Clime Fixed Interest Fund

Fund Performance - September Quarter 2020

The Clime Fixed Interest Fund's primary objective is capital preservation. It aims to generate income returns above the RBA cash rate in the form of monthly income distributions. Its return objective is to outperform the benchmark of the RBA cash rate +2.0% p.a. The Fund's risk objective is set at 1.5% ± 1.0%, as defined by the weekly change of the annualised standard deviation of the unit price movement.

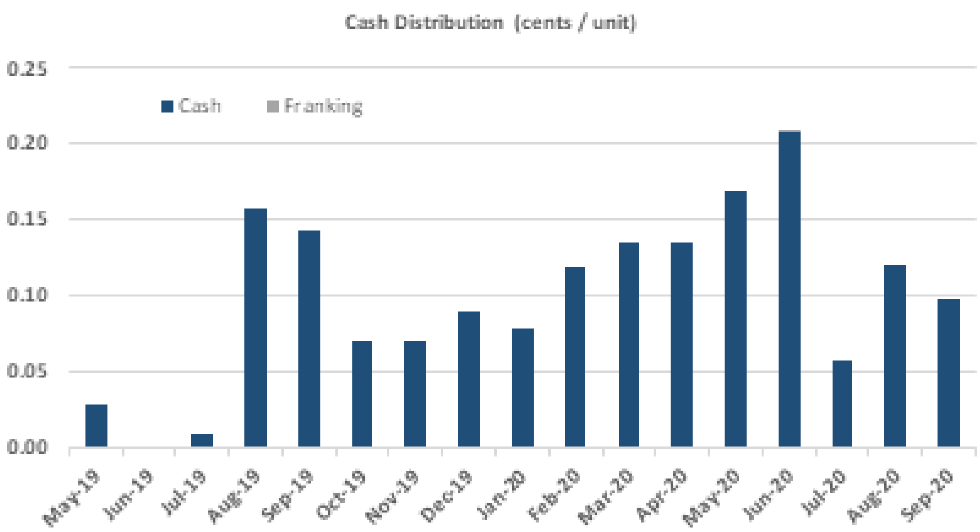
Porfolio Quarter Net Return	Portfolio 6-Month Net Return	Portfolio Net Return Inception p.a.	Fund Size
1.4%	3.8%	2.2%	$21.0m

	1 month	3 months	6 months	1 year	FYTD	Since Inception*
Portfolio Net Return**	0.1%	1.4%	3.8%	1.6%	1.4%	2.2%
Risk				2.2%	-	1.9%

*Inception date: 17 April 2019
**Portfolio return is based on the change of the unit price including distributions and franking.
^The volatility of return is based on the change in the weekly unit price.

Distributions

The Fund distributes income monthly on a cash basis (if available). For the September quarter, we distributed a total of 0.2759 cent / unit, with the latest distribution of 0.0982 cent / unit for the month of September 2020. The chart below shows the monthly distribution profile since inception. After the initial irregular distributions during the formative stages of the Fund, distributions should be more consistent now that the Fund is more fully invested.



Fund Facts

Portfolio Manager	Dr Vincent Chin
Fund Inception	April 2019
Fund Size	$21.0m
Cash Distributions	Monthly

Performance & Volatility of Return

The world has been living with the COVID-19 virus for more than nine months, since it first surfaced in late December 2019, later becoming a global pandemic. With huge fiscal and accommodative monetary policy (including Yield Curve Control or "YCC", a form of QE) implemented swiftly to cushion economic collapse, the subsequent economic data in Australia have been somewhat better than expected. This is not surprising as the equivalent of about 10% of GDP (in various forms) was pumped into the economy. It has felt as though the usual pain that would normally be felt in a cyclical recession was somehow absent, or perhaps it has been delayed due to the Federal Government's temporary support measures.

The enormous stimulus programs introduced in most countries have allowed the world to buy some time to avoid severe economic collapse while the scientists search for effective health solutions. The latest consensus view is that several vaccines may be ready for deployment by early to mid-2021. As investors, we remain hopeful for a credible solution and that the global economy, including that of Australia, will move back to a growth trajectory.

Based on the outcome of the latest FOMC meeting in mid-September, there are unlikely to be any rate increases through to the end of 2023. The Fed announced the adoption of an "average inflation target", a highly significant development because it signals that the Fed may allow inflation to go above the 2% target for some time, seeing that inflation has spent so long below the target. Depending on what average inflation is by then, it may remain low even beyond 2023. This suggests that having an elevated cash level within the Fund in an environment where the return is close to 0% does not make sense, particularly where real returns for cash are now negative.

