Antares Income Fund
Monthly Investment Report
January 2024

Fund Performance

Period Ended 31/01/2024	1 Mth %	3 Mths %	1 Yr %	3 Yrs %	5 Yrs %	7 Yrs %	Since Inception %pa[1]
Antares Income Fund	0.38	1.50	6.41	2.54	2.32	2.35	2.51
Bloomberg AusBond Bank Bill Index	0.37	1.09	4.00	1.83	1.44	1.55	1.81
Difference	0.01	0.41	2.42	0.70	0.88	0.80	0.70

Valuation at month end was $174.46M
Antares Income Fund returns are expressed after investment management fees and before taxes; The difference in returns between the Fund and the benchmark may be out due to rounding;
1. Since Inception 31/01/2013

Key Characteristics at 31/01/2024

	Fund	Benchmark
Interest Rate Duration (yrs)	0.10	0.13
Yield to Maturity*	5.47	4.33
Credit Spread Duration (yrs)	2.03	-
Average Credit Rating	A	-
Liquidity**	20%	N/A

*Estimated return if held to maturity. Market yield for Fixed Rate Bonds whilst FRNs uses a swap assumption rate as an input.
**Liquidity deemed available within 24 hours. Consisting of cash and short-term securities that are held directly by the Fund or within the Antares Short Duration Credit Fund which is used to gain an exposure to a pool of diversified credit.

Rating Exposure (by market value %)

Asset Type	MV %
AAA	9.69%
AA+	1.55%
AA	6.58%
AA-	27.76%
A+	3.29%
A	0.01%
A-	12.15%
BBB+	18.08%
BBB	19.09%
BBB-	1.81%

Investment Return Objective

The Antares Income Fund aims to provide investors with a regular income and a return (after fees) that exceeds the Bloomberg AusBond Bank Bill Index over rolling three-year periods.

Distribution History

Distribution Information	Date
Distribution Date	31-Dec-23
Distribution Amount	0.55 Cents Per Unit
Next Distribution Date	31-Mar-24

Portfolio Review

Key Drivers of Portfolio Performance:

- The steepening 3-10yr curve added to returns.
- Fixed rate bank spreads widened 5-8bps detracting from returns.
- Yield enhancement and rolldown of quality investment grade bond holdings added to returns.

Portfolio Activity and Positioning

- Bought Credit Agricole 1/29.

