

Description/strategy

The Fund's investment strategy is to identify appropriate investments from the pool of Australian sovereign and Australian senior bank bonds that are expected to generate a sufficiently high yield, commensurate with the assumed risk, with minimum volatility of returns. The Fund is not benchmark aware so is without a duration target. It is focused on achieving an absolute return. The Fund is best suited to investors who seek a low to medium risk investment over a 1 to 3-year period.

Investment objectives

To provide income and capital stability and a high degree of liquidity in all market conditions. The total return will mainly comprise income from security income payments. The target rate of return is the Bank Bill Swap Rate plus 1.5% before fees.

ESG

Environmental, Social and Governance issues form part of the risk analysis framework.

Fund details

DDH Graham Limited (DDH) is the responsible entity of the fund. As responsible entity, DDH is responsible for the management and administration of the Fund, including the issue of the fund's Product Disclosure Statement and all other public announcements concerning the Fund.

DDH has appointed GCI Australia Pty Ltd ABN 68 140 364 576 (GCI) as the Fund's outsourced investment manager. GCI is a private, boutique asset manager that has significant experience across the many facets of financial markets.

APIR Code DDH8305AU
ARSN 622 419 578

Fund availability

This Fund can be accessed by investing directly, or indirectly, using the BT Panorama, Allan Gray, HUB24, Netwealth and Macquarie Wrap platforms.

Performance to 31 July 2022 (annualised)

	1M %	3M %	6M %	1Y %	2Y %	3Y %	5Y %	Since inception
Total Return	1.31	0.44	-2.41	-4.05	-1.79	-0.83	n/a	0.50
Cash Distribution	0.00	0.31	0.59	1.14	1.07	1.27	n/a	1.65
+/- Growth	1.31	0.13	-3.01	-5.19	-2.86	-2.10	n/a	-1.15
Index	0.12	0.21	0.20	0.22	0.13	0.33	n/a	0.89

*Fund returns are net of all fees – may not sum due to rounding

Australian index returns 31 July 2022

Index	1M Return	3M Return	12M Return
Bloomberg Australia Bank Bill Index	0.12%	0.21%	0.22%
Bloomberg Australia Gov't 3-5 Yr Index	2.29%	1.09%	-6.29%
Bloomberg Australia Composite 0-3 Yr Index	0.80%	0.48%	-2.18%
Bloomberg Australia Composite 3-5 Yr Index	2.44%	1.07%	-6.60%
Bloomberg Australia All Maturities Composite Index	3.36%	0.93%	-9.10%

Returns are calculated using exit prices and are calculated after all fees and costs have been deducted, assumes any distributions are reinvested and no allowance made for tax. The 'distribution' component represents the amount paid by way of distribution, including net realised capital gains. Numbers may not sum due to rounding. Past performance is not an indicator of future performance.

The benchmark is the Bloomberg Australian Bank Bill Index. The inception date of the fund was 25 October 2004. E&P commenced as Investment Manager on 31 December 2010. GCI commenced as Investment Manager on 01 July 2015.

Fund rating

Initially rated 'Favourable' by SQM Research in December 2018, the Fund was upgraded to 'Superior' in December 2020.



Fund Size

As at 31 July 2022, the Net Asset Value of the Fund was \$81,061,243.65.

Portfolio characteristics 31 July 2022

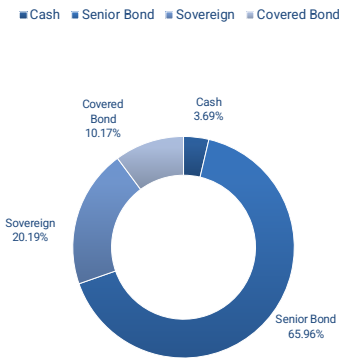
Running Yield	3.36%
Yield to Maturity	3.43%
Average Margin	1.31%
Average Years to Maturity	2.92
Number of Securities Held	34
Floating	29.74%
Fixed	66.57%
Cash	3.69%
Modified Duration	2.68
Credit Duration	0.65

Fees

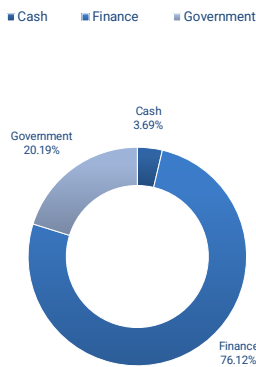
MER	0.40%
Buy/Sell Spread	+0.10%/-0.10%
Performance Fees	Nil

