Antares Diversified Fixed Income Fund

Monthly Investment Report
April 2024

Fund Performance Net of Fees

Period Ended 30/04/2024	1 Mth %	3 Mths %	1 Yr %	2 Yrs %	3 Yrs %	Since Inception %pa[1]
Composite Portfolio - Net	-1.953	-0.94	0.78	1.58	-1.49	-0.16
Bloomberg AusBond Composite Bond Index	-1.984	-1.18	-0.73	0.65	-2.13	-0.87
Difference	0.032	0.24	1.52	0.93	0.64	0.71

Valuation at month end was $360.27M
Composite Portfolio 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 09/07/2019

Sector Exposures

Sector	Interest Rate MDC	Credit Spread MDC	MV%
Cash	0.00	0.00	0.92
Govt Nominal	0.17	0.00	1.31
Semi-Gov Nom	0.19	0.00	1.94
Supra/Agencies	1.93	1.93	23.24
Corp Fin Fixed	0.00	0.00	0.00
Corp Fin FRN	0.86	0.86	23.78
Corp Others Fixed	0.01	0.18	12.94
Corp Others FRN	1.24	1.24	34.05
Covered Bonds	0.00	0.00	0.00
Derivatives Interest Rate	0.69	0.00	-0.27
Derivatives CDS	0.00	-0.16	-0.13
RMBS	0.00	0.02	1.20
Money Market	0.00	0.00	1.01
Total	**5.09**	**4.06**	**100.00**

Portfolio Review

Key Drivers of Portfolio Performance:

- Long duration detracted from returns.
- Financial spreads tightened 1-7 bps adding to returns.
- Semi spreads widened 6-12bps detracting from returns.
- Yield enhancement and rolldown of quality investment grade bond holdings added to returns.

Portfolio Activity and Positioning

- Sold some short-dated corporate bonds including Spark Finance and Brisbane Airport Corp.
- Duration was lengthened mid-April as interest rates rose.

Investment Return Objective

The Antares Diversified Fixed Income Fund aims to outperform the Benchmark over rolling three-year periods, after deducting management fees.

Gross Excess Return Attribution

Description	Feb BPs	Mar BPs	Apr BPs
Duration	-0.3	+0.3	**-4.4**
Curve	-0.4	+1.0	**+0.5**
Sector	+7.5	+2.6	**+2.2**
Yield Enhancement	+7.8	+8.1	**+7.5**
Total Excess Return*	+14.6	+12.0	**+5.8**

*Total excess return is gross. The difference in attribution and fund performance is due to the investment management fee for the month and rounding.

Key Characteristics at 30/04/2024

Description	Fund	Benchmark
Interest Rate Duration (yrs)	5.08	4.97
Yield to Maturity*	5.31	4.57
Credit Spread Duration** (yrs)	4.05	2.30
Average Credit Rating	A+	AA+
Liquidity***	28%	

*Estimated Return if held to maturity. Market Yield for Fixed Rate Bonds whilst FRNs uses a swap assumption rate as an input. **Includes credit spread duration from semi government bonds.
***Liquidity deemed available within 48 hours; includes government and semi government bond holdings plus major bank senior bonds maturing within 12 months.