Portfolio Strategy

Strategy	Implementation
Duration and Yield Curve: Our scenario analysis continues to reflect the probability of structurally higher inflation for longer even as growth slows. However, we continue to increase probability to a below trend growth disinflation scenario with growth slowing but remaining positive. We now have equal weighting globally between our below trend growth disinflation scenario and our mild stagflation scenario. In Australia, our base scenario is still a mild stagflation scenario with soft growth and inflation above the RBA target. With the curve steepening we have reduced our overall bear steepening bias but still retain some given the low long term inflation expectations currently priced by the market. Recent stronger economic data supports a soft landing scenario but also increases reflation risks. Markets have pushout the timing of rate cuts but market pricing still remains more aggressive than central bank expectations. We see an increasing likelihood of growth slowing but remain focused on risks of a "stagflation" scenario where there is low growth accompanied by "sticky" inflation, especially in Australia. Geopolitical risks are also another factor that may contribute to reflation risks.	• Markets have started to push out the timing of rate cuts this year after stronger economic data and hawkish central bank rhetoric but remain more aggressive in their discounting of rate cuts than central banks. Current market pricing in the US shows around 5 rate cuts priced, down from 7 at the beginning of 2024. Market pricing in Australia shows 1.7 cuts, down from 2.75. • Markets are convinced of a goldilocks landing outcome, buoyed by falling inflation, the prospects of imminent rate cuts and the continued strength in the labour market and broader economy. This puts the burden back on the Fed to manage inflation expectations going forward. • In Australia, both the rate cycle and progress in the fight against inflation is behind that of the US. With the RBA citing domestic sources of inflation as a key concern, CPI data in January showed evidence of disinflation but inflation still remains elevated in the services sector. • For the RBA to have confidence that it can ease policy settings it will need to see sustainable evidence that disinflation is broad based, across both goods and services. For now, the RBA remains concerned about wage and services inflation, and the impacts of structural, supply side constraints, and government infrastructure spending. • Given the market's confidence that central bank's are going to be able to engineer a goldilocks scenario, the risk remains that if inflation proves "sticky" at above target levels, or we see inflation increase due to geopolitics or event risks, we could see a repricing of longer-term bond yields to reflect a higher inflation risk premium. • Overall, we are more confident that global central banks are better positioned to bring inflation back to target levels compared to the RBA given Australia's higher core inflation and lower cash rate. • **Yield curve:** In Australia, during January, the 3s10s yield curve steepened, driven by lower yields in the short end and higher yields at the long end. Market pricing of long-term inflation expectations in Australia has fallen but remains above the US. With the steepening episodes we saw late 2023 we reduced our exposure to a steepening of longer-term yields, but we still retain an outright curve steepening position. • **Duration:** Antares had held a strategic short duration position since the start of the rising rate cycle but actively reduced the exposure as rates rose. Towards the end of last year, we moved from being short duration to targeting neutral duration across all portfolios. Going forward, we will consider our strategic positioning but for now we are likely to be more tactical off the back of the strong rally at the end of last year and some retracement seen in January.
Credit exposure: We remain selective about credit issuer exposure within portfolios as economic growth slows and credit becomes more expensive with spreads narrowing. With both soft-landing stagflation and disinflation scenarios having more probability weighting, we see a traditional hard landing as less likely.	• **Valuations:** There have been strong positive credit premiums with credit spreads continuing to narrow, reflecting the market's confidence of rate cuts being delivered by central banks and a perceived reduction in recession risks. Overall credit is starting to look more expensive, and we may look to rebalance some credit exposure going forward. • **High quality issuers:** With our outlook for slowing economic growth, we remain focused on holding high quality credit issuers, which we assess as being more resilient to an economic downturn. These include credits with low leverage, strong cashflows, some inflation protection/pricing power, and robust balance sheets. • **Synthetic credit:** Synthetic credit (such as iTraxx CDS) at current levels is relatively tight and could present an opportunity to de-risk portfolios by buying protection. We continue to monitor the economic outlook to determine the timing of potentially adding protection for those portfolios that can use CDS.
Optimising yield through carry and rolldown: Focusing on high quality credits and inflection points on steep curves.	• **Portfolio construction:** We are using our proprietary analytics to harvest attractive rolldown while maximising opportunities per unit of risk. • **Rate and swap term premia:** For long maturity portfolios, we see value in semi-government bonds in the 7-13yr part of the curve versus Commonwealth government bonds. • **Credit term premia:** Longer term corporates have rallied strongly reducing the previously good term premiums available. 2024 has started with a rush of offshore entities (supras, banks, etc) as well as some of the big 4 domestic banks bringing new primary deals to the AUD market.
Liquidity: Where appropriate, we are maintaining liquidity that can be realised in stressed conditions.	• **Portfolio construction:** Selective semis, major banks, and government bonds are seen as core liquidity building blocks across portfolios.

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Market Review

Central banks continued to push back on market pricing of aggressive rate cuts for 2024 after stronger than expected economic data supported the case for a more patient and data dependent path back to policy normalisation.

In January, the US economy showed further resilience, with stronger than expected data in the labour market, GDP, retail sales, and the housing sector, all while sentiment increased and inflation expectations fell.

While markets become more confident of a “goldilocks” outcome, various Fed members raised concerns around reflation risks, pointing to the excess demand still present in the economy. This gave the Fed justification to take a more patient approach in the timing of rate cuts to ensure they are confident that inflation is sustainably moving back to their 2% target.

US markets responded by pushing out the timing of the first rate cut from March to May. US bond yields rose over the month, and the US Treasury curve bear steepened.

