Hybrid Income Fund

Monthly Report – June 2024

Fund Dashboard

30 June 2024

7.52%

% Yield to Call
(Portfolio as bought)

6.46%

% Yield to Call
(Portfolio if bought today)

6.20%

Running Yield

4.1 Years

Weighted Average
Term to Call

97%

Portfolio Floating Rate

0.35 Years

Interest Rate Duration^

22%

Top 5 Holdings
As % of Fund*

38

Number of Holdings*

Source: Seed Funds Management.
As at 30 June 2024.

*Excluding cash.
^Maximum duration of 1.

Hybrid Income Fund Strategy Net Performance

30 June 2024

FIGURE 1.

	1 Month	3 Months	6 Months	1 Year	3 Years Annualised	5 Years Annualised	SI (Sep 15) Annualised
HYBRID INCOME FUND STRATEGY	0.61%	1.86%	3.83%	8.52%	5.46%	4.71%	6.33%
Hybrid Benchmark (Solactive*)	0.97%	1.43%	3.41%	6.96%	3.81%	3.62%	4.76%
RBA Cash Rate	0.36%	1.09%	2.19%	4.35%	2.48%	1.65%	1.63%

The performance table above represents The Hybrid Income Fund Strategy ("Strategy"). The Strategy commenced in September 2015 and has been continuously operated with identical investment parameters and processes by its portfolio manager, Nicholas Chaplin. The Strategy began in 2015 as the Paraclete Investment Fund until June 2022. The Hybrid Income Fund commenced in June 2022 operating under Evolution Trustees as trustee. Investment management services were novated to Seed Funds Management in March 2024. Performance figures for the Strategy to March 2022 have been reviewed in accordance with ASRS 4400 "Agreed-Upon Procedures Engagements" by Hall Chadwick Corporate (NSW) Limited.

Monthly Commentary

The market settled down after the May volatility and we saw renewed performance in the listed hybrid market in the lead up to the close of the Financial Year. This is often the trend in late June as the market seeks to put cash to work before the books are closed. We noted a particular spike in the index performance in the last two days of the month as hybrids were bought solidly.

Tier 2 and Senior bond trading levels held steady through the latter half of the month quietly accruing their distributions, after good capital growth in the earlier part of June.

We have been delighted in June to welcome John Corr to the Seed Funds Management team. John is a highly regarded authority in portfolio risk management and was a founder and Chief Investment Officer of Fortitude Capital. The Fortitude Capital Absolute Return Fund was awarded Australian Hedge Fund of the year in 2008 and 2009. John joins the Portfolio Management team and is the Chairman of the Risk & Investment Committee.

Research from FundMonitors.com

FundMonitors.com Trusted Targeted Research — Highly Commended

The fund has recently achieved a 'Highly Commended' outcome through FundMonitors.com. Please visit the Seed Funds Management Website to view the research. We are delighted with this recognition from a significantly detail-driven and highly respected research firm.

We have additionally commenced work with Lonsec to provide a rating for the fund. We expect the outcome of Lonsec's research to be ready by September.

Fund to be Offered to Retail Investors in July

Following the positive vote at our recent unitholder meeting, the Hybrid Income Fund will be offered to both wholesale and retail investors from later in July. Consequently, new applications will be via a Product Disclosure Statement (PDS). The PDS, Reference Guide, and Target Market Determination documents will all be available at this time via our website.

Key Portfolio Moves in June

Our investment in the new NABPK listed hybrid landed and has traded well since settlement.

We made some small adjustments to our holding through the month as well given it did

*Solactive Australian Hybrid Securities Index (Net) trade so well. Experience shows that the lower margin hybrid issues suffer the most in times of volatility. While the Australian hybrid market is not showing any broad concerns at present, NABPK has the lowest margin of any Basel 3 issue at 2.60% so trimming holdings when the going is good is reasonable provided yields are maintained elsewhere.

