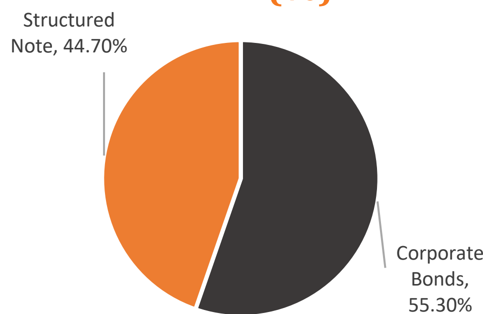
Asset Allocation (%)



Portfolio Key Statistics

Yield to Maturity	4.58%
Average Risk Rating	Upper Medium
Number of Securities	10
Mod Duration	1.28
Credit Duration	1.88
Std Dev	0.43%
Sharpe Ratio	8.58

Portfolio Objective

The portfolio aims to outperform the RBA Cash Rate by 1.5% over the medium term (before fees). It also aims to provide higher income returns than traditional cash investments.

The objective of the portfolio is to provide income with an investment strategy focused on a diversified, high conviction set of investments with either stable or improving credit outlooks.

Although this is not a cash portfolio the focus is on assets which are transparent in terms of price and liquidity. This portfolio is typically used as a defensive investment and therefore capital preservation is equally important as steady, dependable income streams.

BondAdviser Income Plus Model Portfolio

Quarterly Review (March 2017)

Portfolio Performance

The BondAdviser Income Plus Model Portfolio delivered 1.39% over the quarter and 5.43% for the full year (pre-fees) to outperform the benchmark (RBA Cash Rate + 1.5%) by 0.65% and 2.32% respectively.

In terms of individual exposures, the main positive contributors to performance were Qantas 6.50% 2020 (ASX: YTMQF1), returning 0.32%, Wesfarmers 4.75% 2020 (ASX Code: YTMWE1) returning 0.26% and Telstra 7.75% 2020 (ASX Code: YTMTLS) returning 0.26%.

We maintained compliance with the portfolio mandate at all times during the year. As at 31 March 2017 interest rate duration was 1.28 years while credit duration is at 1.88 years. Positively, there were no negative contributors to portfolio performance over the quarter.

Quarterly Review

The first quarter of 2017 was reasonably subdued in terms of market moves. Growing geopolitical risk meant bond markets adopted a 'watch and wait' stance with a slight preference for safety after the Q416 selloff. Credit markets continued their grind tighter (margins) but began to show a marginally softer tone late in the quarter. This cautious tone was absent in the primary market where investors continue to bid aggressively into syndicated issuance and getting scaled back accordingly. As a result, trading margins across the risk spectrum are moving ever closer to their post GFC lows last seen in 2014.

Credit issuance was slightly up on the prior corresponding period (~$5.2 billion) primarily as a result of the non-financial issuance (or lack thereof in Q12016). Following the redemption of Woolworths Subordinated Notes (ASX: WOWHC) in November 2016, we re-invested part of the proceeds into Alumina 7.25% 2019 (XTB) (ASX Code: YTMAWC). In line with our expectations, S&P upgraded the credit rating on Alumina (7 April 2017) to reflect the sound performance of AWAC and the strategic alignment of Alumina and Alcoa Corp. Although this security was added only a month before quarter end we expect it to contribute meaningfully to portfolio performance in the next quarter.

From a duration perspective, we remain relatively conservative as the RBA Governor (Philip Lowe) suggests a 'Period of Stability' in domestic interest rates is the likely course. We continue to expect some volatility in the long end of the yield curve as US policies swing between success and failure on the reflation trade.

As at 31 March 2016 we are near fully-invested (Cash, 5.41%). However, ~30% of our current portfolio is expected to mature over the coming 6 months. That being said we continue to favour slightly elevated cash balances in the current environment primarily because we expect to deploy capital in opportunities as they arise.

However, we continue to reiterate our view that tight supply dynamics against the backdrop of benign economic and corporate fundamentals will result in spreads tightening across the risk spectrum. This imbalance is likely to continue into the near future without any catalyst for change.

