CIPAM Credit Income Fund – Class A

ARSN 620 882 055 APIR HOW8013AU

Monthly Report July 2022

Performance[1]

	1 Month (%)	Quarter (%)	6 Months (%)	FYTD (%)	1 Year (%)	3 Years (%) p.a.	5 Years (%) p.a.	Since Inception (%) p.a.[2]
CIPAM Credit Income Fund – Class A	0.61	0.14	0.03	0.61	1.33	-	-	3.75
CIPAM Credit Income Fund - Class I[3]	0.61	0.14	0.03	0.61	1.33	2.79	-	-
Bloomberg Bank Bill Index	0.12	0.21	0.20	0.12	0.22	0.33	-	0.14
Active return	0.49	-0.07	-0.17	0.49	1.11	2.46	-	3.62

Data Source: Fidante Partners Limited, 31 July 2022.

[1] Returns are calculated after fees have been deducted and assume distributions have been reinvested. No allowance is made for tax when calculating these figures.

[2] The Inception date for Class A is October 1 2020.

[3] As at the date of this report two classes of units are offered: Class I which has been offered since the inception of the Fund on 3 October 2017 and Class A which has been offered since 1 October 2020. For information purposes, and to give a longer term view of the Fund's performance, the returns for the Class I are also provided in the Performance table and shows Class I's performance. The returns quoted for Class I have been adjusted to reflect the fees applicable to the Class A units.

Past Performance is not a reliable indicator of future performance.

Fund Features

Experienced team - Boasting one of the longest track records In institutional private lending strategies, the team is uniquely positioned to exploit opportunities across both public and private lending markets. The team's breadth of experience allows the Fixed Income team to exploit market inefficiencies across all sectors in the global credit market.

Risk management - The Fund aims to reduce market risk by considering low cross-sectoral correlations and maintaining a relatively short spread duration. The team identifies complexity risks to provide income and what they consider to be attractively priced but hard to access liquidity, allowing the Fund to minimise more volatile currency and interest rate risks.

Diversification - The Fund invests across both public and private credit markets providing the opportunity to allocate to the most attractive sectors over time. The Fund targets a weighted average investment grade rating and the diversified set of asset classes in which the Fund can invest includes secured loans, securitised credit, corporate bonds and real estate debt.

Strong governance - The Fixed Income team's clients benefit from a robust governance framework including an independent credit risk management team within the Challenger Group.

Fund Objective:

The Fund aims to achieve superior absolute returns over the medium to long term whilst offering capital stability and a steady income stream.

Fund Details

Management Fee	0.60% p.a.
Strategy FUM	$498.8 mil
Buy/Sell Spread	+0.18/-0.18%
Distribution Frequency	Quarterly
Redemption Terms	Monthly with 10% Fund level gate

Key Statistics

Number of Issuers	117
Running yield (%) p.a.	4.3
Modified duration (yrs)	0.04
Average Rating	BBB-
Credit Spread Duration (yrs)	3.4
Non-AUD Denominated	28%
Private Credit Allocation	20%

Monthly Commentary

Performance Update: The Fund returned to positive territory in July, delivering 0.61% for the month. This lifted the return on a trailing 12 month basis to 1.33%, an active return of 1.11% over the bank bill index. While below our target, the return compares favourably to the low beta Credit FRN index which delivered -0.21% over the prior 12 months and the high beta Credit Suisse Leveraged Loan index which delivered a hedged to Australian dollar return of -1.19% over the same period.

Given the strong rally in markets over the month, it was not a surprise to see the bulk of the monthly performance being driven by spread tightening. Effectively the 1 month gain was equivalent to around 10 basis points of credit spread tightening across the entire portfolio, a significant move. Yield curve movements had a very small negative impact on returns for the month, mostly a function of wider basis between bond futures and swaps. Income generation remained consistent at 0.34% for the month.

Fund Positioning: Having ended the financial year at the wides, risk markets have rallied strongly in July. We began the month with the following themes in place:

- Extending spread duration to increase exposure to public markets which we felt were relatively cheap on a medium term basis;
- Increasing our exposure to foreign currency denominated bonds which we believed were cheap to Australian dollar public markets
- Increasing our exposure to financials relative to securitised; and
- Reducing our weighting to private markets unless we felt that we were receiving an appropriate illiquidity premium to public markets.

As a result of the strong rally through July (which has continued into August), plus some re-pricing across relative sectors our targeting positioning is a little more nuanced.

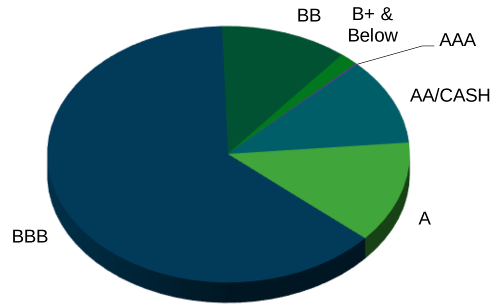
- We don't like foreign currency denominated corporate and financial bonds nearly as much as we did a month ago and are positioned to rotate back to Australian dollars;
- Domestic securitised mezzanine tranches are starting to look like okay relative value for the first time in many months; and
- We do not see as much value in extending spread duration further from here and are starting to see value emerge in private lending markets.