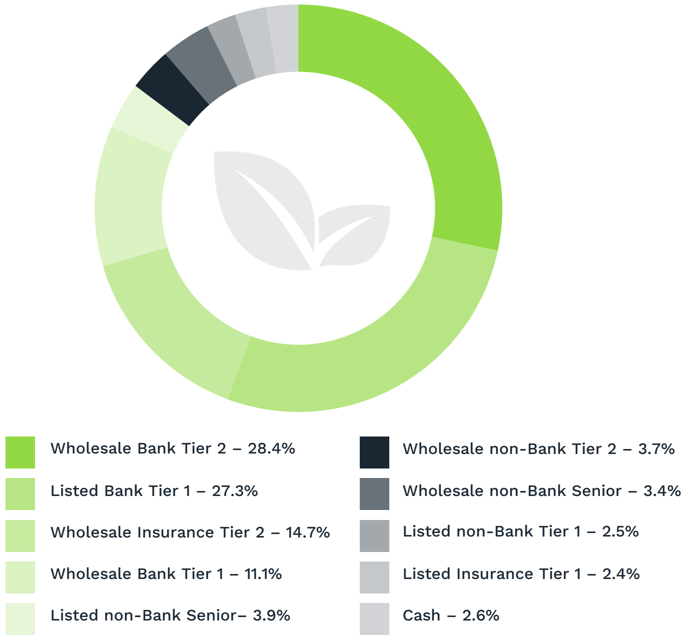
We took the opportunity to make some adjustments to our Tier 2 instrument holdings selling our position in ANZ's January '29 bond which had also traded well. This provided some room to pick up the new issue from Heartland Bank Australia and a handy net increase in yield as the difference in yield between these two issues is approximately 1.75%.

Following the changes to the portfolio through June, the portfolio maintains its weighted average investment grade position at BBB.

Portfolio Holdings

(as at 30 June 2024)

FIGURE 2.



90-Day BBSW Reacts to CPI - Another Rate Rise Due?

The sticky CPI numbers reported for the month of May have finally managed to move the 90-Day Bill rate away from matching the RBA Cash Rate in recent days. At the time of writing, the Bill rate, which is the underlying basis for Australian hybrid returns, has lifted from near 4.35% to 4.45% as the market starts to see greater potential for rates to rise further in Australia.

For months the Australian media has reported the market predicting as many as two rate reductions in 2024. This has been all but thrown out now as inflation levels are back above 4%. The last time monthly CPI was above 4% was as long ago as November 2023 – 8 months ago - indicating an incredibly slow response from the economy to the rate rises to date. This should provide some indication of the low likelihood of a reduction in interest rates this year in our opinion.

Australia's Banks Grow Through Domestic Strength

It was reported recently that the Commonwealth Bank of Australia – the largest bank in the country – had overtaken US giant Citibank in terms of market capitalisation. Reporters stated that the rise of CBA speaks to the strength of the Australian economy, as well as highlighting Citi's moves to exit business lines around the world as management is streamlined. That sounds to us like corporate speak for exiting riskier, failing businesses where they don't have appropriate market share or scale. Australian banks have been doing this over the years as well as they focus on the areas where they can, and do, succeed consistently – borrowing deposits from Australians and lending them out as mortgages. A very straight-forward business model that, with the oversight of an excellent prudential regulator in APRA, becomes a model for a comparatively strong banking industry.

CBA is currently the 13th largest bank in the world measured by market capitalisation. Reports of the bank heading into the top 10 will no doubt prove prescient as Australian banks, with justifiable high credit ratings continue to just do good business very well.

30 June Comes & Goes Without APRA Update

As noted last month, APRA had previously stated in its "Targeted Changes to ADI Liquidity and Capital Standards" paper that the consultation process would be finalised by 30 June. While the consultation process has concluded, no update has yet been provided.

It's quite possible that APRA may take some months to agree and announce any changes to the requirements for Tier 1 instruments and placing any potential restrictions on the investor market for these instruments could be a political minefield. These considerations will, and should, take time.

Expert Management

The HIF provides access to highly skilled specialist management, with extensive expertise in regulated capital products including hybrids, subordinated debt and mutual equity.

Senior Portfolio Manager

Nicholas Chaplin is an authority in the Hybrid and capital issuance market having structured, originated, distributed, and educated on many issues since 1998.

Over his career he has originated over $200 billion in hybrid & capital issues. From 2009 to 2021, Nick was Head of Hybrid & Structured Capital at NAB and prior to that he was Head of Hybrid Origination at Westpac.

Unit Pricing:	Weekly
Applications:	Weekly
Distributions:	Quarterly
APIR Code:	EVO3184AU
Management Fee:	0.70% per annum
Performance Fee:	Not Applicable
Website:	Click here
Offer Document:	Click here
How to Apply:	Click here
Contact Details:	Click here

Fund Information

The Hybrid Income Fund strategy was established in September 2015.