Market Outlook

Although economic data and sentiment indicators continue to suggest a renewed expansion phase for the global economy, 2017 continues to be overshadowed by political risk.

The cyclical picture has improved, driven in part by Chinese fiscal stimulus (and associated lift in commodity prices) and expectations of Trump's delivery of both large fiscal spending and an overhaul of the tax system. Together, the valuation and cyclical factors suggest that government bonds remain vulnerable, although we are growing a little more cautious that much of the recent good cyclical news is 'in the price'.

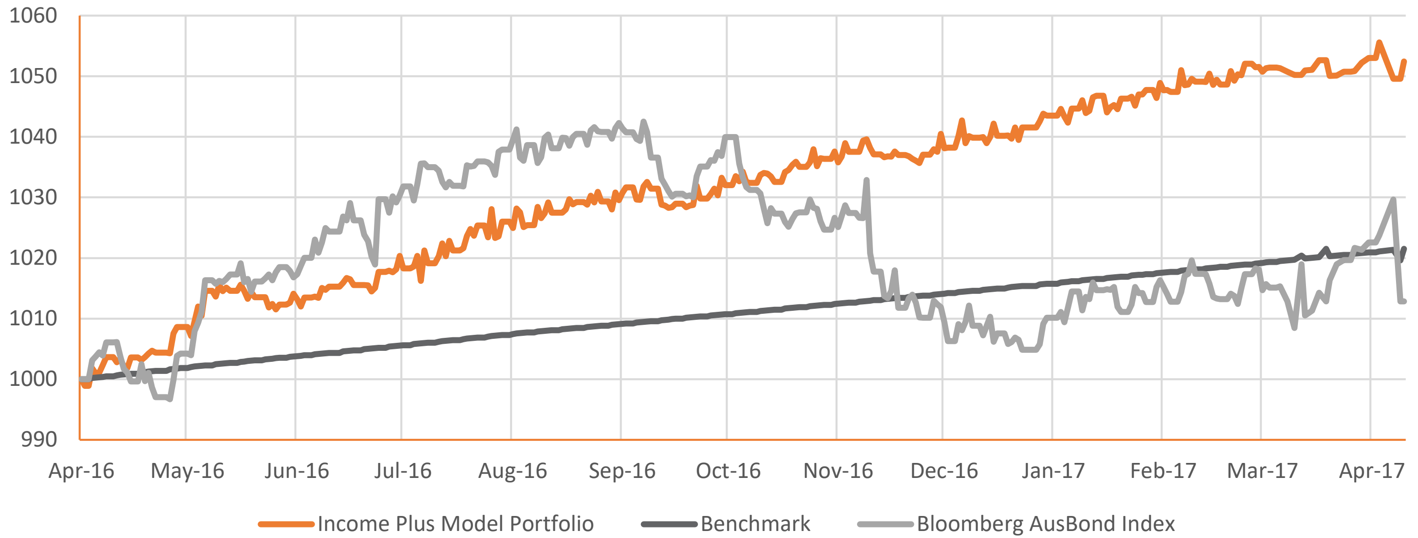
Credit continues to enjoy the benefits of a stronger technical environment, but the narrowing of spreads has taken corporate bond valuations back towards expensive territory.

Domestically, government agencies like the Australian Prudential Regulation Authority (APRA) and Australian Securities and Investments Commission (ASIC) have been implementing further oversight and prudential intervention into the overheated housing market housing market. This is made more complex as headwinds in global regulatory consensus (for banks) means APRA may have to adjust policy away from consensus.

APRA Chairman, Wayne Byres, provided a recent update: "we will be looking at many components of the capital adequacy framework, but given its position as a dominant asset on the balance sheet of the banking system, the adequacy of capital requirements for housing-related risks will be a critical part of that assessment". As we stated in January 2017 (First Half Outlook: Where to from here?) any change to capital adequacy is likely to come from changes in risk-weighted residential mortgage assets. While we expect this is probably inevitable, APRA has always been gradual and cautious in its transition phases and we don't expect it to be any different this time.