In Australia, the RBA’s rhetoric was similar. While inflation data for last quarter showed evidence of strong goods disinflation, the RBA remains concerned about services inflation, a strong labour market, and low productivity levels, which all reflect excess demand as being a key risk to bringing inflation back to their 2.5% target.

Bond markets in Australia responded by pushing out expectations of the first rate cut by the RBA from June to August. The Australian government curve bear steepened, with yields falling in the 2 to 6 year part of the curve and increasing at the back end.

Globally, geopolitical tensions escalated over the month as the US and UK led joint military strikes in the Red Sea, leading to an increase in shipping costs.

Macro Outlook

If you believe current market pricing, the outlook for 2024 offers a goldilocks outcome where disinflation continues to trend back towards target without the recessionary impact that usually accompanies such an aggressive rate hiking cycle.

The problem with this scenario is that we keep getting upside surprises in the economic data, which suggests that the market’s timing of rate cuts is premature. And while markets are starting to listen to the messaging coming out of the Fed and the RBA around how the resilience in the economy to date requires more patience in the timing of the rate easing cycle ahead, there still exists a large divergence between the two.

It has been difficult to know how much of the disinflation we are seeing is attributable to the impact of restrictive monetary policy when the economy has held up relatively well, and most of the disinflation has been driven by the goods sector, reflecting improving supply chains post pandemic. Services inflation remains elevated.

Geopolitical tensions are now also contributing to reflation risks. This adds to the risk of the outcome that central bankers fear, which is where inflation becomes structurally embedded in the broader economy. To date, inflation breakeven rates remain well within the 2-3% band, however, the longer it takes to bring inflation back to target, the greater the risk to this outcome.

Antares Scenario Analysis

The Antares Scenarios table reflects the interplay between growth, inflation, and bond yields, and how they will drive the level and shape of yield curves in the different scenarios.

Antares Scenarios - Growth & Inflation - Latest Market Yields

Scenarios		AU GDP	AU Inflation	1YR	AU 3YR Bond	AU 5YR Bond	AU 10YR Bond	AU 30YR Bond	US 10YR Bond	iTraxx	Probability Weighting
1	Strong Growth	5.00%	4.50%	6.30%	6.75%	7.43%	7.88%	8.38%	7.88%	150	0.1%
2	Above Trend	4.00%	3.50%	5.25%	5.78%	5.95%	6.13%	6.63%	5.95%	110	2.6%
3	Trend	3.00%	2.50%	3.50%	3.88%	4.00%	4.25%	4.75%	4.38%	75	18.8%
4	Below Trend	1.50%	1.50%	1.95%	2.03%	2.18%	2.40%	2.70%	2.48%	100	23.2%
5	Recession	-2.00%	0.50%	1.25%	1.50%	1.75%	2.25%	2.75%	2.00%	250	9.1%
6a	Stagflation (low growth/high inflation)	1.50%	3.50%	4.38%	4.55%	4.73%	5.08%	5.25%	5.25%	150	34.6%
6b	Stagflation (neg growth/high inflation)	-1.50%	3.25%	3.25%	3.58%	3.90%	4.23%	4.88%	4.23%	150	11.5%
Market	Latest Yields as @	14/02/2024		4.18%	3.87%	3.91%	4.27%	4.59%	4.31%	69.2	

In January, Antares continued to reallocate weight from stagflation scenarios where inflation remains structurally higher above central bank targets with both a low positive growth (6a) and a negative/recessionary growth (6b) scenario, to the below trend scenario, acknowledging the continued disinflation data.

However, strong economic data in January showed that resilience in the economy and labour markets remains, despite restrictive monetary policy settings. This suggests there are still risks around a structurally higher for longer inflation outcome, which is why we still retain a large probability weighting to scenario (6a). Here, we see the potential for bear flattening as central banks see the need to continue to tighten or maintain restrictive policy settings as growth remains low but positive and unemployment remains low.

