Kapstream
—JANUS HENDERSON—
Monthly Report

# Kapstream Absolute Return Income Fund

## April 2021

### Performance

| | Month (%) | 3 Months (%) | 1 year (%) | 3 years (%) p.a. | 5 years (%) p.a. | Since Inception[1] (%) p.a. |
|---|---|---|---|---|---|---|
| Fund Return (before fees and sell spread) | 0.16 | -0.05 | 2.95 | 2.69 | 3.13 | 4.94 |
| Fund Return (after fees, before sell spread)[1] | 0.12 | -0.16 | 2.51 | 2.23 | 2.68 | 4.59 |
| Fund Return (after fees and sell spread)[2] | 0.12 | -0.13 | 2.74 | 2.20 | 2.67 | 4.59 |
| RBA Cash Rate | 0.01 | 0.02 | 0.18 | 0.85 | 1.12 | 2.91 |
| *Active return[3] (before fees and sell spread)* | 0.15 | -0.07 | 2.77 | 1.85 | 2.01 | 2.03 |
| *Active return[3] (after fees and sell spread)[2]* | 0.11 | -0.16 | 2.56 | 1.36 | 1.54 | 1.67 |
| Bloomberg AusBond Banks Bill Index | 0.00 | 0.00 | 0.07 | 1.06 | 1.36 | 3.16 |

**Past performance is no guarantee of future results.** After fee returns are inclusive of 0.41% annualised total expenses for class I units. Fund inception date 31 May 2007. No allowance is made for tax. Numbers may not add due to rounding. 1) For a continuing investor the actual return experienced based on the NAV performance of the Fund, after accounting for management fees. 2) The return experienced by a redeeming investor, based on the exit price performance of the Fund which accounts for the end of period sell spread of 0.07% and management fees. 3) Active return of the Fund compared to Benchmark (RBA Cash Rate).
Source: Fidante Partners Limited, 30 April 2021.

### Performance & Market Commentary

The fund returned +0.12% in April (after I class unit fees), and over the trailing 12 month period showing a pleasing return to form by comfortably exceeding its cash +2% return objective. Coupon income remained the primary driver of returns. Interest rate exposure, at ~1 years' duration, was neutral for returns over the month but remains a negative calendar YTD as rates moved higher amidst renewed inflation concerns. Increased prospects for US fiscal stimulus led markets to believe growth would rebound quicker than anticipated, leading to increased inflation expectations. We don't believe in material inflation risks and expect to continue to predominantly hold bonds with 2-7 year maturities with expectations that central banks will keep rates low for the next 2-3 years. Default risks in high-quality corporate bonds remain small although current pricing more accurately reflects this decreased risk. A small US dollar short position vs. the CAD, GBP, JPY and Euro, which cost the portfolio about 3bp to performance over the month, unwinding gains from March.

### Outlook & Portfolio Strategy

We remain optimistic on global recovery, perhaps seeing global GDP return to pre-COVID levels by Q3 2021, the primary driver being further good news on the vaccine front. We expect greater levels of vaccination will open businesses sooner and permeate to additional pockets of global economies. However, the effects of the pandemic will remain with us throughout 2021 and 2022, particularly in Australia as the border remains closed through the first quarter of 2022. Although we expect a temporary spike in inflation, persistently high inflation is not a story for 2021, given it will take many years to reach full employment, globally. We remain confident being on the front end of the yield curve as there has been less volatility which we believe will remain the case.

It will take years for US jobs to fully recover the more than 20 million lost over the crisis. We expect the Federal Reserve to continue its bond purchases and keep rates at zero for the intermediate term. In Australia, the Reserve Bank will also maintain low rates while continuing its purchase program, preventing any sharp rise in yields. Job growth will be the key, with the RBA maintaining ultra-accommodative policies until unemployment falls below 5%, a minimum target for inflation to move into the RBA's 2-3% target. With unemployment currently at 5.9%, it may take years to reach.

As telegraphed, we have maintained low cash levels given penalty rates. Strong consumer balance sheets, fiscal expansion and expectations for solid employment data (once the vaccine begins wider distribution) add to our more optimistic outlook. The ability for US Democrats to pass budget legislation including greater COVID-19 relief programs mean both fiscal and monetary stimulus will be running on all cylinders in the shorter-run. Whilst we believe bond yields have risen beyond our medium-term expectations, we will maintain slightly shorter interest-rate duration in the 1 year range as volatility has increased.

Low short-term rates are a given for the next 12-18 months. We are not believers in the consensus view for a steeper yield curve as massive deficits fuel record US Treasury bond issuance. Lessons from Japan and Europe demonstrate longer-term deflation risks combined with central bank purchases override supply concerns. Nonetheless 2-7 year bonds remain attractive given their yield advantage over cash rates and prospects for 'roll-down' gains or yields falling as these bonds move closer toward maturity.

Bond market liquidity continues to improve toward pre COVID-19 levels. We remain 100% investment grade, biased toward shorter dated (<7yr) issues, and with a continued avoidance of more volatile or higher beta sectors (such as commodity, energy, gaming, tourism and autos) as well as the worst affected regions. We maintain only a modest exposure to China (and only in USD-denominated quasi-sovereign issuers), and otherwise nothing in emerging markets. Our portfolio can be simply split across three major 'buckets'; financials (~40%), corporates (~35%), and mortgage-backed (~15%) with the residual in governments and cash. Geographically, we have maintained a roughly 2/3rds to 1/3rd split between Australian and international issuers (the latter divided between the US and developed Asia). Again, we have no greater concern with default risk across any portfolios we manage as we did before the turmoil in markets began.

For the coming period our main goal will remain protecting the portfolio from a further sell-off in risk assets and corporate bond spreads.

## Contact Details

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