



# Investment Strategy Group Fixed Income

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**Prepared by the Fixed Income Team**

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**PUTTING WEALTH TO WORK FOR GENERATIONS**



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# | Fixed Income Investment Philosophy

We believe the investor is best served by following a philosophy that focuses on three main elements:



## Capital Preservation

- Preservation of capital is paramount
- An overarching strategy and disciplined selection process are followed to achieve the objective
- Credit quality is first and foremost the focus to ensure capital preservation and the receipt of scheduled coupons and return of capital at the call/maturity date



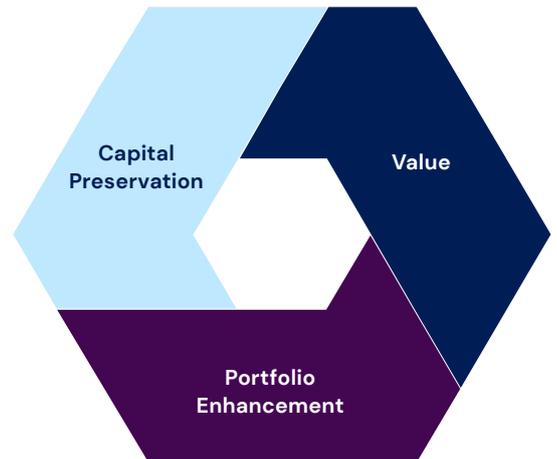
## Value

- The expected return must compensate for the risks assumed
- For a potential investment to be added to the portfolio it must adequately reward the investor for its underlying credit, market, tenor and liquidity risk
- Consistent with our objective of preserving capital our focus is on quality and an appropriate risk-adjusted return rather than the level of return



## Portfolio Enhancement

- Instruments added to portfolios must enhance the portfolio's attributes in terms of the:
  - level and quality of yield;
  - diversity;
  - liquidity; and
  - defensive qualities.
- Moreover, instruments added to portfolios should not create concentration or reinvestment risk.



“ The investment philosophy of JBWere’s fixed income team is transparent, concise, and uncomplicated. ”

## | Bespoke Solutions

Direct fixed income investments undertaken by JBWere clients are varied as the composition of our bespoke portfolios are specifically designed to match each client's individual circumstances.

JBWere provides advice, investment guidance and execution on a variety of fixed income investments.

The universe of investing options, outlined below, is not exhaustive but captures for the majority of our clients the types of direct exposures they hold. The direct investments are in many cases accompanied by exposures to other specific markets and segments through approved managed funds. We remain indifferent as to which investment avenue or avenues a client chooses to gain their exposure to fixed income so long as the level and type of exposure is appropriate for their individual circumstances and provides them with the desired holistic investment solution.

“ We remain indifferent as to which investment avenue or avenues a client chooses to gain their exposure to fixed income so long as the level and type of exposure is appropriate for their individual circumstances. ”

## | Potential Investment Universe

The domestic ASX-listed and over-the-counter (OTC) or wholesale markets are for many JBWere clients their primary source for implementing their direct fixed income portfolio. With the OTC market generally requiring minimal bond parcel sizes of \$500,000, using the OTC market will be influenced in part by the volume of money to be invested and the need for adequate diversity of exposures.

The investments included within client portfolios often include a combination of the following fixed income securities which may be fixed-, floating- or variable-rate in nature:

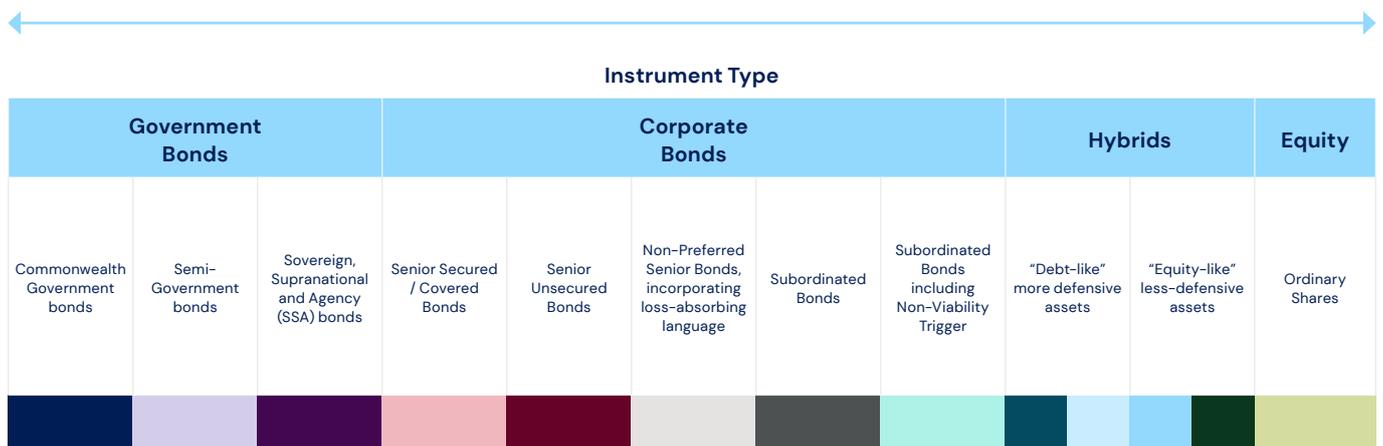
- Government Bonds – both Australian Commonwealth Government and Semi-government (state) bonds
- Senior Secured bonds – including covered bonds issued by banks and corporate bonds issued infrastructure owners such as Transurban
- Senior Unsecured Bonds – financial and corporate
- Subordinated Bonds
- Subordinated Notes (which include terms providing the issuer with the ability to defer distribution payments)
- Capital Notes
- Convertible Notes
- Convertible Preference Shares
- Income Securities
- Perpetual Securities
- Exchange Traded Funds

