Security with Performance

Investment Update - January 2024

MCF - Mutual Credit Fund

Mutual Limited

All figures as at 31 January 2024

Fund Performance

	3 months %	6 months %	12 months %	3 years %	Inception % p.a.
MCF (pre-fees)	2.44	4.87	8.88	4.45	4.18
MCF (post-fees)	2.32	4.62	8.39	3.96	3.69
BBerg AusBond Bank Bill Index	1.09	2.15	4.00	1.83	1.45
Relative Performance (Net)	1.23	2.47	4.39	2.13	2.24

Investment Objective and Investment Strategy

Mutual's objective for the Mutual Credit Fund is to source and actively manage a portfolio of fixed interest credit assets across APRA regulated institutions, corporates and structured assets. Targeted portfolio construction is to hold assets with a shorter credit duration to ameliorate periods when risk assets sell-off.

Mutual manages interest rate risk by predominately investing in assets that reset their reference rate every 30 or 90 days.

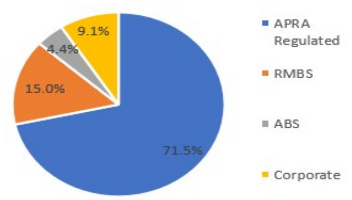
Portfolio

Liquidity
Up to 5 days

Fund Statistics

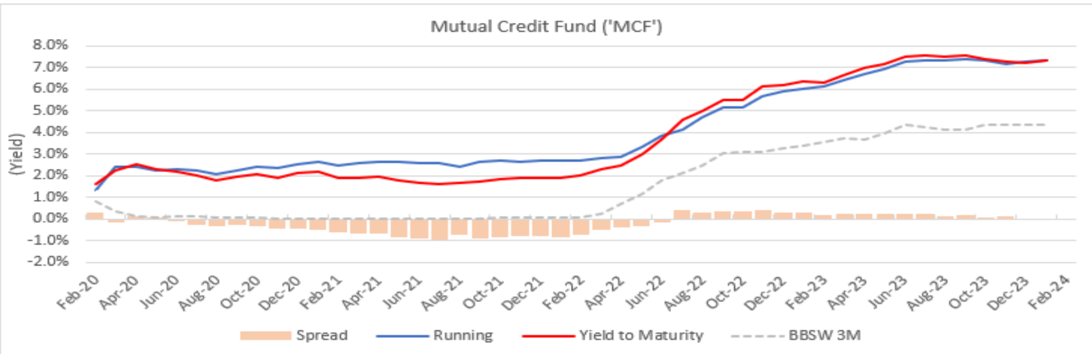
Running Yield:	7.35%
Yield to Maturity:	7.32%
Credit Duration (years):	2.42
Interest Duration (years):	0.10

Current Portfolio Diversification



Month in Review

Performance: MCF returned 0.68% (net) in January, continuing a period of above benchmark returns. The return for the past quarter was 2.32% (net) and for the past 12 months 8.39% (net). January was a busy month for issuance with two major bank senior deals and a second AUD Tier 2 deal announced at the end of the month. While the volume of issuance was well absorbed by the market, the amount issued was enough to halt the credit spread compression seen over the prior 2 months.



Overview: There was no RBA meeting in January, but we did see some meaningful changes to market pricing for future cash rates. The Q4 CPI data printed inside consensus estimates, +4.1% YoY versus +4.3% YoY expected, and well down on the Q3 print of +5.4% YoY. It has been 12-months now since inflation peaked at +7.8% YoY. While goods inflation continues to moderate, services inflation remains stubbornly high. Prior to the Q4 CPI release the market was pricing in one rate cut in 2024. The market has since shifted expectations, now pricing in two rate cuts in 2024. As at the end of January, the first cut is expected in August and the second in December. It is worth highlighting the RBA were slow to start hiking interest rates, and will be very wary of making another policy error. Their CPI forecast released in November had Q4 CPI at +4.5% YoY. The result is ahead of the forecast, but CPI remains above the top of the target 2 – 3% target band.

The global market narrative has been dominated by talk of the timing of any Fed policy pivot toward the dovish side of the spectrum, with markets pricing in an aggressive 130 – 140 bps of rate cuts this calendar year, almost double what the Fed has previously signaled in their dot-plots (75 bps). Moderating inflation measures and moderating growth have underpinned such dovish expectations. On the last day of January, the FOMC met and affirmed the expected dovish pivot, albeit with caveats. The Fed left rates on hold, as expected, and the accompanying statement was devoid of any rate hike possibilities. They also confirmed the next move in policy would be a rate cut, however the language around the timing of such cuts was cautious.

Portfolio Manager
Mutual Limited

Inception
21 February 2020

Fund Size
$642.9 million

Month End Price
$1.024622

Benchmark
Bloomberg AusBond Bank Bill Index

Distribution Frequency
Quarterly

Minimum Investment
$1 through IDPS
$20,000 for Retail & Wholesale Investors

Minimum Investment Term
Longer than 5 days (suggested)

Management Fees
0.4930% p.a. (inclusive of GST)

Buy / Sell Spread
Nil / Nil

APIR Code
PRM8256AU

ISIN
AU60PRM82564

Ratings
Zenith
Lonsec

Platforms
Asgard
BT Panorama
BT Wrap
Colonial First State
HUB24
Netwealth
Powerwrap

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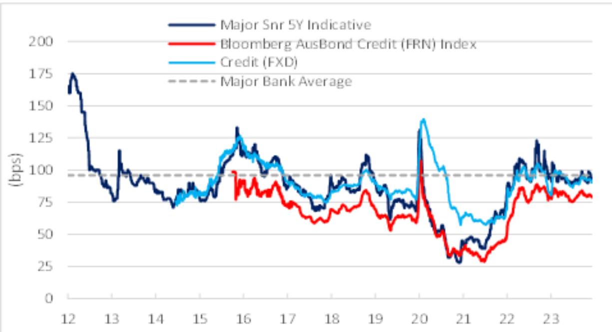
Outlook