If inflation does turn out to be structurally higher than expected or we see reflation risks materialise, then we could also see the potential for curve steepening under stagflation scenario 6b as central banks struggle to maintain a restrictive policy setting while the economic backdrop deteriorates. If this scenario were to play out, there is a risk that markets could lose confidence in the ability of Central Banks to use monetary policy to bring inflation back to target.

Interest Rate & Inflation Outlook

As flagged in our December report, the risk of an unwinding in near-term rate cut expectations in the US came to fruition in January. Several members of the FOMC helped walk back market expectations for an early cut in March, with the market at one point implying 35bps of cuts.

The market continues to look for 5-6 cuts over the next year, albeit from a later starting point, with the first fully priced rate cut expected by June. In a similar vein, the market expects the RBA policy rate to drop by 50bps by year end with the first cut deferred from June to August, following the RBA meeting.

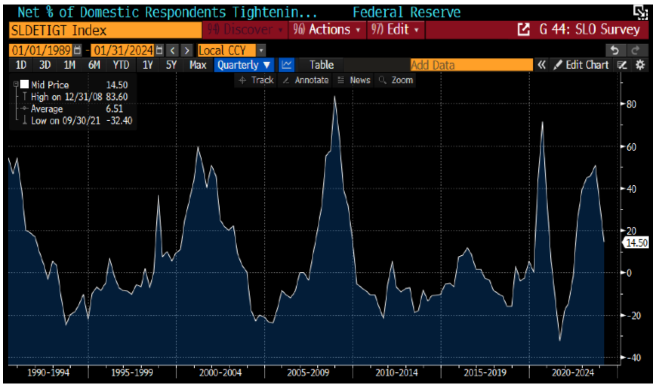
The newly formatted RBA meeting presented a balanced assessment of the risks to inflation, remaining moderately hawkish given still elevated inflation and a move to a hard 2.5% target. The RBA received some encouragement on this front with a weaker-than expected Q423 CPI print. The report highlighted a notable deceleration in inflation, coming well inside the RBA’s forecast profile. As a result, the RBA now expects inflation to moderate to 3.2% by Dec 2024, 2.8% by Dec 25 and 2.6% by mid-2026.

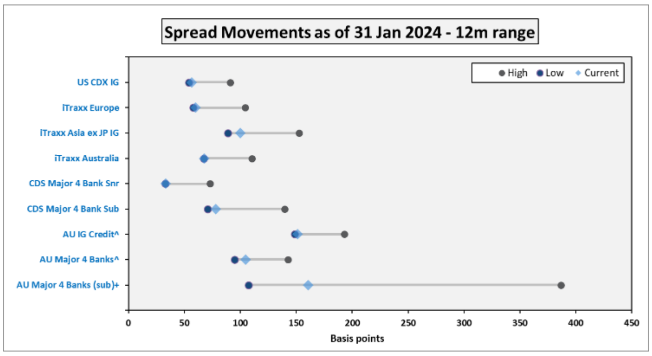
Credit Outlook

January started the year with record corporate bond issuance in Australia and the US which was met with solid investor demand. During the month credit spreads mostly tracking sideways or slightly tighter. Investment grade indices and synthetic CDS indices ended the month mostly unchanged from the December 2023 level, but US high yield index credit spreads tightened another 30 bps to 330 bps. At the current spread level, the implied US high yield corporate default rate is around 4.1% if we assume a recovery value of 20%, which is lower than the current 12-month trailing US high yield default rate of 4.4%. S&P expects the US high yield default rate to reach at least 5% by September 2024, which implies that credit spreads of US high yield should be at least 400 bps based on a 20% recovery rate.

Underpinning the continued spread tightening trend is the rapid easing of financial conditions that was observed in November and December 2023. The latest US Senior Loan Officer survey shows a sharp drop in the percentage of respondents reporting a tightening of lending standards, which declined from 34% in the September 2023 quarter to 14.5% in the December quarter. We believe this is a sign that the loose capital market conditions are likely to start to translate into U.S real economy soon.