Hybrid Income Fund (HIF) actively invests in a diversified portfolio of financial capital with a heavy weighting to Australian-regulated capital instruments. The underlying securities include hybrids (Tier 1 capital notes and convertible preference shares), Tier 2 bonds, subordinated debt, senior debt, mutual capital instruments and cash. The Fund typically holds ~40 positions whose underlying issuers are banks, insurance companies and non-bank lenders.

Fund Objective

HIF aims to provide returns that exceed the hybrid benchmark on a net basis. The Fund has a meaningful track record of exceeding its target after fees through active management with low volatility and access to franking credits.

The Hybrid Market

The listed hybrid market includes issues totalling approximately $45 billion across a broad range of financial and corporate issuers. In focusing on the financial issuers in this market, over 90% of listed hybrid issuers will be available for investment. Additional diversity and liquidity will be achieved via investment in wholesale unlisted senior, hybrid capital issues and subordinated bonds issued by banks, insurers and other financial entities.

The Investment Strategy

The investment manager intends to apply a tactical approach in terms of which securities it invests in and the timing of such investments with a focus on delivering a robust risk adjusted yield through market and interest rate cycles.

The investment manager will:

- Manage interest rate risk by holding predominantly floating rate instruments;
- Provide portfolio diversity by security type, credit risk, duration and issuer;
- Aim to distribute franking credits;
- Aim to provide regular income.

Platform listings

HUB24 · Australian Money Market · praemium · Powerwrap · netwealth

Unit Price and Core Data

The unit price on 30 June 2024 was $1.0678. The unit price is published weekly on our website here.

As at 30 June, the weighted average yield to call of the portfolio was 7.52%. This is the yield of the portfolio to its collective call dates based on the prices at which each security was purchased. Please note we also show below the yield to call based on security prices today. The running yield of the portfolio was 6.20%.

Franking credits have added an additional 0.88% to returns over the last 12 months with 34% of the portfolio receiving full franking value. Franking credit exposure is reduced with additional investment in Tier 2 securities or senior bonds as these are debt instruments for tax purposes.

Fund returns are made up of three key aspects: 1) regular distributions (either taken as cash or reinvested according to your preference, 2) franking credits associated with these distributions, and 3) changes in the capital value (unit price) over time.

We continually measure the relative value of the prime asset classes of the fund and adjust weightings actively. On 30 June, the fund was holding 43.3% Tier 1 instruments (including both listed and wholesale), 46.8% Tier 2 instruments, 7.3% senior bonds, and 2.6% cash. Figure 2 on Page 2 depicts these current allocations.

The average credit rating of the portfolio is investment grade at BBB.

Glossary

The following details are provided to assist in understanding of terms used in this report:

Credit Spread Duration: Measures the sensitivity of a bond's price to changes in its credit spread. This measure reflects the potential change in the bond's value in response to a 100-basis point (1%) change in the credit spread. For example, if credit spreads tighten by 100 bps for a portfolio with a credit spread duration of 2.5 years, it will result in a + 2.5% return assuming all else is equal.

Interest Rate Duration: The weighted maturity of a fixed-income investment's cash flows, considering all coupon interest payments and the maturity date - used in the estimation of the price sensitivity of fixed-income securities for a given change in interest rates i.e. shorter duration bonds are less sensitive to interest rate movements than long bonds.

Running Yield: The ratio of interest to the current market price of the bond, stated as a percentage. For example, a bond with a current market price of $100 that pays $6 per year in interest would have a running yield of 6%.

Yield to Call: A yield on a security calculated by assuming that interest payments will be paid until the call date, when the security will be redeemed at the call price.

Yield to Maturity: A yield on a security calculated by assuming that interest payments will be made until the final maturity date, at which point the principal will be repaid by the issuer. Yield to maturity is essentially the discount rate at which the present value of future payments (investment income and return of principal) equals the price of the security.

General Disclosures

Wholesale Fund Material
The material contained within this document about the Hybrid Income Fund (‘Fund”) has been prepared by and is issued by Seed Funds Management Limited (ABN 25 675 247 506) Corporate Authorised Representative (no. 001308397) of its related body corporate, Seed Partnerships Ltd the holder of AFSL No. 492973.

APIR Code: EVO3184AU

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