DAINTREE HIGH INCOME TRUST (NZD)

QUARTERLY FACTSHEET: 30 June 2019

Awards & Credentials

Daintree Capital is proud to have been nominated as a Finalist for the Money Management Fund Manager of the Year Award in the Emerging Manager category for 2019. We are also a signatory to the United Nations Principles for Responsible Investment.

Fund Description

The Daintree High Income Trust NZD (the Fund) is an absolute return bond strategy. The Fund is not constrained by any traditional fixed income index, which provides us the flexibility to seek out the best risk adjusted returns available across regions, sectors and securities.

Fund Objective

The aim of the Fund is to provide a steady stream of income over the medium term by investing in a diversified portfolio of fixed income securities. The Fund seeks to produce a return (net of fees) that exceeds the RBNZ Cash Rate by 3%-4% p.a. over a rolling three to five-year period.

Quarterly Highlights

- Expectations of easier central bank policy saw a strong interest rate rally dominate the quarter
- Credit markets globally also performed well, with higher beta credit well-supported
- Fund performance was underpinned by income generation and long duration positioning. Credit spreads also narrowed, supporting performance

Key Statistics

Modified Duration (Yrs)	1.53
Spread Duration (Yrs)	3.50
Portfolio Yield (%)	4.67
Average Credit Quality	BBB+

Note: Portfolio yield is the expected return over the next year, assuming no changes to either portfolio composition or market yields.

Fund facts

Trust name	Daintree High Income Trust (NZD)
Responsible Entity	Perennial Investment Management Ltd
Portfolio managers	Mark Mitchell & Justin Tyler
Inception date	1 November 2018
APIR code	WPC0529AU
Management costs	0.75% pa
Buy/sell spread	+0.15% / -0.15%
Entry and exit fees	None
Pricing frequency	Daily
Initial investment	$10,000
Distribution frequency	Monthly
Currency	New Zealand Dollar

Platforms

The Daintree High Income Trust NZD is available on the following platforms:

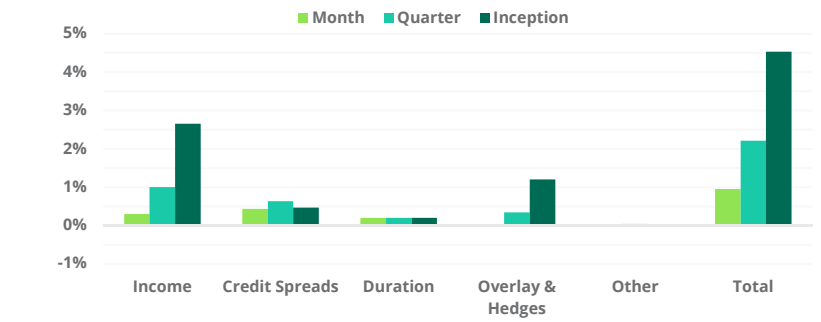
- FNZ
- FINZO
- Aegis

Performance & Analytics

	Month (%)	Quarter (%)	Inception (%)
Fund (gross)	0.95	2.21	4.53
Fund (net)	0.89	2.02	4.03
Distribution (net)	0.20	0.59	1.85
Growth (net)	0.69	1.43	2.18
RBNZ Cash Rate	0.13	0.43	1.00
Excess Return	+0.75	+1.59	+3.02

Note: Performance inception is 1 November 2018. Excess return is measured with reference to net performance. Returns for periods longer than one year are annualised. Distribution return is the monthly cents per unit distribution divided by the net asset value unit price at the start of the month. Past performance is not a reliable indicator of future performance.

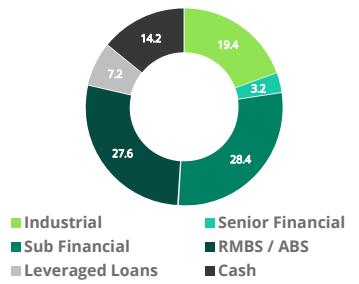
Performance Contribution (Pre Fees)