# Defensive Characteristics and Volatility

Not all tradeable fixed income investments are created equal in terms of their defensive characteristics.

Fixed income investments carry different levels of risk, with some more defensive than others from a credit and or instrument structure perspective. On a continuum this can be demonstrated by placing risk-free government bonds at one end and more volatile growth assets such as equities at the other. Residing on the continuum between the two bookends are a myriad of fixed income investment options that have differing defensive attributes in terms of their structure, complexity, and risk. The investment challenge is to find the right mix of instruments to enable the portfolio's objective to be met, while adhering to the investor's individual circumstances.

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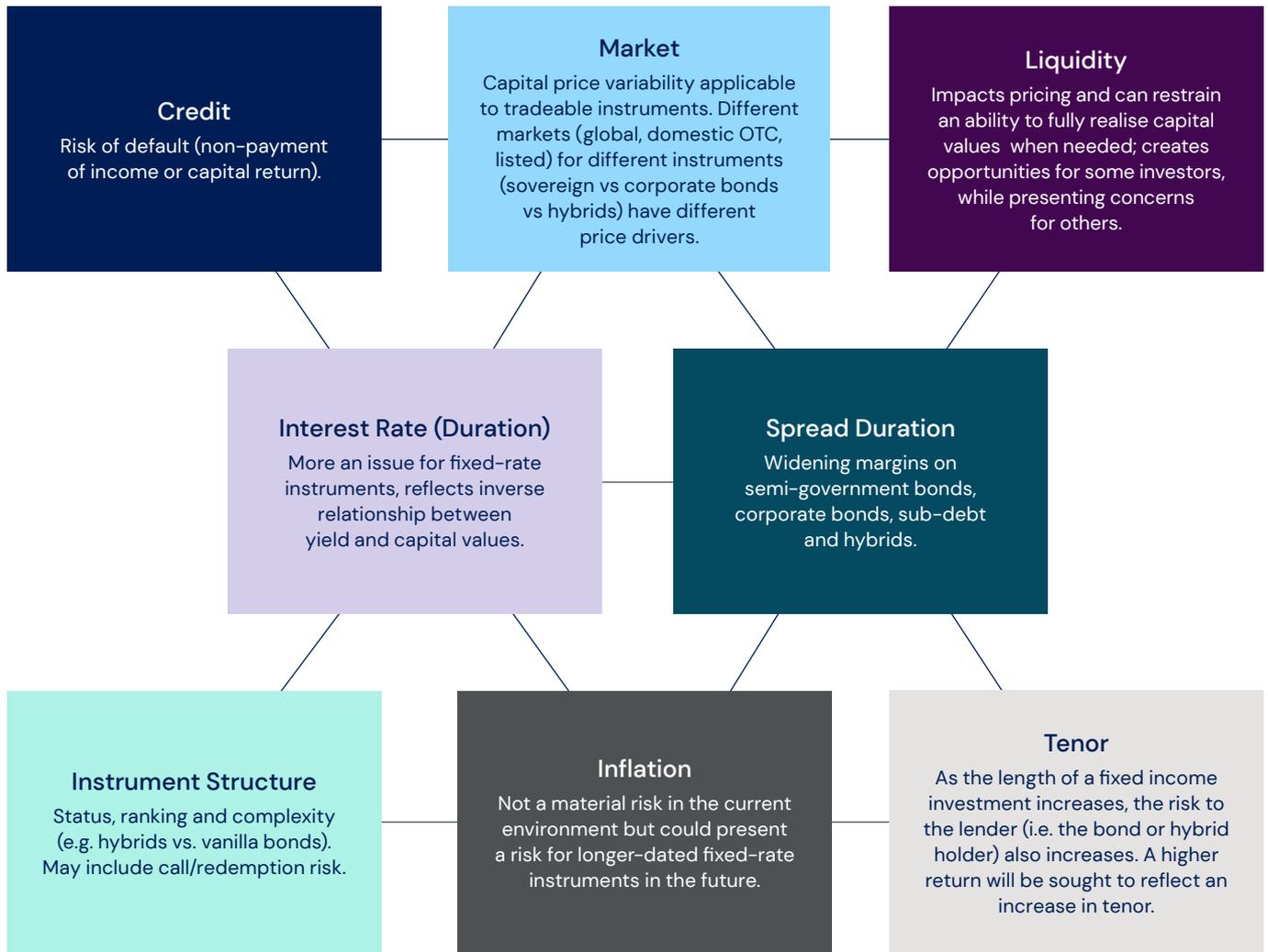