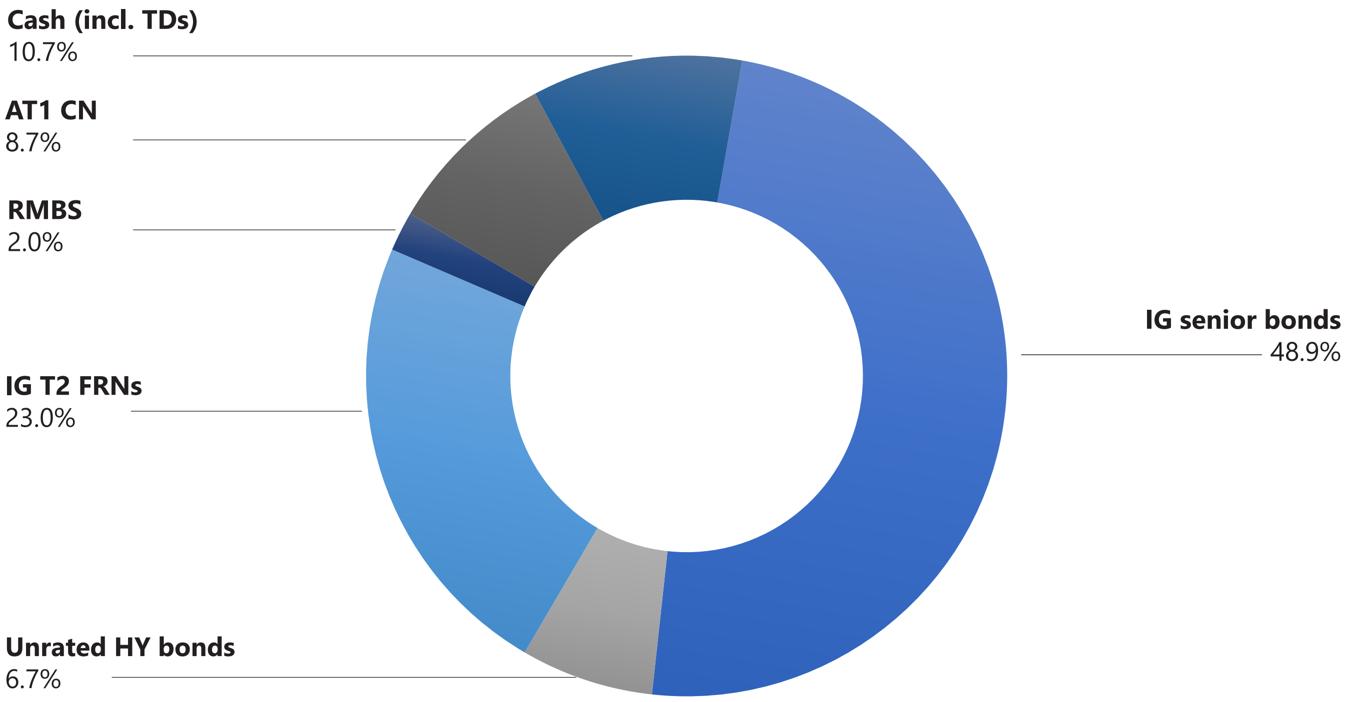
The notion that there might not be interest rate increases for 3 to 4 years suggests that we can be more confident in investing in longer duration fixed rate bonds, potentially beyond 5 years (as we have done this quarter).

The Fund achieved a return of 1.4% in the September 2020 quarter and 2.2% since inception in April 2019. As credit spreads tighten and with the gradual rolling off of duration, the prices of bonds are expected to rise. By late August, we noted that the Fund had recovered its losses incurred from the sell-off in late-February 2020, once monthly distributions are added back. This means that an investor who came into the Fund at the peak unit price in mid-February would have gained back all losses within 6 months, while the equity market as measured by the ASX200 accumulation index is still 16% below its February peak. However, we reiterate that this is not a short-term cash fund and the suggested time frame for this investment is 2 years.

The risk as defined by the annualised weekly change in the unit price is estimated to be 2.2% for the past 12m and 1.9% since inception. This is at the high end of the risk objective, but given the bout of volatility in March 2020, it is understandable. Subject to no significant increase in credit spreads widening, we expect volatility will likely trend lower over time.

In order to generate some meaningful yield, we continue to rebalance and finesse the portfolio's holdings.

Asset Allocation



Portfolio Commentary

At 30 September 2020, the Clime Fixed Interest Fund was diversified across investment grade (IG) senior and IG subordinated debt, high yield bonds, RMBS and AT1 Capital Notes / Hybrids. The largest portion of the portfolio is in investment grade FRNs and fixed rate bonds at around 72%. This is core to our investment strategy as this segment will likely provide the capital preservation / price stability required by the Fund while earning interest returns above that of the RBA cash rate. The objective of these coupons is to provide steady and regular monthly income distributions.