Portfolio Strategy

Strategy	Implementation
Duration and Yield Curve: Antares continues to still see risks of structurally "higher for longer" inflation but we also acknowledge the potential for the disinflation trend seen at the back end of 2023 to be reestablished. As such, Antares' core scenarios currently have a mix of either sticky inflation or disinflation driving inflation back towards trend. On the growth side, Antares' core scenarios are still skewed towards lower growth outcomes, but we do have a decent weighting to an "at trend" growth outcome given the continued resilient economic data, particularly as seen in the US. We continue to question the consensus expectation of a goldilocks "soft landing" but have reduced our weighting of a hard landing scenario.	• Although most central banks haven't adjusted cash rates recently, we have seen swings in financial conditions (FCs). In the case of the US, after the rapid easing of FCs in late 2023, rising long term bond yields and USD strength in 2024 has seen FCs tighten again. For the US, the question is "are FCs tight enough to reestablish the H2 2023 disinflation trend?" • In Australia, the RBA appears to want to go softly in bringing inflation back to target over an extended timeframe. With fiscal policy initiatives that could be broadly described as accommodative the RBA may find its current settings being challenged if we don't see a softening of Q2 inflation. • Fed commentary has been consistent in expressing an expectation of rates being required to be held higher for longer and any easing of cash rates (or additional tightening if required, although seemingly not viewed as the base case) to be data dependent. • **Yield curve:** We are biased to retaining an outright curve steepening position but see the Australian Government bond 3-10year curve still range trading broadly between 20bps to 50bps. • **Duration:** In November 2023 we shifted from being short duration to close to neutral duration. More recently we have tilted portfolios towards slight long duration positions given higher outright real yields and a slight rise in longer term BEIs. • **BEI:** Inflation linked bonds are currently held within nominal diversified fixed income portfolios as a partial hedge should the market price in longer term structurally higher inflation.
Credit exposure: We continue to be selective about credit issuer exposure within portfolios as credit has become more expensive with spreads narrowing.	• **Valuations:** There have been strong positive returns from credit exposure as credit spreads have continued to narrow, reflecting the market's confidence of lower recession risks and a base expectation of a soft landing. Overall credit has become more expensive and thus we may look to reduce credit risk exposure going forward. • **High quality issuers:** With our outlook for below trend economic growth, we remain focused on holding high quality credit issuers, which we assess as being more resilient to an economic downturn. These include credits with low leverage, strong cashflows, some inflation protection/pricing power, and robust balance sheets.
Optimising yield: Security selection targeting quality, rate, swap and credit term premia. Focusing on maximising carry and rolldown using the steep semi government bond yield curve and/or high-quality credits.	• **Rate, Swap & Credit term premia:** Long term corporates have rallied strongly reducing credit premiums. We are targeting shorter duration credit exposure to harvest yield enhancement while reducing credit spread sensitivity. Semi-government bonds in the 10-15yr part of the curve have continued to steepen versus Commonwealth government bonds and offer good value relative to historical spread ranges. • **Portfolio construction:** We are using our proprietary analytics and breakeven assessments to harvest attractive rolldown while maximising opportunities per unit of risk. This leads to security selection at inflection points on steep yield curves.
Liquidity: Maintain liquidity for normal and/or stressed conditions as appropriate.	• **Liquid Securities:** Selective semis, major banks, and government bonds are seen as core liquidity building blocks across portfolios.

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Market Review

Bond yields rose in April as stronger than expected inflation, employment data, central bank hawkish messaging, and escalating geopolitical tensions saw markets continue to push out the timing of rate cut expectations.

In the US, data showed a reversal of the disinflation trend of late last year with core CPI running at an annualised rate of 4.8%, and the Fed's preferred PCE core deflator measure at 4%, with services inflation the main contributor. The labour market continued to be resilient with stronger than expected nonfarm payrolls and job openings. The rise in nominal bond yields was predominately driven by an increase in real yields, with the US 10-year real yield rising around 40bps over the month.

Similarly, Australian inflation data surprised with the quarterly trimmed mean CPI at 4% annualised, and unemployment falling to 3.8%. While the increase in nominal yields was also mostly real yield driven, inflation risk premiums were repriced more aggressively in Australia with AU 10-year breakeven rates increasing 15bps over the month.

AU US 10-year government bond spreads narrowed after US GDP data printed more in line with Australia's 1.5%, coming in at 1.6% vs 2.5% expected.

Both central banks acknowledge that inflation remains too high to consider rate cuts, and that the strength in the labour market affords time to be patient to consider the incoming data to provide the confidence needed to move to an easing cycle. Markets have followed by paring back further on rate cut expectations for 2024.

Geopolitical tensions increased volatility in markets over the month as risks escalated in the middle east.

Macro Outlook

Market pricing suggests less conviction in the goldilocks soft landing scenario as the latest economic data reiterates there is more work to do on the inflation front, especially with labour markets remaining resilient.

The current economic environment is akin to a soft stagflation scenario with both US and Australian GDP growth tracking below trend while inflation remains elevated above trend.

With central banks likely at the peak of their hiking cycles, looking forward, uncertainty remains around how long rates will need to remain at current levels to create sufficiently restrictive financial conditions conducive to achieving inflation targets. With bond yields rising substantially this year, this has helped tighten financial conditions, but will it be enough?

If inflation continues to remain sticky, then central banks may need to consider further cash rate rises. As markets continue to unwind rate cut expectations it is looking more likely that the beginning of the policy easing cycle may extend beyond this year.

Antares Scenario Analysis

The Antares Scenarios table 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.

Antares Scenarios - Latest Probabilities				
Scenarios		**AU GDP**	**AU Inflation**	**Probability Weighting**
1	Strong Growth	5.00%	4.50%	0.0%
2	Above Trend	4.00%	3.50%	4.1%
3	Trend	2.75%	2.50%	24.7%
4	Below Trend	1.50%	1.50%	22.6%
5	Recession	-2.00%	0.50%	8.0%
6a	Stagflation...Growth & employment softens and inflation	1.50%	3.50%	34.4%
6b	Stagflation...Growth & employment fall sharply but inflation elevated	-1.50%	3.25%	6.2%

With the rebound this year in monthly and quarterly inflation data alongside a softening of the growth data, Antares highest probability weighting is to the "Stagflation Light" (6a) scenario. The "Trend" scenario still has a decent weighting as does the "Below Trend" scenario; but for these scenarios to come to fruition we would need to see a repeat of the disinflation trend of H2 2023.

