29.60

Ratings / Awards

Zenith RECOMMENDED

Important Information