

Description/strategy

The investment strategy of the Arculus Preferred Income Fund (name changed from DDH Preferred Income Fund on 29 November 2022) is to identify appropriate investments to generate a sufficiently high yield, considering risk and minimum volatility of returns. The Fund is constructed with reference to macroeconomic factors and industry exposure. The Fund does not employ leverage either directly or using derivatives and has no offshore currency or market exposure. Up to 30% of the Fund can be invested in non-investment grade securities (S&P, Fitch rated below BBB-, Moodys rated below Baa3). The Fund is best suited to investors who seek a medium risk investment over a 3 to 5-year period.

Investment objectives

To provide unitholders with returns in excess of cash and bank deposits over the medium to long term by investing in Australian sovereign bonds, senior & subordinate debt issued by Australian financial institutions, senior & subordinate bonds issued by Australian corporates and ASX-listed hybrid and debt securities. The return is a combination of income distribution and capital growth. The target rate of return is the Bank Bill Swap Rate plus 350 basis points.

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 (one of Australia's leading investment management businesses) ABN 68 140 364 576 (GCI) as the Fund's outsourced investment manager. Arculus Funds Management Pty Ltd (Arculus), a wholly owned subsidiary and Corporate Authorised Representative of GCI undertakes the investment management activities for the Fund.

APIR Code DDH0001AU
ARSN 108 161 575

Fund availability

This Fund can be accessed by investing directly, or indirectly, using the Wealth02, HUB24, Netwealth, OneVue, Praemium Investment, Ausmaq, BT Panorama, Macquarie Wrap and Australian Money Market platforms.

Performance to 31 December 2022 (annualised)

	1M	3M	6M	1Y	2Y	3Y	5Y	Since Inception
Total Return	0.80%	2.13%	3.43%	-0.51%	1.85%	2.03%	2.96%	4.35%
Cash Distribution	0.84%	0.85%	1.73%	3.40%	3.26%	3.12%	3.59%	5.34%
+/- Growth	-0.04%	1.28%	1.70%	-3.90%	-1.41%	-1.09%	-0.63%	-0.99%
Index	0.24%	0.74%	1.17%	1.25%	0.64%	0.54%	1.01%	3.33%

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

Australian index returns 31 December 2022

Index	1m Return	3M Return	12M Return
Bloomberg Australia Bank Bill Index	0.24%	0.74%	1.25%
Bloomberg Australia Gov't 3-5 Year Index	-1.13%	0.91%	-5.60%
Bloomberg Australia Composite 0-3 Year Index	-0.18%	0.90%	-1.56%
Bloomberg Australia Composite 3-5 Year Index	-1.04%	1.03%	-5.91%
Bloomberg Australia Composite All Maturities Index	-2.06%	0.38%	-9.71%
ASX Bonds and Hybrids; All Issues incl. franking	2.30%	5.36%	4.28%

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. Arculus commenced as Investment Manager on 01 July 2015.

Fund rating

Initially rated 'Favourable' by SQM Research in December 2016 the Fund was upgraded to 'Superior' in December 2020.



Fund Size

As at 31 December 2022, the Net Asset Value of the Fund was \$210,619,921.51.

Portfolio characteristics 31 December 2022

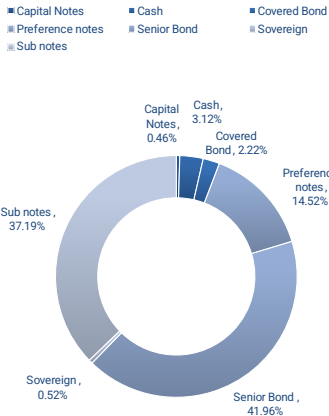
Running Yield	5.69%
Yield to Maturity	6.36%
Average Margin	3.14%
Average Years to Maturity	2.81
Number of Securities Held	46
Fixed	34.69%
Floating	62.19%
Cash	3.12%
Modified Duration	1.30
Credit Duration	1.91

Fees

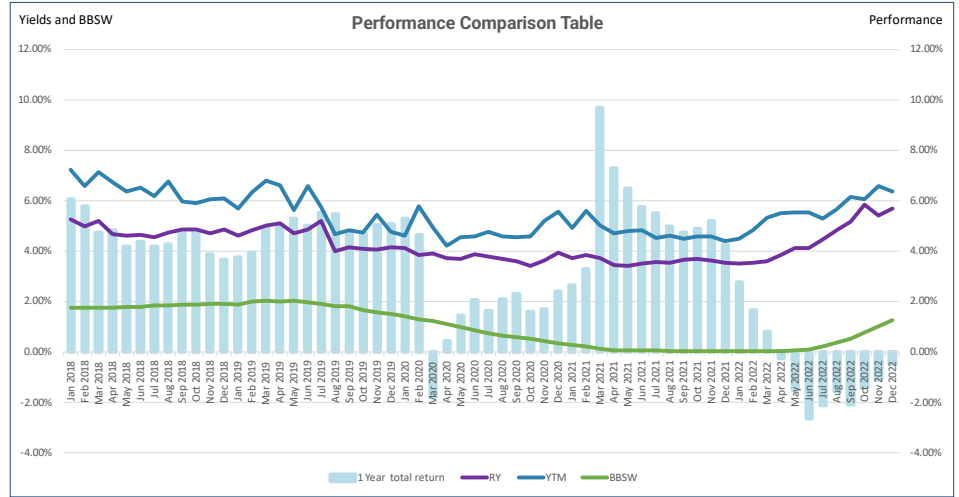
MER	0.82%
Buy/Sell Spread	+0.15% / -0.15%
Performance Fees	Nil

