

## Quarterly performance report

31 March 2020

### Mason Stevens Wholesale Fixed Income Managed Portfolio

The Mason Stevens Wholesale Fixed Income Managed Portfolio (Managed Portfolio) is a Managed Discretionary Account (MDA), also sometimes referred to as a Separately Managed Account (SMA).

Performance as at 31 March 2020 <sup>1</sup>							Portfolio statistics <sup>2</sup>	
	1mth (%)	3mths (%)	6mths (%)	1yr (%)	2 yrs (%pa)	Annualised since inception (%pa)		
<b>Portfolio</b>	-4.61	-3.16	-3.16	1.62	3.80	3.98	Yield to call	5.11%
Benchmark	0.04	0.16	0.35	0.97	1.24	1.36	Trading margin	4.85%
Excess/under performance	-4.65	-3.32	-3.51	0.65	2.56	2.62	Running yield	4.08%
							Term to call/maturity	3.46yrs

## Performance and portfolio review

The Managed Portfolio (MP) delivered a net return of -4.61% for the month of March, -3.16% for the past 3 months, and 1.62% for the past 12 months.

The negative return for the month of March was primarily the result of widening credit spreads of European bank Tier-1 Hybrids, as well as Corporate Hybrids, which accounted for approximately 27% of total holdings. There were with no significant declines in the credit quality of the investment grade (IG) fixed income securities held in the Managed Portfolio. The widening spreads of European bank Tier -1 Hybrids were primarily driven by their long credit duration profile and the high beta nature of these securities. Another security that was heavily impacted was Virgin Australia's 2024 listed bond (~5% of the MP's holding as of 29/2/20). Liquidity stress and solvency concerns have been amplified as all non-essential travel between cities in Australia is effectively prohibited. It is an evolving situation with Virgin discussing bail-out solutions with government as well as potential private bidders providing Virgin with a lifeline. The portfolio benefited from the AUD's depreciation against USD of ~6% for the month of March, with the portfolio holding ~12.4% in USD securities.

We are of the view that market volatility in IG bonds will be short term in nature, given massive monetary intervention and liquidity-support injected by global central banks to ensure that credit markets function properly. We have seen the credit markets begin to stabilize and expect further improvements in liquidity premiums for the bonds held in the portfolio in the June quarter.

## Market overview

The COVID-19 pandemic has created numerous economic uncertainties, leading to considerable pricing volatility within equity and credit markets during the March quarter of 2020.

### Massive global central bank interventions have put a price floor on IG bonds

So far, central banks have introduced extensive liquidity support and asset purchase programs to ensure credit markets are functioning properly. These measures have begun to work and have calmed markets. Asset purchase programs conducted by global central banks have helped to put an effective price floor on high investment grade (IG) bonds. Credit spreads on these securities are gradually recovering from the height of the crisis.

However, market volatility will likely remain until positive developments regarding containment measures and vaccines emerge. Recent data on Australian infection rates is encouraging, with a relative flattening in infection rates. Should this trend continue, we will likely see a severe but short correction in Australia's economy.

<sup>1</sup> The Managed Portfolio Benchmark is the RBA Cash Rate (after fees). Returns are calculated net of management, performance, administration/custody and transaction fees, but excluding any adviser fees from the Managed Portfolio's inception date of 19/09/16, and assumes reinvestment of all income (but not franking credits). Returns are based on the theoretical performance of a portfolio which implemented the Managed Portfolio from the inception date based on simplifying assumptions and stock weightings. Actual individual returns of each client's portfolio will differ depending on factors such as date of initial investment, timing of transactions, contributions and withdrawals, fees and any customisations. Past performance is not a reliable indicator of future performance and may not be achieved in the future. Each client should also take into account their own taxation situations. All information provided in this Report is correct as at the date of this Report.

<sup>2</sup> Weighted averages based on current market prices and target portfolio weights as at 31 March 2020. Running yield includes any applicable franking credits. Expected cash distribution assume 31 March 2020 Managed Portfolio weights are held for the entire quarter and do not include any franking credits – projected coupons are cash only, based on a notional \$200,000 investment at market prices on 31 March 2020. The portfolio is actively managed, and as such actual outcomes will vary with changes made to positions in the portfolio, which may occur at any time. Portfolio statistics are for illustrative purposes only.

The contrast between fixed income and equity asset classes cannot get any clearer. Investment grade fixed income investment portfolios have in general demonstrated more stable returns than the highly volatile share investment portfolio. This has been supported by historical data in the previous three financial crises, as well as market performance in the past quarter.

Performance of major credit and equity indices

Market Indices	Price (31/3/20)	March Performance (%)	March Qtr Performance (%)	12-Month Performance (%)
ASX200	5076.83	-21.2	-24.0	-17.9
AusBond Credit FRN <sup>6</sup>	2721.32	-0.9	-0.6	+1.1
AUD/USD	0.6131	-5.9	-12.7	-13.6
ISHARES US IG ETF <sup>7</sup>	123.51	-6.6	-3.5	3.7
ISHARES US HY ETF <sup>8</sup>	77.07	-10.4	-12.4	-10.9

<sup>6</sup> Bloomberg Ausbond Credit Floating Rate Notes 0+ Yr Index

<sup>7</sup> iShares IBoxx \$ Investment Grade Corporate Bond ETF

<sup>8</sup> iShares IBoxx \$ High Yield Corporate Bond ETF

The key risks associated with fixed income investments are the default risks associated with extending credit. Investors do not suffer losses if the bonds are re-paid in full at maturity. It is important to note that according to Moody's Investors Service, during the most recent global financial crisis (2007-08), the average credit loss rate for IG bonds was approximately 2%.

