# Fund Update

31 December 2017

## Altius Bond Fund

Altius Asset Management (Altius) employs a diversified strategy to fixed interest funds management that aims to take advantage of the mispricing of bonds in all market conditions

### Performance as at 31 December 2017

| | 1 mth % | 3 mths % | 1 yr % | 3 yr % | 5 yr % | Since inception %pa |
|---|---|---|---|---|---|---|
| **Total return[1]** | **-0.15** | **0.51** | **2.64** | **2.56** | **3.28** | **4.56** |
| Benchmark[2] | -0.20 | 0.91 | 2.58 | 2.43 | 3.14 | 3.98 |
| Active return[3] | 0.05 | -0.40 | 0.06 | 0.13 | 0.13 | 0.57 |

1. Total returns are calculated after fees and expenses and assumes the reinvestment of dividends. Past performance is not a reliable indicator of future performance. Inception date for the Portfolio is 1 October 2011
2. Effective 1 July 2016, Benchmark is 50% Reserve Bank of Australia Cash Rate and 50% Bloomberg∞ AusBond Composite 0+Yr Index and applied retrospectively for all periods.
3. Active return is calculated on Total return

## How the Altius Bond Fund performed and activity

The Portfolio produced a total return of -0.15% for the month which lagged cash but outperformed the return from our blended benchmark. Other highlights were:

- The dominant theme over the month was the solid sell-off in rates coupled with a continuation of the flattening of the yield curve with 10 year bond yields rising 0.13% while 3 year bonds rose 0.23%.
- Our strategic interest rate positioning was a strong contributor over the month tempted by our positioning for a steepening yield curve
- Portfolio duration began the month at 0.49 years. The markets traded with an optimistic tone as US Congress worked through the President's tax cuts. Once again the RBA left the cash rate at 1.50%. Strengthening local economic data enabled the market to pull forward rate hike expectation to December 2018, relative to mid-2019 at the end of November. With yields pushing towards our forecast level we took the opportunity to add duration to the portfolio. At the end of the month portfolio duration was 1.55 years.
- Credit spreads were flat to marginally wider over December with liquidity muted going into the holidays. While credit spreads were marginally weaker the additional return still resulted in credit outperforming the other sectors of the market over December.

We maintained our cautious overweight position in credit. Issuance was low over December with only $3.1bn of primary deals as the market wound down for the holiday period. This was markedly lower than the $9.2bn in November. Despite the markets ongoing appetite for credit product there appeared to be some cautiousness to push spreads too far below GFC lows.

We selectively added to our credit holdings over the month with investments made through the primary markets. We purchased the inaugural University of Wollongong 10 year deals with Universities remaining a preferred sector due to their defensive characteristics. We continued to add to our Mortgage Backed exposure with the purchase of the Progress Trust (AMP bank) class A (AAA rated) notes at swap plus 95 basis points.

## Outlook

Global growth enters 2018 with the most synchronised growth in a decade. At the heart of this is the improvement in the middle class income levels of many developed economies.

US tax cuts are expected to add 0.5% to growth over the next year, to an economy that is currently tracking at around 3% per annum. The European economy is transitioning from being overly reliant on increased activity in the US and China, to one where rising employment is generating more income and thus business investment; a more virtuous growth cycle.

Although we expect further increases in cash rates in the US over 2018, we do not expect any lifts in Europe, Japan or Australia as core measures of inflation are expected to remain contained.

Many of the forces that had held down long dated yields over the second half of 2017 are likely to give way over 2018. The reduction in the US Fed Balance sheet ought to increasingly outweigh the FX reserve related purchases of Government Bonds by the PBoC. The new US financial year reduces US pension fund demand for US Treasuries, related to the new corporate tax rate, and rebalancing out of profitable equity.

The reduced asset purchase program by the ECB allows longer dated European bond yields to lift and reduce the magnetic effect on all yields, including Australia and the US.

Despite the extraordinary population growth over recent years, Australian unemployment has fallen to 5.4%. The flipside of the impressive absorption of a larger labour force has been that wage growth is non-existent. Middle class incomes, particularly in real terms, are yet to lift. Related to this, non-mining capex growth, a key element in kicking the Australian economy into a higher gear, has been subdued.

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When these elements are combined with a persistently strong Australian dollar, the RBA is not expected to lift cash rates until 2019.

With cash rates on hold during 2018, we expect short dated bond yields to remain anchored, with corporate bonds adding yield. We are positioned to profit from our underweight in long bonds, should our expectation for higher long term interest rates, associated with the global unwind of QE be realised.

## Sector Profile as at 31 December 2017

| Asset Class | Portfolio % | Benchmark % |
|---|---|---|
| Commonwealth Government | 17.76 | 25.39 |
| Semi Government | 17.21 | 12.12 |
| Supra Nationals | 10.74 | 7.43 |
| Financials | 19.45 | 2.30 |
| Industrials | 14.32 | 2.71 |
| Asset Backed | 9.58 | 0.05 |
| Money Market | 1.81 | 0.00 |
| 11am | 0.23 | 0.00 |
| Cash at Bank | 8.90 | 0.00 |
| RBA Cash | 0.00 | 50.00 |

## Top 10 Holdings

| Issuer | Portfolio % | Benchmark % |
|---|---|---|
| Commonwealth of Australia | 17.99 | 25.33 |
| Cash at Bank | 8.74 | 0.00 |
| State of Queensland Australia | 6.98 | 4.52 |
| State of Victoria Australia | 4.57 | 1.76 |
| Royal Bank of Canada | 4.10 | 0.04 |
| State of New South Wales Australia | 3.93 | 2.37 |
| World Bank Group/The | 2.36 | 1.16 |
| Federal Republic of Germany | 2.27 | 1.47 |
| Kingdom of the Netherlands | 2.09 | 0.30 |
| Australia & New Zealand Bank | 1.82 | 0.20 |

## Ratings exposure

| | Portfolio % | Benchmark % |
|---|---|---|
| AAA | 48.08 | 36.86 |
| AA+ to AA- | 19.43 | 9.69 |
| A+ to A- | 21.52 | 2.29 |
| BBB+ to BBB- | 10.97 | 1.16 |
| RBA Cash | 0.00 | 50.00 |

## Maturity Profile

| Term | Portfolio % | Benchmark % |
|---|---|---|
| 0 – 1 year | 20.13 | 52.96 |
| 1 – 3 years | 27.35 | 11.89 |
| 3 – 5 years | 23.35 | 10.11 |
| 5 – 7 years | 9.82 | 6.94 |
| 7+ years | 19.35 | 18.1 |

## Fund Asset Allocation

| | Fund % |
|---|---|
| Australian Fixed Interest | 90.81 |
| Cash and cash equivalents | 9.19 |
| Total | 100.00 |

[1]Cash and cash equivalents may include cash at bank, 11am cash (i.e. overnight bank deposits) and discounted securities (e.g. bank bills).

## Portfolio summary statistics

| Asset Class | Portfolio % | Benchmark % |
|---|---|---|
| Running yield | 2.66 | 2.01 |
| Modified duration (years) | 1.55 | 2.54 |

## Fund snapshot

| | |
|---|---|
| APIR Code | WFS0486AU |
| Inception date | 14 Jun 2011 |
| Fund size (net asset value) | $221.10 m |
| Minimum initial investment | $5,000 |
| Management Fee* | 0.46% p.a. |
| Buy/Sell spread | Nil |
| Distributions | Quarterly |
| Advice fee | Available |

*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.