**Notes:**

\*The continuum reflects features of the instruments that point to them being more 'debt-like' and defensive in nature or more 'equity-like' and less-defensive in nature. 'Debt-like' and more defensive instruments exhibit features that point to greater capital stability (lower correlation with equity valuations), lower likelihood of cashflow interruptions (lower income uncertainty) and greater clarity of maturity and capital redemption (low extension risk). More 'debt-like' features also include cash coupons and cash redemption rather than distributions comprising franking credits and the potential for equity conversion at maturity/call date.

# Risks Inherent in Fixed Income Investing

Fixed income portfolios represent the low-risk component of an investor's asset allocation; however the varied nature of the different fixed income instruments means they each carry different types and levels of risk. In a bid to ensure stability and preservation of capital JBWere constructs portfolios in a manner to mitigate many of the inherent risks embedded in individual instruments. These risks can include:



# Fixed Income Investment Process

## Selection Criteria

In the process of selecting suitable direct investments to add to fixed income portfolios, JBWere's fixed income team follows a well-established criteria and disciplined approach incorporating both fundamental and technical factors. In addition, the team applies an Environmental, Social, and Governance overlay to its decision making.

### The criteria include, but is not limited to:

the issuer's credit quality

the instrument's structure (defensive or 'equity-like' in nature, complex or simple)

liquidity of the instrument – taking into consideration size, daily turnover, and secondary market support

the composition and level of expected return as measured by the instrument's trading margin and whether it adequately compensates the investor for the risk assumed

visibility of maturity or value-triggering event

appropriate portfolio positioning

how an instrument compares to secondary market peers in terms of price, credit quality, tenor and liquidity

current and expected market dynamics

the impact an addition will have on the portfolio – for example will it enhance or detract from the portfolio's defensive attributes and or be a risk mitigant

## Portfolio Positioning

The composition of a fixed income portfolio must reflect the investor's individual circumstances. To ensure the client's bespoke portfolio is fit for purpose the following circumstances are considered:

- investment objective
- risk tolerance
- investment horizon
- cash flow and capital needs
- yield expectations
- wider asset allocation position

## Ensuring Portfolios are Fit For Purpose

To assist, we assess fixed income instruments to determine their suitability for three general categories of investors, subject to price, with the investor's profile playing a key role in determining the portfolio's attributes.

### Investor profile determines:

- Type and level of instrument exposure
- Weighting to individual instruments
- Maturity profile
- Credit quality, rating limits
- Composition of returns

**Risk averse / conservative portfolios:**  
generally shorter-dated, higher quality, low hybrid exposure, liquid and low yielding

**Balanced portfolios:**  
medium-term investment horizon, exposures across most asset types, investment-grade focus

**Yield enhancing portfolios:**  
longer-dated exposures, higher hybrid weightings, less liquid, potential sub-investment grade exposure

# Risk Management

Mitigating risk within portfolios is embedded through:

- targeting better quality issues from a credit perspective;
- targeting more liquid instruments;
- ensuring diversity of issues, issuers, sectors, market exposure (listed and wholesale), fixed and floating rate, and instrument type;
- well-laddered maturity profile to reduce reinvestment risk;
- appropriate weightings by asset type and across individual exposures; and
- transparency of exposure, open architecture execution and third-party pricing.

# Ongoing Management

Risk management post portfolio construction carries through to implementation and portfolio management.

JBWere's Fixed Income team assists in the ongoing management of fixed income portfolios through active monitoring of markets and issuers. Recommendations are made to add instruments to portfolios when better relative value opportunities present in primary and secondary markets or in the event of redemptions, while recommendations are also made to remove issues from portfolios where there has been a change in value and or change in credit quality such that the investor is no longer being compensated for the risk assumed. Furthermore, changes in the form of a portfolio's composition and or weighting in the wider asset allocation will also be recommended should JBWere's tactical view change as a result of changes in the economic environment and or investment markets more generally.