Furthermore, several U.S regional banks, small Japanese banks, and specialist European banks have reported large asset impairments due to their exposure to U.S commercial real estate. So far, the market has treated these stories as idiosyncratic issues, but we think there is likely to be further negative news relating to this segment throughout 2024.



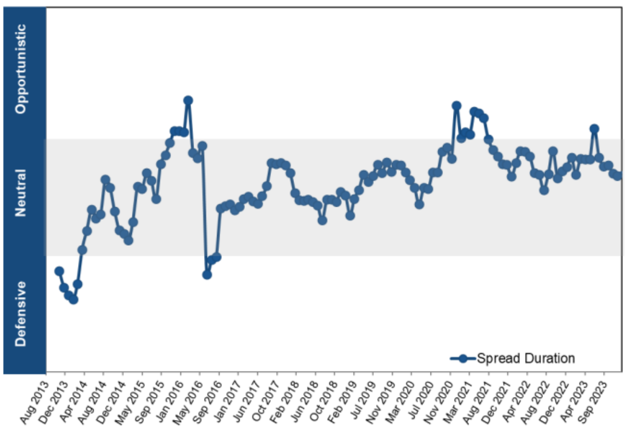


ESG

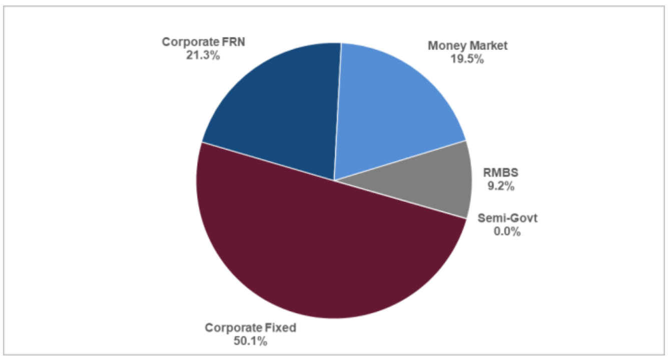
We have decided to increase Toyota's Governance risk score from Low to Moderate to reflect the Daihatsu Motor safety test manipulation scandal. In December 2023, Toyota announced that it was suspending shipments of all vehicles manufactured by its subsidiary Daihatsu Motor following an independent investigation into the alleged manipulation of safety test results involving 64 models. The investigation revealed that Daihatsu Motor had used a different airbag control unit in crash tests than the one used in products sold to the public. The misconduct also included false reports on headrest impact tests and test speeds for some models. Some cases trace back decades. Daihatsu recalled 322,749 vehicles in Japan after this revelation, while The Ministry of Land, Infrastructure, Transport, and Tourism (MLIT) of Japan has taken disciplinary actions against Daihatsu, including revoking its safety certification for certain models.

Whilst we don't believe this controversy will have a material financial impact on Toyota, the nature and length of the deceptive behaviour raises concerns for Toyota's internal control and corporate culture. This is not the first time it's been revealed that Toyota's subsidiaries have engaged in fraudulent practices, as Hino Motor, one of its other subsidiaries, was found in 2022 to have falsified emissions data on at least 115,525 vehicles since 2016. These events raise a red flag for potential wider and more persistent problems within Toyota's corporate culture, not to mention the reputational damage to the brand. However, we take some comfort in the fact that the Daihatsu scandal was discovered through Toyota's internal whistleblower channel and the independent investigations were commissioned by the company itself, which gives us some confidence in the effectiveness of Toyota's internal controls.

Defensive to Opportunistic



Sector Breakdown (Market Value %)



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About Antares Fixed Income

Antares Fixed Income (Antares) is a specialist fixed interest manager covering a range of domestic and international securities. Antares has managed fixed interest and cash portfolios for investors since 1990 and currently has over A$25.67 billion* in funds under management across a range of cash management, fixed income and liability driven investment strategies. Antares is focused on delivering performance objectives for its clients within a carefully managed and defined risk framework.

*as at 30 June 2023

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Important information