Asset breakdown

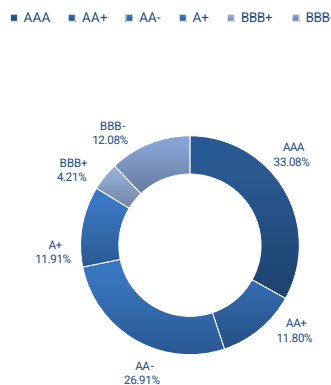
Sub Type Analysis



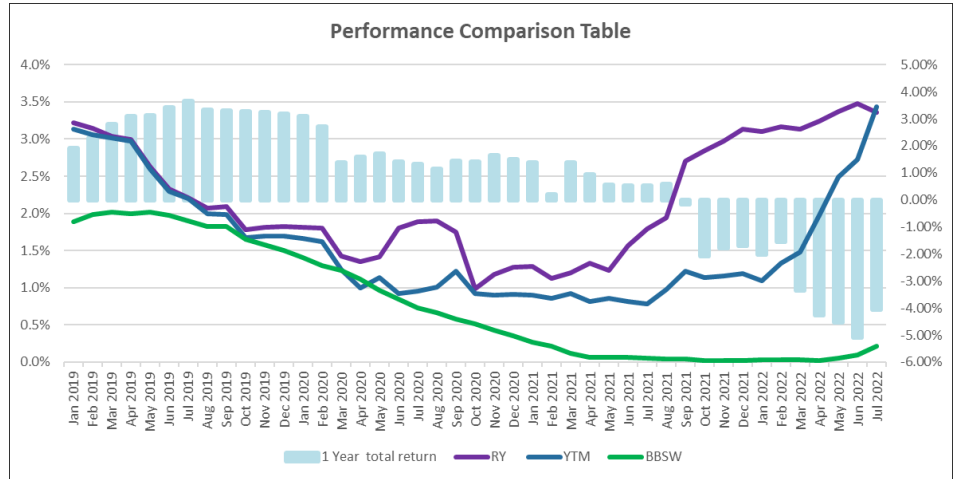
Sector Allocation



Credit Rating



Performance



Source GCI Australia, DDH Graham data

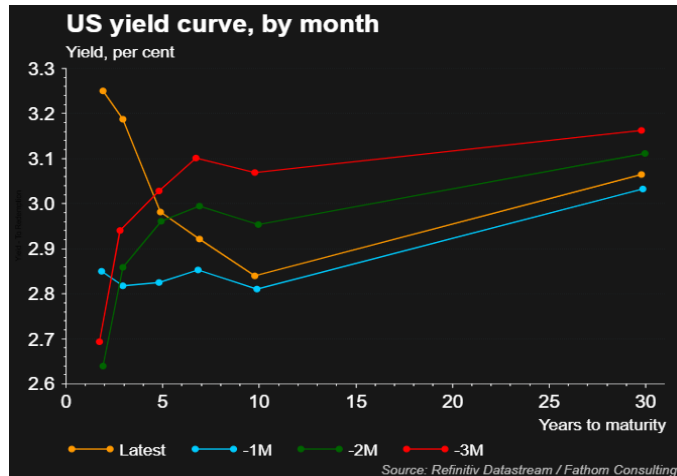
The Fund had a strong monthly return in July of 1.31% benefiting from a flattening of the yield curve following rate rises by the RBA. At the current unit price where all securities have been marked to market the Fund has a running yield of 3.36% and a YTM of 3.43%. These yields are expected to rise further with further increases in official rates reflected in a higher 90-day BBSW rate because many of the securities held have coupons set at a margin above the 90-day BBSW rate, adjusted quarterly.

Market review & outlook

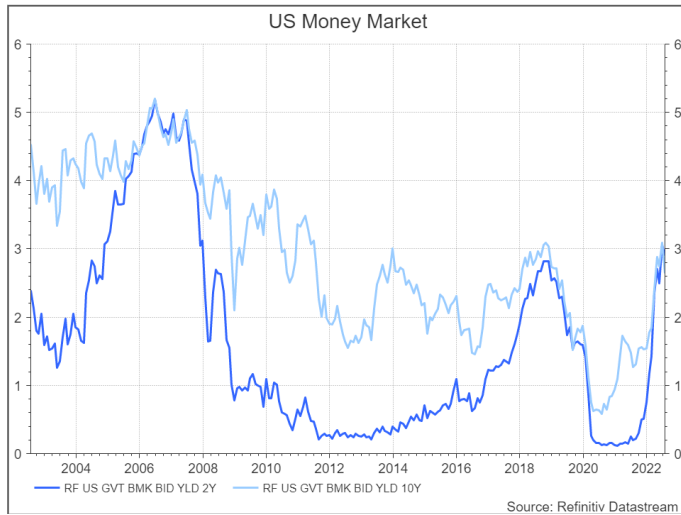
By the end of July investors faced conflicting signals from the US markets. These were:

- US yield curve inversion.
- A decline in both equity and credit market volatility that brought about a contraction in credit margins.