Our portfolio remains biased to higher quality exposures that have lower default risk. So whilst market pricing may move, our expectation of a deterioration in credit quality (or default) remains very low given the quality of the portfolio. Elevated cash levels combined with our interest rate and credit positioning leaves us more defensively positioned and focused on protecting capital as markets adjust to developments.

Investment Performance as at 31/03/2017



	1 mth (%)	3 mths (%)	1 yr (%)
Total Return	0.63	1.39	5.43
Benchmark	0.25	0.74	3.11
Excess Return	0.38	0.65	2.32

Portfolio inception 31 March 2016.

Past performance is not a reliable indicator of future performance

Top Five Holdings (%)

Qantas 6.50% 2020 (XTB)	12.45
Wesfarmers 4.75% Mar 2020 (XTB)	12.42
Westpac Subordinated Notes	12.27
NAB Subordinated Notes	12.24
ANZ Subordinated Notes	12.23

Maturity Profile (%)

0-1 years	48.87
1-3 years	31.95
3-5 years	13.67
5+ years	5.41

Security Profile (%)

Floating Non-Discretionary	51.4
Fixed Non-Discretionary	48.6

Capital Structure (%)

Senior Unsecured	50.30
Subordinated	7.45
Tier 2 Regulated Capital	36.74
Other (Cash)	5.41

Holdings by Risk Bucket (%)

Very Low	5.41
Low	0.00
Lower Medium	49.19
Upper Medium	30.77
High	14.53
Extreme	0.00
Default	0.00

Figure 1: Trailing Composition

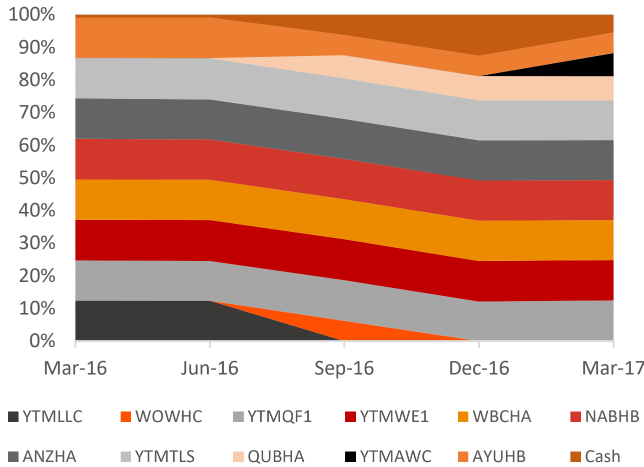


Figure 2: GICS Sector Breakdown

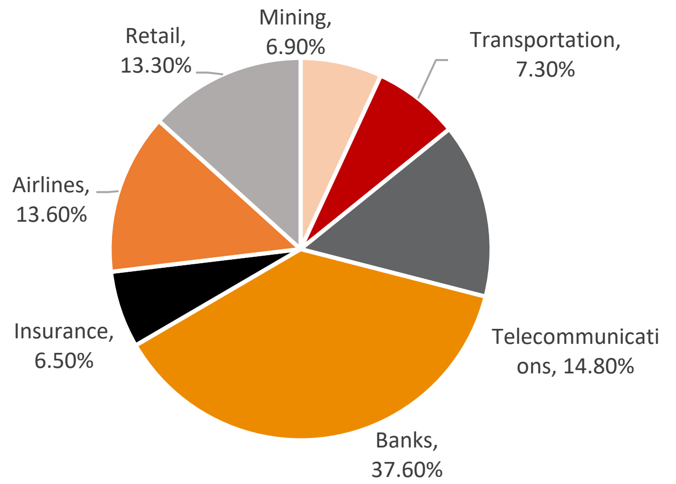


Figure 3: Performers & Detractors - Top 3 / Bottom 3 (3 Month Cumulative Return)