This may seem like a fairly substantial shift in positioning and it is but consider the moves in public credit markets. Since peaking in early July, US high yield credit spreads have tightened by close to 150 basis points. Now this only takes markets back to early March levels but to us this is more a reflection of how tight credit spreads were leading into the year. Investment grade markets appear cheaper in a relative sense which seems a little counterintuitive to us; our view is that the decidedly cloudy macro outlook should have a greater impact on high yield markets.

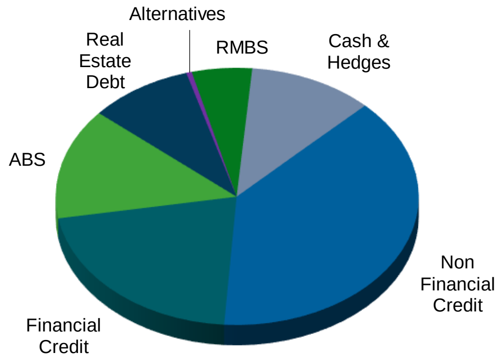
Performance Statistics

Standard Deviation (ann.)	2.4%
% of Down months	8.6%

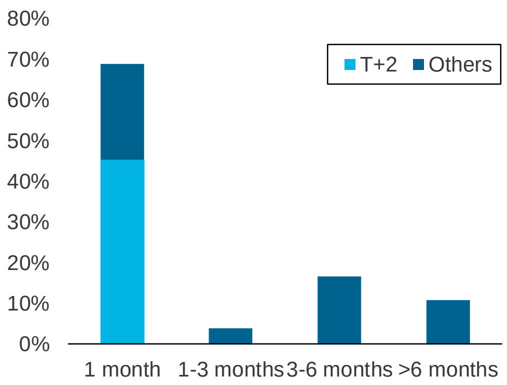
Fund Credit Quality



Fund Asset Allocation



Fund Liquidity Exposure



One thing that remains intact is our key positioning theme of flexibility. On a historical basis our confidence with regards to our positioning is relatively low. Hence, we are being deliberate (i.e., relatively slow) in adjusting our portfolio allocations, running higher levels of liquidity (currently 69% in the 1 month bucket of which 45% is T+2 liquid) and relatively high levels of cash.

Market conditions: Well (just like in 2020), that was quick. As soon as spreads widened to what we thought were attractive entry points, financial conditions seemed to bottom out and a strong risk on rally ensued.

The predicate for the rally seemed to be a reset in inflation expectations. Having peaked in June at 3.5% the US 10 year interest rate ended July at 2.6% and the 2s10s flattened to -0.2% at July month end even reaching -0.4% in mid-August. The inverted yield curve pointed to a slowing economy, with attention turning to a negative Q2 US GDP print, as well as weakness in earnings (S&P500 ex-energy index net income is expected to be 1.5% lower in Q3).

Conversely, as recession fears increased and interest rates declined, risk assets rallied. Australian equity markets are up 7.5% since the end of June. As foreshadowed above, the rally was driven by multiple expansion rather than earnings. US leveraged loan discount margins are close to 150 basis points tighter than the wides of early July with high yield markets outperforming investment grade.

Perhaps the exception here is the Australia credit market which actually widened over the same period. This is a function of the illiquidity of the Australian credit market; because it didn't trade as markets widened, the markets were still playing catch up in July when they tightened.

A lack of primary issuance, especially in non-financial A$ corporate bond markets exacerbates the repricing issues. Q2 issuance was less than A$5 billion, the lowest since Q1 2020 with issuance in July only A$1 billion. We have long maintained that in Australia primary markets reset secondary markets, not the other way around. During periods of volatility, trading in secondary basically stops and borrowers turn to the friendly embrace of the banking sector. And friendly it has been with major banks increasing non-financial loans at a quarter-on-quarter growth rate of 3.5%, the highest level since April 2020.

From a global perspective, issuance was also anaemic. There was less than US$5 billion in high yield bond issuance in July, the lowest level of primary issuance since December 2018. It was a similar story within leveraged loan markets and to a lesser extent investment grade bond markets.

Signs of borrower stress remain low, but signs are emerging that the bottom may be in. Trailing default rates remain near historical lows in the debt capital markets but the June quarter insolvency statistics from ASIC were the highest since the March 2020 quarter (albeit still well below pre-COVID averages). The biggest sectoral contributions came from the construction industry (30%) and accommodation & food services (18%). We'll be watching these statistics closely in the coming quarters at the impact of higher interest rates begin to bite.

For further information, please contact:

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