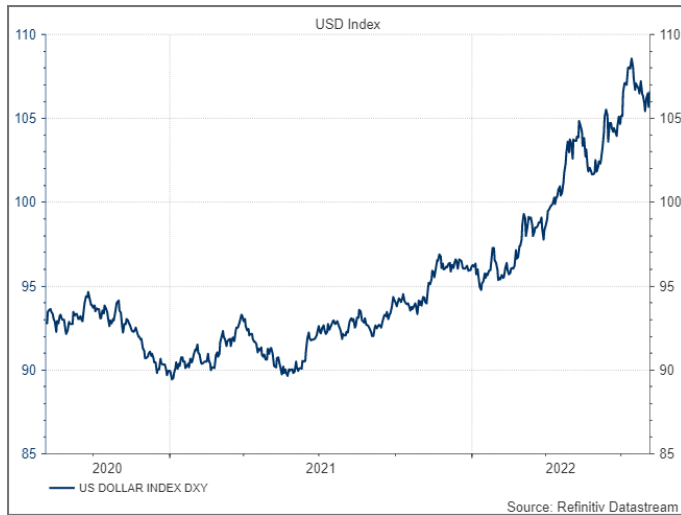
A yield curve inversion occurs when the 10-year benchmark yield falls below the 2-year yield. By the end of July, the yield curve was inverted by 37 basis points. The following chart shows how the US yield curve has inverted gradually over the past three months.



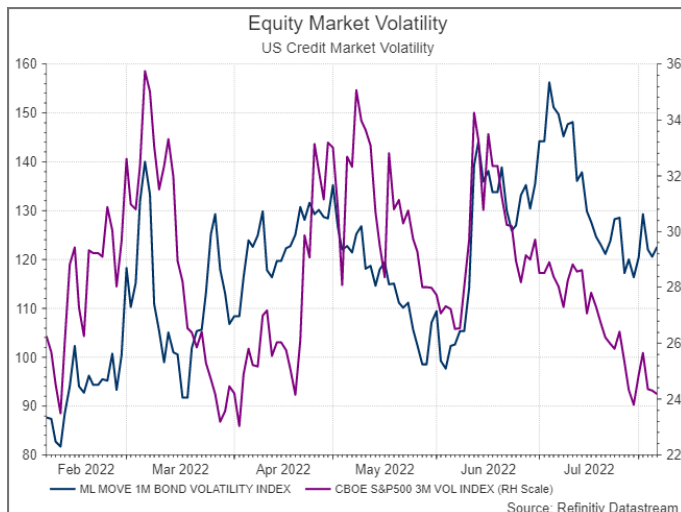
Traditionally, a yield curve inversion happens when the markets believe that the Federal Reserve has either tightened rates too much or left rates too high for too long and an economic contraction will occur in 6-9 months' time. The US bond market has a very good track record of predicting economic slowdowns and contractions. Every time the 2-year yield gets near the 10-year yield the economy slows. The following chart shows the 2-year yield and 10-year yields.



This time the inversion is likely to be due to the expected impact of the USD strength over the past six months. Under a flexible exchange rate mechanism, the transition mechanism for monetary policy is via a change in the exchange rate. By reducing money supply and increasing interest rates the Federal Reserve encourages money to flow into the US which increases the value of the dollar. The higher dollar both reduces the demand for US exports resulting in lower national output and increases the demand for imports because they are now cheaper in USD terms. Monetary Theory may well prove to be more effective than it has been over the past 20 years because of this currency impact.

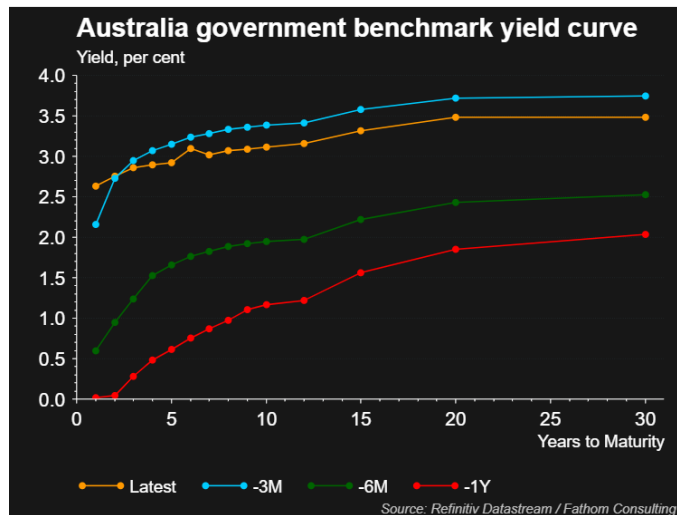


Throughout July both equity and credit market volatility declined amidst the US company reporting season and the ongoing geopolitical events. This decline in volatility has broadly been reflected in a decline in floating rate credit spreads.