### Government fiscal stimulus helps to cushion credit deterioration

Although the bonds in the portfolio have been subject to market volatility and illiquidity, none were downgraded during the March quarter. So far in the month of March, we have witnessed very few ratings downgrades to Australian IG issuers. Most negative rating actions in IG bonds have been related to rating outlook changes and reviews for possible rating downgrades.

To-date, negative rating actions have been tempered by significant RBA intervention and government fiscal support, as well as the intrinsic financial strength and flexibilities of the IG issuers. In addition, selected corporates have begun to raise equity to strengthen their balance sheet. These market developments are positive from an IG bond perspective.

Issuer ratings impacted by COVID-19 pandemic by region and rating actions

	Asia Pacific	Europe, the Middle East and Africa	Latin America	North America	Total
Credit watch negative	31	30	11	105	177
Downgrade	5	66	34	164	269
Downgrade & credit watch	2	26	12	68	108
Outlook revision	30	60	18	118	226
<b>Total</b>	<b>68</b>	<b>182</b>	<b>75</b>	<b>455</b>	<b>780</b>

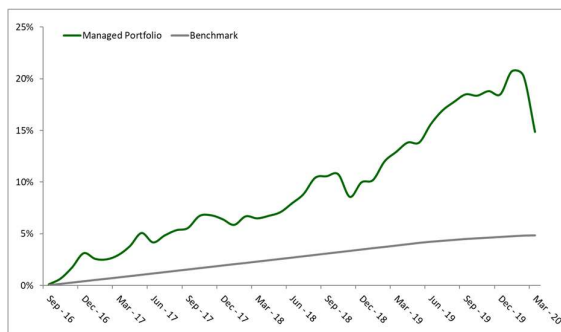
Source: Moody's S&P

### Outlook and Strategy

While it is difficult to predict the magnitude and length of the fall-out from the coronavirus pandemic, markets will likely recover once there are positive developments on COVID-19 global infection rates and clinical trials for vaccines. We are keeping a watchful eye but remain confident that the likelihood of default for the bonds held in the MP is remote.

We have also seen improvements in the liquidity of high investment grade bonds and expect further improvements in liquidity premiums for IG bonds in the June quarter. We will continue to manage the MP through this market volatility by positioning the MP in issuers which are resilient to the impact of the COVID-19 pandemic and those which have intrinsic financial flexibilities to sustain further credit deterioration.

## Performance since inception<sup>1</sup>



## Investment objective & strategy

The investment objective of the Mason Stevens Wholesale Fixed Income Managed Portfolio is to provide investors with a pre-tax return that outperforms the RBA Cash Rate by 3.00%pa after fees over a time horizon greater than three years.

It will seek to achieve this objective by investing in a portfolio of predominantly investment grade fixed interest securities, government, semi-government and corporate bonds, subordinated debt securities, hybrid instruments (including converting preference shares, convertible notes, and income securities), residential mortgage backed securities (RMBS), asset backed securities (ABS), floating rate notes (FRNs), cash and term deposits. The Mandate can invest in over-the-counter (OTC) instruments such as repackaged securities, credit linked notes (CLNs). It may also include international securities.

## Portfolio management

The Managed Portfolio is managed by Mason Stevens Asset Management Pty Limited (MSAM) as the Sub-Investment Adviser. MSAM is part of the Mason Stevens group of companies.

Investment decisions are governed by an Investment Committee that ensures the appropriate discipline and rigour is applied to the investment process.

## About Mason Stevens

Mason Stevens provides a multi-asset and multi-currency investment administration and managed account service to help produce tailored investment outcomes for advisers and their clients. Clients benefit from efficient portfolio

administration, secure online access to their investments, as well as comprehensive reporting.

## Investment team

**Annie Zhao**, Portfolio Manager

**Vincent Hua**, Portfolio Manager & Chief Investment Officer

Other members of the team include: Patrick Eng; Managing Director – Fixed Income; Leanne Leong, Managing Director – Finance & Credit; Peter Liao, Head of Strategy, Performance and Analytics; Roman Gerber, SMA Manager.

## Key features & details

<b>Investment universe</b>	Bonds (corporate, bank, government), subordinated debt securities, hybrids, RMBS, ABS, FRNs, cash deposits, term deposits, Securities may be listed on an exchange or unlisted, including repackaged securities, CLNs and CDSs. It may include overseas securities
<b>Benchmark</b>	RBA Cash Rate
<b>Target return</b>	RBA Cash Rate + 3.00% per annum after fees
<b>Cash weighting limits</b>	0-100%
<b>Maximum non-rated/sub-investment grade weighting</b>	20%
<b>Maximum foreign currency exposure</b>	100%
<b>Minimum investment</b>	\$200,000
<b>Suggested timeframe</b>	3-5 years +

## More information

Further information about the Managed Portfolio, including fees and costs, is outlined in the Mason Stevens Wholesale Fixed Income Managed Portfolio Investment M

### Contact

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Please speak  
to your adviser

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