# Fixed Income Team

Name	Role	Responsibilities	Years in Industry	Years in Team (JBWere)
Laurie Conheady	Head of Fixed Income	Fixed Income strategy, investment research and recommendations on all fixed income investments, run model and discretionary fixed income portfolios, as well as providing asset allocation and portfolio construction advice.	23	11
Nick Pryor, CFA	Senior Analyst, Fixed Income	Investment research and recommendations on all fixed income investments, contribute to the running of model and discretionary fixed income portfolios, as well as providing asset allocation and portfolio construction advice.	6	5

# Fixed Income Model Portfolios

Portfolio	Investment Objective	Investment Strategy	Purpose
<b>Hybrid</b>	<p>Within an investable universe of ASX-listed hybrid instruments, the manager's investment objective is to construct a relatively defensive portfolio that:</p> <ul style="list-style-type: none"> <li>• preserves capital and exhibits a relatively low level of capital and earnings volatility;</li> <li>• adequately rewards the investor for the credit, market, tenor and liquidity risks assumed;</li> <li>• provides a steady and secure income stream;</li> <li>• offers a solid absolute return that represents a premium to rates earned on term deposits; and</li> <li>• is liquid enough to ensure sufficient investing flexibility.</li> </ul> <p>The Portfolio is an absolute-return focused, benchmark unaware portfolio.</p>	<p>The manager's investment style is to focus on ensuring investors receive an adequate (risk-adjusted) level of distributions, with trading undertaken when material relative-value opportunities arise or in response to credit events. Turnover is; however, expected to be low.</p> <p>While management of the Portfolio is consistent with a "hold to maturity" approach, the portfolio manager retains the flexibility to make changes when and where appropriate. Developments that may warrant a portfolio change include:</p> <ul style="list-style-type: none"> <li>• changes in JBWere's tactical view;</li> <li>• positive or adverse changes in the credit quality of individual issuers or instruments;</li> <li>• redemptions and new issuance; and</li> <li>• compelling relative value opportunities.</li> </ul>	<p>The JBWere Hybrid Model Portfolio aims to provide clients with access to an actively managed hybrid exposure that serves to complement their more traditional fixed income exposures.</p> <p>The Portfolio is designed for clients looking for enhanced returns over that realised on traditional fixed income instruments through regular cash and franked income and realisation of capital appreciation.</p>
<b>Listed Fixed Income</b>	<p>Within an investable universe of ASX-listed fixed income instruments, the manager's investment objective is to construct a relatively defensive portfolio that:</p> <ul style="list-style-type: none"> <li>• preserve capital and exhibits a relatively low level of capital and earnings volatility;</li> <li>• adequately rewards the investor for the credit, market and liquidity risks assumed;</li> <li>• provides a steady and secure income stream;</li> <li>• offers a solid absolute return that represents a premium to rates earned on term deposits; and</li> <li>• is liquid enough to ensure sufficient investing flexibility.</li> </ul> <p>The investment objective of the Portfolio is to outperform the RBA Cash Rate by 250bps p.a. before fees.</p>	<p>The manager's investment style is to focus on ensuring investors receive an adequate (risk-adjusted) level of distributions, with trading undertaken when material relative-value opportunities arise or in response to credit events. Turnover is; however, expected to be low.</p> <p>While management of the Portfolio is consistent with a "hold to maturity" approach, the portfolio manager retains the flexibility to make changes when and where appropriate. Developments that may warrant a portfolio change include:</p> <ul style="list-style-type: none"> <li>• changes in JBWere's tactical view;</li> <li>• positive or adverse changes in the credit quality of individual issuers or instruments;</li> <li>• redemptions and new issuance; and</li> <li>• compelling relative value opportunities</li> </ul>	<p>The JBWere Listed Fixed Income Model Portfolio aims to provide clients with a well-researched and transparent and relatively conservative listed fixed income exposure.</p> <p>More specifically, the Portfolio is designed for clients seeking a capital protection-focused investment providing a higher and/or steady and secure return above that earned on lower-yielding fixed income options such as term deposits or more volatile investments such as equities.</p> <p>The Portfolio should represent a subset of an investor's diversified fixed income portfolio as hybrids represent among the least defensive instruments in the Australian fixed income market.</p>

# About JBWere Investment Strategy Group

Our Investment Strategy Group (ISG) is a team of highly experienced investment strategists and analysts; the driving-force behind our investment recommendations and asset allocation strategies. The ISG group undertakes in-house research across a diversified suite of asset classes, including international and domestic equities, international and domestic fixed income, and alternative investments. Supporting the team's research is a wide range of views including those from our domestic and global research partners and other well-respected external industry research bodies.

Drawing on these insights, the ISG provides the intellectual property, insights and tools for JBWere's Advisory Team to manage clients' portfolios including:

- The economic outlook;
- Analysis of global investment trends, opportunities, challenges and investment markets;
- Strategic asset allocation and the identification of tactical portfolio tilts;
- Direct model portfolio and advice; and
- In-depth managed strategies research.

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