Asset breakdown

Sub Type Analysis



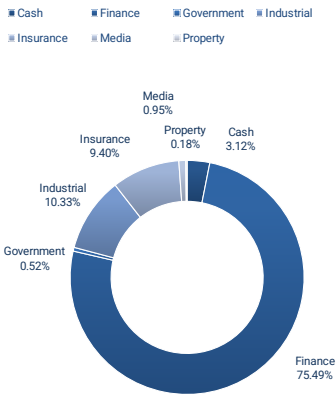
Performance



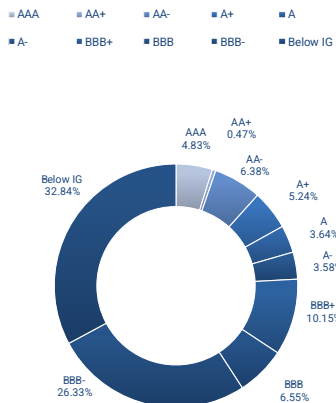
Source Arculus, DDH Graham data

The Fund had a strong performance in December supported by the strong running yield of 5.69% and the YTM of 6.36%. These yields are expected to support performance over the next 12 months in what is likely to be another difficult year for asset markets.

Sector Allocation

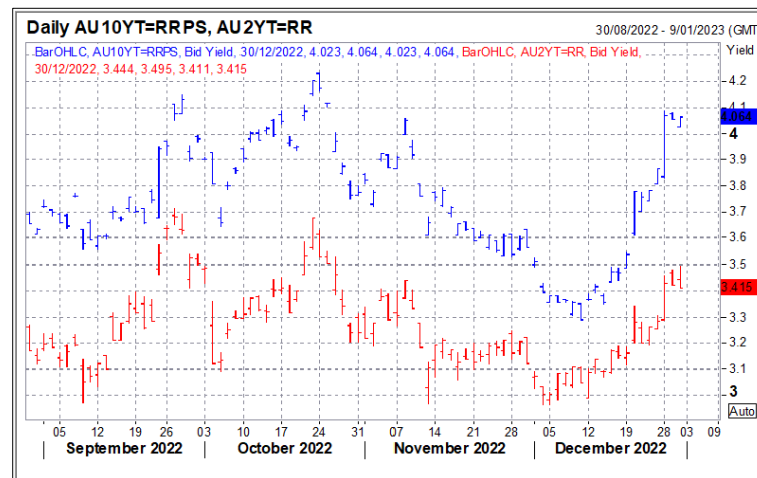


Credit Rating



Market review

December was a month of two halves with a bond rally in the first half following further signs that inflation has peaked in developed economies and then a steep sell-off in the second half (just in time for Christmas) after the Bank of Japan surprised the market by adjusting its yield curve policy. To be clear the Bank of Japan has only moved its yield target for the 10-year Japanese bond from 25 basis points (bps) to 50bps and it has not signalled any intention to make any other changes to monetary policy.



The impact in the week before Christmas on the Australian bond market was much more pronounced. The 2-year bond yield moved from near 3.00% to 3.41% and the 10-year yield rose sharply from 3.29% to finish at 4.06%. The 2-10-year section of the yield curve steepened from near 25bps to 62bps. The steeper yield curve may be reflecting a more positive outlook for the Australian economy with China COVID restrictions being lifted, however, it could also be reflecting offshore investors restoring some of the sovereign risk premium that was there in the June quarter when the Australian 10-year yield was briefly 75bps higher than the US 10-year yield. In November the spread between the Australian 10-year and US 10-year contracted to minus 30bps and has now moved back up to positive 20bps.

These movements in spreads between dollar block bonds may also be the result of a shift out of UK and Euro Area bonds following the bond market's reaction to the Truss Budget in October and perhaps also a move out of the US dollar by investors.

Environmental Social and Governance

Arculus Funds Management believes that integrating Environmental, Social and Governance (ESG) factors into our investment decision-making and ownership practices is fundamental to delivering the results our clients seek.

Investing demands active and ongoing engagement and we are committed to maintaining a focus on long-term sustainability and returns. We also recognise that the ESG investment world is constantly evolving, and we seek to partner with clients and ensure our principles align with theirs on this journey.

At a corporate level, ESG principles influence our people, our culture, and our choices, helping to make us better investors. At an investment level, we consider ESG in our analysis and processes, helping us identify opportunities and risks. Recognising that there is a lack of consistency in ESG implementation and articulation across the industry, we seek to be clear in our communication as well as providing insight for our clients. Arculus does not explicitly exclude any industry, rather we aim to invest only in what we consider to be the best company within an industry group that displays industry leading ESG principles.

Arculus Funds Management's policy is to integrate sustainability risks in their investment solutions across all our products by identifying, evaluating, and managing relevant risks in our investment decisions. We believe sustainability risks are most relevant to investment outcomes when they exhibit financial materiality, and, like all investment risks, are incorporated by balancing expected risk with expected reward. In managing investment solutions, Arculus consider financially-material sustainability risks in the context of expected rewards using a blend of inputs from sources including, but not limited to, our own portfolio managers and external third-party data sources.

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.

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 much more difficult offshore when we are not able to fully understand the cultural practices of that country or verify that the regulatory and governance framework of that country meets our standards.

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