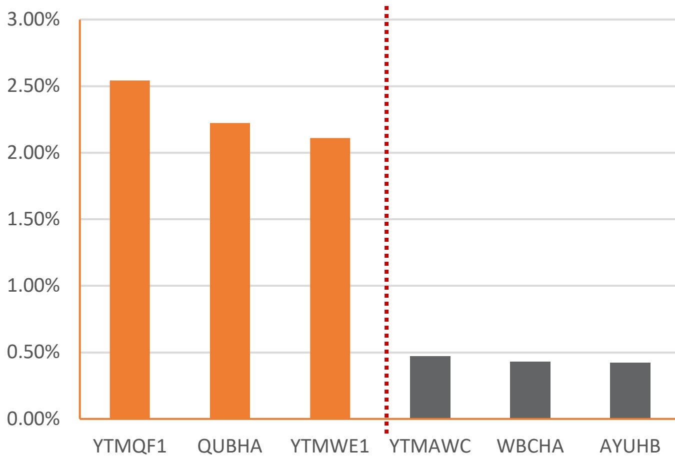


Figure 4: Attribution to Portfolio - Top 3 / Bottom 3 (3 Month Cumulative Return)

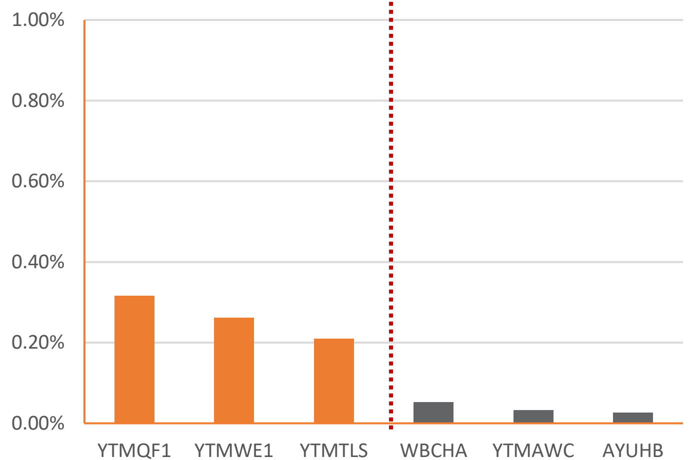
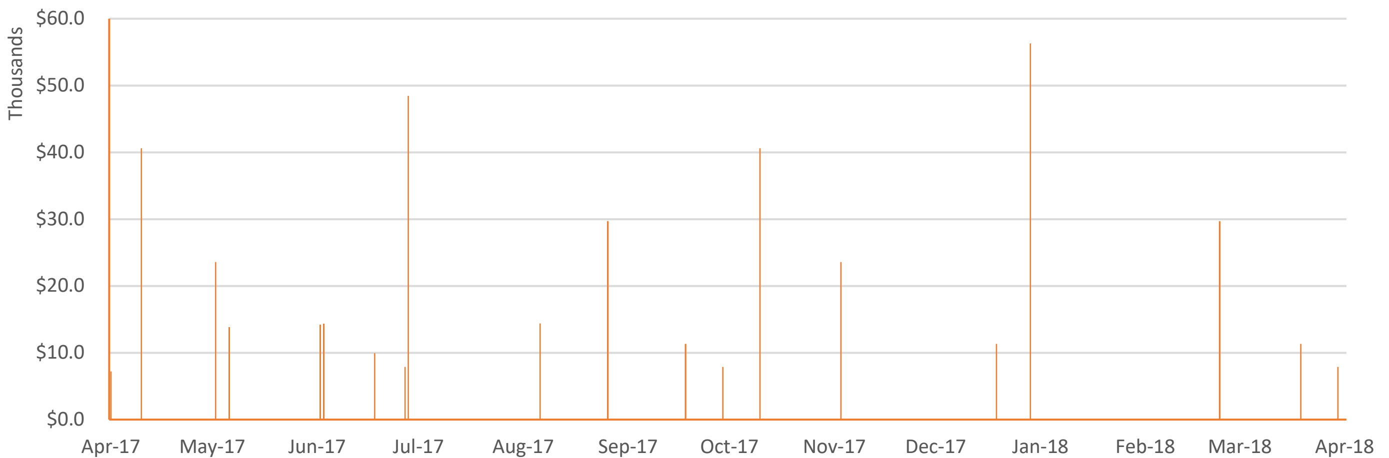


Figure 5: Expected Distribution Payment Profile (next 12 months)



Source: BondAdviser, HUB24