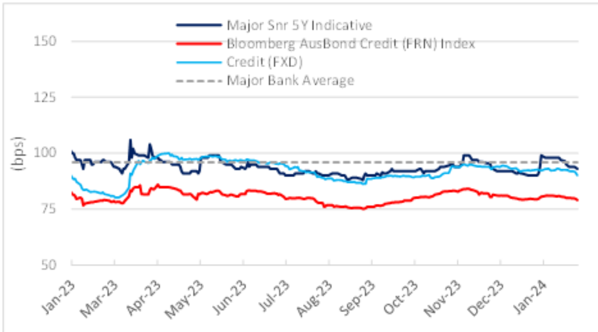
We were expecting issuance to come at the start of 2024 but were still surprised by the volume. NAB were first off the mark heading to the US for a multi tranche senior deal. This deal priced on the 3rd January and more than likely took Westpac's idea as on the 4th they announced an AUD senior deal. The mandate was announced on the Thursday, with pricing expected on the following Monday. This time between mandate and deal launch is longer than normal, giving the market plenty of time to look at the deal, no doubt a way to offset the very early timing of the first transaction for the new calendar year. ANZ followed a similar theme, announcing on Friday 5th a 10NC5 year Tier 2 transaction that would price on Tuesday. The NAB senior deal priced at +100bps, providing ANZ with an easy decision to start their Tier 2 transaction at +205bps, a fraction over the 2 times senior ratio the market likes to focus on. Final pricing landed at +195bps, a +15bps concession to where the latest CBA 33-28 was trading into the end of December. Both books were very well supported and large deal sizes ensured. Towards the end of January ANZ came back to the market for senior, pricing a 3 and 5 year FRN and FXD tranche deal at +80bps and +96bps respectively. The print size was a whopping $5bn in total, from a book of over $7.5bn.

Credit Spreads – long run history



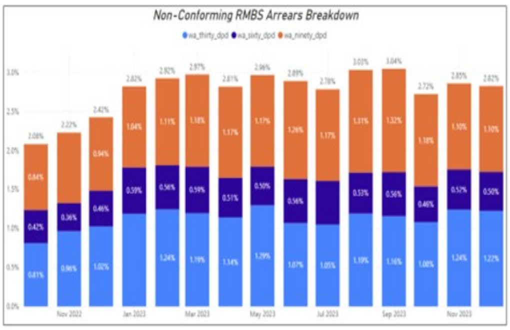
Source: Bloomberg, Mutual Limited

Credit Spreads – short run history



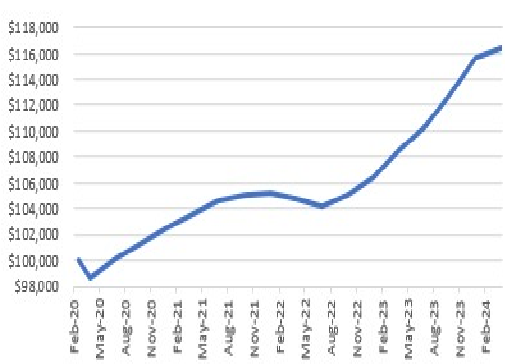
Source: Bloomberg, Mutual Limited

Normally in structured credit we look forward to a very orderly start to the calendar year with January traditionally skipped by issuers. This has been the case since 2020, but was broken this year with a funding only RMBS transaction priced by Westpac, plus transactions from Plenti and La Trobe. La Trobe did not offer notes all the way down the capital structure, as they are known to do, so we did not get a full pricing picture. For the BBB rated D notes though, it was a very strong opening to the year with pricing revised twice and eventually set at +340bps. If we go back to November last year, a Pepper prime transaction priced the same rated BBB notes at +375bps. If we look back 12 months, Resi priced a non-conforming transaction in December 2022 where the BBB D notes priced at +495bps. Despite the tight pricing level achieved by La Trobe, the book was over 7 times covered even after the transaction was upsized to A$1.25bn. This illustrates the underlying demand for RMBS assets, despite the prospect of economic headwinds building towards mid-year as higher interest rates clamp down on consumer spending.



Asset quality in the portfolio remains resilient with RMBS arrears recording a 3bps decline in non-conforming arrears to 2.82% (vs 3.65% in the broader market – S&P SPIN), well down on the cyclical peak in August of 3.03%, and well below the post GFC average for the broader market of 8.40%. Meanwhile, prime arrears rose 12bps to 0.90% for December, a new cyclical peak.

Value of $100,000 invested since inception



As is the tradition at the turn of a new calendar year, research notes abound with predictions for property prices in 2024. Unlike last year, where most forecasters got it completely wrong, the consensus looks to be for a rise of 5% in '24. Most forecasters are highlighting risk to the upside of this forecast, particularly if the RBA start cutting rates in the second half of the year. Supply will remain a key driver. There is little growth expected on the approximate 160,000 of building commencements in 2023, well below the ~240k per year needed to achieve the government's objective of 1.2m new dwellings over 5 years. The housing start numbers are not just missing this target by a small margin, they are no where near it which highlights the structural issue in housing in Australia, underpinning confidence in RMBS assets as the collateral will continue to increase in value.

Overall we remain positive on Australian credit. Despite the volume of new issuance in Australia, spreads have consolidated inside reoffer levels for both senior and Tier 2 which will underpin ongoing performance of the fund.

If you would like more information on MCF please visit www.mutualltd.com.au or contact Mutual on + 61 3 8681 1900