Kapstream
—JANUS HENDERSON—

Kapstream Absolute Return Income Fund

KANGANEWS AWARDS 2017, 2018, 2019, 2021, 2022, 2023 — WINNER – AUSTRALIAN CREDIT FUND MANAGER OF THE YEAR

Fund Objective

The Fund aims to provide a superior stream of income and capital stability over the medium term while aiming to outperform its benchmark through market cycles.

Fund Application

Investors seeking to enhance their overall fixed income returns with a higher yielding, predominantly investment grade (IG), absolute return-oriented global fixed income portfolio.

Fund Details

APIR code	HOW0165AU
Inception date	31 May 2007
Fund size	AUD 2012.73M
Distribution frequency	Quarterly
Management fee	0.41%
Buy/sell spread	Please contact us for latest spreads

Fund Statistics

Interest rate duration	0.8yrs
Credit spread duration	2.23yrs
Average credit rating	BBB+
No of issuers	77
Yield to maturity	5.39%

Fund Guidelines

Target return	cash plus 2-3%
Target volatility	less than 1.5% annualised
Duration limits	-2 to +2 years
Credit quality	>85% investment grade

Dan Siluk
Portfolio Manager

Dylan Bourke
Portfolio Manager

May 2025

Performance (%)	1 month	3 months	1 year	3 years p.a.	5 years p.a.	Annualised since inception
Fund Return (before fees and sell spread)	0.67	1.30	7.54	5.56	3.78	4.73
Fund Return (after fees, before sell spread)[1]	0.63	1.21	7.07	5.11	3.35	4.35
Fund Return (after fees and sell spread)[2]	0.63	1.21	7.08	5.11	3.39	4.35
RBA Cash Rate	0.32	1.00	4.26	3.71	2.27	2.88
Active return[3] (before fees and sell spread)	0.34	0.30	3.28	1.84	1.52	1.85
Active return[3] (after fees and sell spread)[2]	0.31	0.21	2.81	1.40	1.12	1.47
Bloomberg AusBond Bank Bills Index	0.34	1.05	4.42	3.79	2.28	3.07

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, 31 May 2025.

Performance Commentary

The Fund added 0.63% in May, taking 12 month returns to 7.08% (after accounting for Class I fees). This was significantly above returns from the cash benchmark, as May saw the market walk back much of the negative reaction to Liberation Day tariffs. Risk markets rebounded quickly, with equities such as the S&P 500 re-taking not just the early April levels but approaching the record highs set in February. Similarly, credit spreads compressed but are still above the low levels seen earlier in the year. Bond yields finished the month more mixed. US 2-year yields have recovered to their early April levels, while longer-dated yields such as US 30-year yields are well above on supply concerns. Outside the US, front-end yields remain lower than levels seen a month ago - the negative growth impacts of even lower levels of tariffs remains. In Australia, a second RBA rate cut for this cycle has lowered the cash rate to 3.85%. Nonetheless, the yield to maturity on the portfolio rose 10bps to 5.37% on the further additional spread accessed in May. This remains a solid base for absolute and relative-to-cash returns looking forward.

Market Commentary

Just as the tariffs have been wound back from their initial levels, so has the market's reaction reversed. Deals, delays, exceptions and even courts striking the tariffs down (albeit temporarily) have all seen the size and economic implications of the tariffs reduce. Many of the moves that had begun to be unwound in from early April, continued into May. Risk markets continued to climb and ended the month around halfway between the Liberation Day levels of early April (i.e. before the big moves in response) and the record highs of February before the tariff fears became the dominant market theme. In contrast, the US dollar has not rebounded with one market narrative being that the US exceptionalism premium is being unwound.

Similar to the rebound in equities, credit spreads are broadly back to Liberation Day levels but are not making fresh lows for the recent cycle. The Bloomberg US Aggregate Corporate Average OAS index compressed 17bps to 88bps in May, remaining above the 74bps low seen in November. The Australian Credit Index spread to swap fell 5bps to also be at 88bps, above the lows of 81 bps in late February.

Bond markets are having a much less clear time of it. US 2-year yields were up 29bps in the month and are now back to their pre-Liberation Day level, as the fears about economy killing sized tariffs has reduced and the inflation fears have balanced these out. However, US 30-year yields have risen to now be back to their 2023 highs (2-year yields are ~100bps below as the Fed has cut rates). This steepening reflects additional term premium built it to compensate for the significant amount of bond issuance that is expected with the currently expected policy outlook. Outside of the US, yields at the front end of the curve are generally considerably below the early April levels. For example, Australian 3-year yields were up just 1bp, as the RBA continued with a second 25bps easing this cycle to 3.85% and presented a very dovish outlook due to tariff-related downside risks to economic activity. German 2-year yields were up 9bps to 1.78%, while Canadian 2-year yields were up 11bps.