In the September Quarter 2020, we participated in the following investment grade bonds:

- MyState 10NC5 Subordinated T2 deal at 3m BBSW +4.35%;
- Ausgrid 3.5y FRN new benchmark secured senior with a margin of 1.10% over the 3m BBSW;
- QBE 16NC6 T2 FRN rated at 2.75% over the 90-day BBSW;
- Goodman Australia Partnerships (GAP) inaugural AUD bond. The company issued $400mil of 7-year fixed paper at +1.75% to swap;
- CBA 10NC5 Subordinated T2 FRN debt at 3m BBSW + 185bp;
- NSW Electricity Networks Finance (TransGrid), 10y fixed rate bond at 1.77% to swap;
- Ausnet (A-/A3) domestic hybrid 60NC5 FRN at a margin of 3.10% over the 90-day BBSW.

We participated in an OTC NAB AT1 capital notes which was priced at 4.00% + 90 day BBSW. Furthermore, we introduced National Income securities (NABHA) as we see value here.

To accommodate some of these purchases, we rebalanced the portfolio after considering the yield, duration and credit risks of these debt securities and those we exited. As the interest rate will remain extremely low for an extended time, during the quarter the Fund:

- exited a 5y Suncorp senior debt, and
- reduced a NAB subordinated debt slightly to be in line with the peer's exposure.

We are pleased that the outcome of disposing of these bonds has been a positive one. This is attributed mainly to the stronger reversion post the COVID-19 panic for highly rated investment senior bonds. In other words, they have more or less reverted to pre-COVID-19 conditions. As we purchased these bonds well before in early January / February 2020 when the iTraxx dropped below +50bp, we were able to sell these bonds at higher prices, resulting in net positive returns.

By investing in corporate bonds, we have been able to diversify away from predominantly financial debt in the Fund as we continue to invest outside financial credits.

Asset Type	Average Duration (years)
IG Senior Bonds	4.1
IG Tier 2 FRN's	4.3
Unrated HY bonds	3.2
RMBS	2.9
AT1 Capital Notes	5.5

From the table above, note that we have increased the duration slightly to capture a higher yield as we see ultra-low interest rates to remain into the medium term.

Figures below show the breakdown of the credit rating of the IG senior debt.

Rating	Allocation
AA	2.7%
AA-	5.0%
A+	0.8%
A	7.0%
A-	6.8%
BBB+	34.1%
BBB	22.9%
BBB-	8.3%
BB	2.1%
NR	10.2%

Following the rebalancing, we expect the Fund's income generation should increase marginally. We also expect to be able to continue to pay monthly interest.

Outlook

The good news is that the pandemic crisis in Victoria is gradually improving. At 28 September 2020, restrictions have begun to ease. NSW appears to have avoided the worse and it is likely that State borders can further ease, and our economy should commence its recovery. Naturally, our international borders will remain highly restrictive. Consequently, it is likely that international tourism, hospitality, travel and the education sectors will remain weak for an extended period. With this backdrop, it is unlikely that the Australian economy can fully recover until an effective health solution can be found.

Our immediate concern is to navigate the Fund through these crises with certainty of monthly distributions and strong price stability. The Clime Fixed Interest Fund will adhere to its goal-based investment strategy of generating regular monthly income and capital preservation.

We thank you for your ongoing support.

Sincerely,

Vincent Chin, Portfolio Manager - Multi-Asset Income Strategies

Market Commentary

Following the severe COVID-19 global pandemic which commenced in the first months of the year, leading to shut-downs and recessions across the world, the global economy has begun a patchy yet vigorous recovery. This is evidenced by strength in consumer spending, housing activity and surveys of business conditions. In August, the JPMorgan Global Composite purchasing managers index (PMI) rose to 52.4 from 51.0, its highest since the pandemic began (and above its 51.7 average during 2019). Recent Chinese activity data, as well as exports from Japan and Taiwan, suggest global activity has picked up strongly during the third quarter.

The true shape and durability of the recovery in the months remaining until the end of 2020 and beyond, however, remains uncertain. We do not know the path which the pandemic will follow, although prospects for a vaccine and other treatments appear promising. Therefore, it remains unclear the pace at which consumers and businesses will be able to return to near-normal activity, amid the social impacts of the crisis and ongoing requirements for physical distancing and restricted business. Renewed lockdowns in the UK and other parts of Europe will likely weigh on near-term demand.

Equity markets sold off in September as rising virus numbers, the US presidential election and the stalled US fiscal stimulus gained attention. Despite these risks, the prospects for recovery remain positive.

We expect markets to remain volatile as the COVID-19 picture evolves, the earnings outlook becomes clearer, and we approach the end-game for the presidential election in the US. At present, polls suggest a Joe Biden victory over President Trump. We do not expect that this will be a cause for a market correction: whereas Biden may raise corporate taxes, his support for broad social security spending and a higher minimum wage would be a boost for income and consumption, both critical ingredients to the US domestic economy.