If the US benchmark yield curve is correct about a recession in 6-9 months' time, then this will mean an increased risk of corporate debt defaults - particularly in the US where the level of corporate debt is very high. This increased risk would normally bring about wider credit margins while US long-term fixed rates are falling, however, in July this did not occur. The reason we did not see credit margins widen in July is that there is still some uncertainty over whether or not the US will actually enter a real recession amongst the investors that generally hold floating rate bonds and corporates will have held off issuing new bonds until they had reported June quarter results.

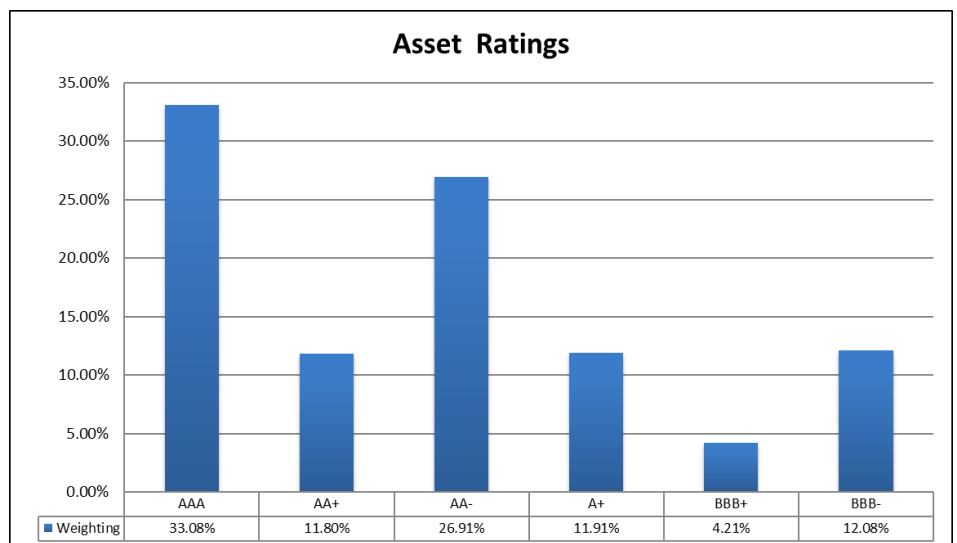
In an Australian context the benchmark yield curve has retained a positive or normal shape, implying that recession is not expected here yet. Bond yields did fall in unison with the US in July, they just did it consistently across the entire curve so that the yield curve held most of its shape.



Fund positioning

In response to our perception that geopolitical, market and economic risks will rise over the next 12 months, funds have been switched actively to higher credit rated issuers over the past few months while still being able to increase the portfolio yields. Prima facie this is an odd outcome, given that higher risk usually supports higher returns, but it is now clear that the pandemic and the actions taken by both governments and central banks have temporarily and intentionally distorted the efficient operation of the markets.

Throughout the past month, funds were rolled from lower-rated, regional bank, floating rate bonds into sovereign or covered AAA rated short-dated bonds. This has resulted in 33.08% of the Fund being in AAA rated bonds. Additionally, the Fund has an 11.80% AA+ weighting which reflects holdings of Commonwealth corporations such as Australia Post and semi-government bonds.



ESG

As an Investment Manager we employ the same ESG policies across all our mandates. We recognise that certain industries represent increased risk from not meeting prescribed ESG principles. This risk can be at a few levels:

- Government regulatory changes.
- Access to capital markets.
- Market pricing reflecting community perceptions.

Our focus is primarily on investigating the governance structures of each issuer as this is central to understanding the underlying business risks. Attention is also given to the level of equality and diversity because we have found that in the long term, businesses that employ the best people regardless of their gender, racial background or age tend to outperform. As part of this we would exclude any business that relies on a supply chain that utilises modern slavery.

Across all the discretionary mandates of GCI Australia there is no exposure to the following industries:

- Gambling.
- The Australian power sector at both generation and distribution levels.
- Fossil fuel mining (coal, gas, oil, uranium).

We do not chase higher short-term returns by investing in offshore company securities because of the increased risks that include currency but also regulatory differences that protect the Australian financial system. Identifying inadequate governance practices is more difficult offshore when we don't fully understand the cultural practices.

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