Currently Antares three key Antares' scenarios are:

- "Stagflation Light" scenario (6a) – with growth being below trend but inflation still elevated.
- "Trend" scenario (3) – with both growth and inflation tracking towards longer term averages,
- "Below Trend" scenario (4) – with both growth and inflation tracking below longer-term averages.

Interest Rate & Inflation Outlook

The Q1 2024 CPI of 1% highlighted persistent non-tradables inflation. The RBA consequentially revised upwards its forward headline CPI forecasts, keeping the bank biased for another hike. For Q2 CPI, several items are likely to generate another high print of +0.8% or so. Key drivers are likely to be medical and hospital services +0.14%, housing +0.3% (including 0.14% for rents), childcare +0.1%, and clothing +0.05%. To this, we can add petrol +0.16%, which is mostly known.

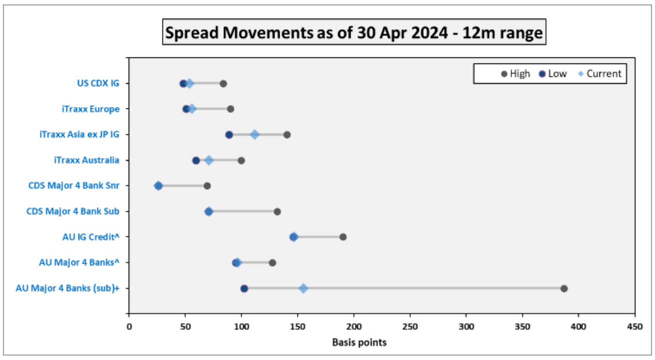
One area of services inflation that continues to challenge the RBA's forecast is the demand-supply imbalance in housing. Rents are expected to grow at around 2.2% for Q2 as immigration continues to surge while building approvals are running at an average of 13,500/month (162,000p.a). At current household formation rates and a net immigration of 500,000p.a, the number of new dwellings required is in the order of 200,000 a year. This is an additional ~40,000 homes required per year above current construction levels, assuming an average household size of 2.5 people. Without a dramatic slowdown in immigration, rental inflation is likely to persist for at least another 2 years.

Credit Outlook

April saw credit spreads widen briefly on the news of Iran attacking Israel with drones and missiles, spiking concerns that the Israel and Hamas conflict would spill over to a much broader conflict across the Middle East and drag in others such as the US. However, as both countries showed restraint and a lack of intention to further escalate the situation, the credit market retraced its losses and ended the month mostly unchanged.

On the economic front, the first quarter US reporting season shows that US companies are performing very well, seeing growth in revenue and earnings across most segments, and exceeding the consensus by more than 8% on earnings expectations. The Australian banks have also reported a resilient set of results, which showed that mortgage borrowers are able to adjust their discretionary spending and continue to service their mortgages despite higher interest rates.

The resilient economic backdrop, supported by solid employment, and expectations of rate cuts on the horizon, has seen credit spreads compress to relatively tight levels. If this continues, we may see them tighten further but Antares believe there are still risks of a harder landing and as this is not priced by markets, we prefer to stay cautious.



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ESG

We engaged with Worley's management in April to discuss the recently reported corruption controversy by its subcontractor in Ecuador. We understand that Worley was not directly involved in any corruption, and that Worley conducted an internal investigation leading to the termination of the subcontractor who was accused of corruption. We also learned that the accusation of corruption occurred after the Ecuadorian government failed to pay Worley's outstanding invoices for historical services provided between 2011-2017. We are not confident that the Ecuadorian court decision was impartial as it is unclear whether the Ecuadorian court itself has judicial independence from the government. We cannot find any evidence or reports of similar incidents by Worley in recent years. Worley has confirmed to us that it has further strengthened its processes with suppliers and contractors post this incident to enforce Worley's internal code of conduct requirements on such entities. At this stage we believe this was an isolated incident instead of a firm-wide corporate governance failure by Worley. We take comfort in knowing that it is expected that there will be no further financial losses or provisioning required regarding this issue. That said, we have increased our governance risk score for Worley from Low to Moderate to reflect the operational risks to which Worley is exposed when operating in higher risk jurisdictions. We remain comfortable to continue to hold our existing exposure to Worley bonds.

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$25.67 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 2023

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