Within Australia, the containment of the second wave in Victoria has offered great relief, and the hope is for all lockdown measures and restrictions to be gradually lifted. Economic growth in Australia in the second quarter fell by 7.0%, confirming our first recession in almost 3 decades. This was better than many other countries, with the exception of China, which has staged a quite remarkable recovery. Within the domestic economy, retail sales have been predictably volatile, rising 6.0% over June and July, before falling 4.0% in August, as Victoria's lockdown intensified. But strong home loans data point to a stabilising housing sector, and consumer and business confidence has recently improved. Jobs market data continue to positively surprise, with unemployment dropping back to 6.8% from 7.5%, though renewed weakness may lie ahead.

The strong recovery in China and demand and prices for commodity exports such as iron ore have underpinned an improvement in Australia's outlook. The OECD has lifted its forecast for 2020 from -5.0% to -4.1%. In September, the Reserve Bank of Australia added further stimulus through its bank lending facility, and there has been recent speculation that rates could be cut in November from 0.25% to 0.10%. The federal budget to be brought down on 6 October is expected to provide further stimulus to the economy.

While the global recovery is most welcome, risks remain and volatility in investment markets in coming months would not surprise us. The US Presidential election (and including many Congressional seats and Governorships) remains a fierce battle, and the potential for a contested result creates great uncertainty. Many other risks abound, including further periodic outbreaks of the virus, geopolitical and international trade tensions, record levels of unemployment, disruption of manufacturing supply lines, and relatively high valuations in many markets.

Yet, on balance, unprecedented monetary and fiscal stimulus, a capex pick-up and broad progress in containing the virus suggest the world is still on track for a broad economic recovery. Central banks have been emphatic that they will err on the side of supporting the nascent recovery rather than allow the threat of incipient inflation to curtail their cheap money policies. After a 4.5% decline in 2020, the OECD expects global growth to rebound to 5.1% in 2021. Global interest rates are likely to stay low for an extended period, measured in years rather than months.

As always, we continue to recommend diversification across both securities and asset classes. Increased volatility in the face of the risks and uncertainties alluded to above should be seen as opportunities for asset allocation reviews, and if appropriate, for additional investment in high quality long term themes, such as technology, healthcare, automation, artificial intelligence, and care for the ageing population. We particularly favour securities able to generate growing revenue and profitability streams, and which have the potential to distribute rising levels of dividends over the long term.

Adrian Ezquerro
Head of Investments

Fund Information

Investment Objective

The Fund's main objective is capital preservation. In addition, we aim to generate income returns above the RBA cash rate in the form of monthly income distributions, with a target of 2% over the RBA cash rate (including franking if available). The Fund's risk objective is set at 1.5% ± 1.0%, as defined by weekly changes of the annualised standard deviation, which is substantially lower than the equity market. In order to maximize the chance of achieving these objectives, the recommended investing time frame is at least 2 years.

Investment Methodology

The Clime Fixed Interest Fund seeks to provide an income stream above the RBA cash rate by investing mainly in the over the counter (OTC) market from a range of investment grade senior and subordinated debts, high yield bonds, asset backed securities, RMBS, income notes, capital notes and other fixed income / hybrids securities with a strong capital preservation focus. The portfolio will invest in selected high-quality individual debt and hybrid securities with consistent income generation.

Portfolio Manager

Dr Vincent Chin

Vincent joined Clime in February 2009. He has a wide range of investment experience spanning fixed income to equity. He has more than 10 years of portfolio construction and managing risk across multi-asset classes. Before joining Clime, he gained his investment experience in the late 1990s to 2000s at Ausbil Dexia and Maxim Asset Management (now wholly subsidiary of Charter Hall) where he has developed multi-factors quantitative models for stock selections and attribution performance analysis. Vincent is passionate about ethical investment across any assets including alternate investments. Prior to this, Vincent worked in semiconductor device and material research in academia and industry for more than 15 years. His research spanned III-V and IV groups semiconductor materials and its application. He specialised in transport properties (numerical modelling and characterisation) in these semiconductors for devices and solar cells applications. He has published about 50 international refereed scientific publications and co-edited a proceeding in opto-electronics.

Fund Information

Name	Clime Fixed Interest Fund	**Investor Eligibility**	Wholesale
Structure	Managed Investment Scheme	**Minimum Investment**	100,000
Investment Universe	< 90 to 95% over the counter (OTC) in the capital debt market, AUD denominated only	**Liquidity**	Weekly Unit Pricing Applications and Redemption
Benchmark	Return : RBA cash rate + 2.0%; Risk : 1.5% ± 1.0%	**Fees**	0.41%
Fund Size	$21.0m	**Admin**	Mainstream Fund Services Pty Ltd
APIR Code	CLA0724AU		

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