Outlook

Policy uncertainty moderately significantly in May, but April was not a high hurdle to beat on that front. The market is being reminded of US President Trump's *modus operandi*. Start with an outlandish starting position and get negotiated down to something still outlandish but much more reasonable than what was outlined. We expect this to continue not just over the course of this year but throughout the next four years.

Markets may have mostly recovered from the own goal from the policy announcements regarding tariffs, but we are not back to where we are in an economic sense. Effective tariff rates, even if the lower increase of 10% is implemented across the board at a minimum, represents a significant jump in the context of the past 100 years. Central banks will have to wrestle with the inflationary impacts of the tariffs versus what will be a notable negative impact on activity on what amounts to an increased tax on trade. The positive benefits from any fiscal boost from the big, beautiful bill are expected to offset these, which is why we remain defensive in the rates space.

Portfolio Strategy

Credit carry and spread tightening also added to returns in May. The portfolios were again active in the post Liberation Day volatility. The portfolio's spread duration increased as we added new issues, we found attractive, as new financial and corporate issues that were delayed over a more volatile April were issued. We bought credits with higher new issue concessions and tended to have a higher beta. We used April and May as an opportunity to bolster the credit spread compared to Pre-Liberation Day. The Fund's near decade high coupon is providing higher return stability due to an above-average credit spread from shorter-term assets and an attractive cash rate. This makes us cautiously optimistic about future return prospects.

The outlook for risk assets is nuanced, now they have rallied back significantly. Over the next few months there is risks to sentiment including tariff negotiations with Europe and China, risks around the timing or ability to pass the 'Big Beautiful Bill', risks around lifting the debt ceiling, as well as long end funding risks for countries including the US and Japan. All these offer the opportunity for shorter term wobbles that are likely to be resolved quickly. Over the medium term, the Trump Administration will likely need a strong economic tailwind leading into the 2026 midterm elections, with positive economic actions likely starting in the second half of 2025. As such lower taxes, and a likely boom in corporate investment in the US may provide a solid underpinning for US earnings and global sentiment.

Fund Platform Availability

- AMP North, Wealthview, eWrap
- AMP PortfolioCare (Badge of Asgard)
- Asgard eWrap & Infinity
- Australian Money Market
- Australian Unity Lifeplan Investment Bond
- BT Panorama
- Centric Wealth (Findex)
- CFS Edge, FirstChoice & FirstWrap
- Clearstream/Ausmaq
- DASH
- Grow Wrap (Insignia)
- Hillross PortfolioCare (Badge of Asgard)
- HUB24
- Insignia – eXpand
- Insignia – Rhythm (private label HUB24)
- Insignia – Asset Administrator (BT Badge)
- Macquarie, Accumulator, Wrap IDPS and Super
- Mason Stevens
- Netwealth
- Praemium
- Powerwrap
- Oasis
- OnePath
- OneAnswer
- OneVue
- Platform Plus (Infocus)
- Voyage (Oasis Badge)
- Xplore Wealth

We plan to maintain our spread duration at around 2 - 2.5 years in the upcoming months, balancing our view that we expect the US government to potentially extend the credit cycle, offset by the possibility of short bouts of tariff and policy induced volatility. The exposure has been skewed towards Australian credit because credit spreads were closer to their long-term averages compared to the significantly tighter spreads observed in the US before this sell-off. Considering the sustained interest from yield-seeking high-net-worth and Asian investors, we anticipate that Australian spreads will likely move back towards the lower end of their historical ranges, unless disrupted by an unforeseen macro event.

In terms of asset allocation, the portfolio can be split across three major ‘buckets’; financials (~64%), corporates and REITs (~17%), and asset and mortgage-backed securities (<15%), with the residual in cash and liquids. Close to ~76% of the portfolio is held in Australian & New Zealand names, and by currency <5% is held in non-AUD denominated securities.

Portfolio liquidity remains strong with ‘Level 1’ liquidity at ~10% (cash, commercial paper, SSGA) and at the high end of the range for ‘Level 2’ liquidity at ~16% (<1yr investment grade paper).

After rates duration was reduced notably in April, to take advantage of the additional emergency rate cuts that were built into the curve, these reductions were unwound in May as yields rebounded. The Funds are now back to something close to the structural or average amount of duration we have in the portfolio. Kapstream views this as being particularly important as a hedge against other sharp deteriorations in risk sentiment that could occur. This risk remains spread in not just the US but several regions where we think it’s of the most value: namely Europe and New Zealand. Our exposures in Canada have been trimmed with recent increases in core inflation.