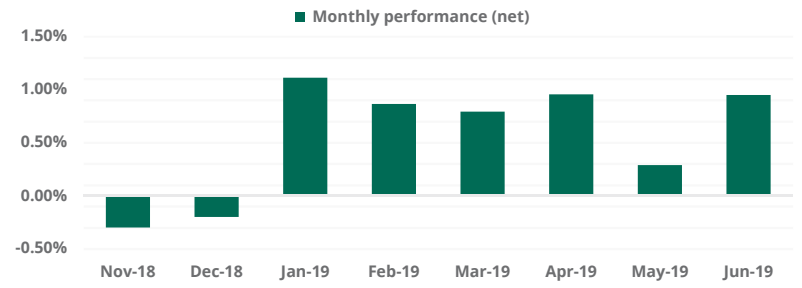
Note: Overlay strategies use derivatives to ensure that the fund exposure to interest rates, credit and other relevant factors is controlled separately to the physical assets in the portfolio

Rating Exposure (%)

Sector Exposure (%)

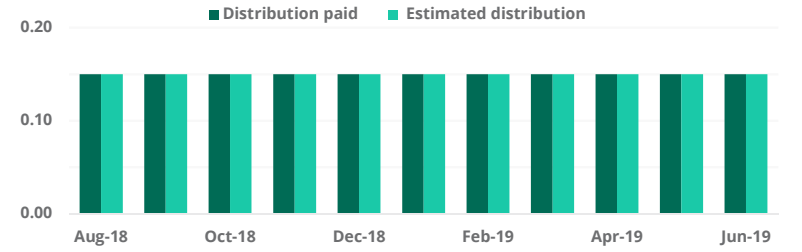


Monthly Performance



Cash Income

The Fund distributed 0.20 cents per unit in June, in line with our estimate.



Daintree CAPITAL

DAINTREE CORE INCOME TRUST (NZD)

QUARTERLY FACTSHEET: 30 June 2019

Fund Review

The Daintree High Income Trust NZD (the Fund) posted a net return of 202 basis points for the quarter. Performance was driven by income generation, along with long duration positioning as global central banks moved into easing mode. In particular the RBA and RBNZ have both now reduced their cash rates to record lows. We participated in the accompanying re-pricing of Australian 3-year bond yields to record low, sub-1% levels.

This global central bank easing once again drove both risky and defensive assets alike during the quarter in fact it was difficult to find a poorly performing asset class. In this environment we once again saw the unusual combination of good performance in both government and corporate bonds. Credit spreads ended the quarter tighter, and locally this was led by shorter-dated financials in the latter part of the quarter. As usual, Australian credit spreads were much less volatile through the quarter than their offshore counterparts.

The performance of credit this quarter came despite persistent worries around global trade, slower global growth, geopolitical risks and the broader uncertainty that all of these have created in the real economy. Any of these factors alone may have been expected to push investors into government bonds at the exclusion of other asset classes, but omnipotent central bankers have once again ensured this is not the case. Central banks (particularly in Europe) may, however, be forced once again to push the bounds of unconventional policy. At the same time, we worry that although each successive foray boosts financial assets, it also further reduces the future potency of monetary policy and increases the importance of fiscal efforts (possibly multilateral) in offsetting the next downturn when it happens. Thus, we will not be reaching for yield in our portfolios to boost returns. Our risk management approach will ensure investors continue to receive a stable return in excess of cash that retains defensive characteristics against a backdrop where those characteristics may come into focus quite suddenly.

Outlook

Events of recent weeks have set up the second half of 2019 to be a challenging period for investors, which may sound counter-intuitive as local credit spreads tighten to the lowest levels of the year and equity markets reach multi-year highs. The situation is more complicated because the rally has been induced by a distinct dovish tilt that has included: reductions in the cash rate locally (with further cuts priced in), the Fed "dot-plot" indicating significant chance of downward movement in the Fed Funds rate, and weak inflation data in Europe prompting expectations of renewed QE in the Eurozone.

Falling interest rates have contributed to an easing in financial conditions and will support the near-term growth profile, but on the other hand, economic data has been broadly undershooting expectations for some time. The RBA has downgraded growth and inflation forecasts for 2019 and 2020, despite a labour market that continues to perform well – just not well enough. RBA Governor Phil Lowe has clearly stated that rate cuts are one of the catalysts to kick-start wage inflation, but that other measures are likely required to reduce the unemployment rate toward the downwardly revised NAIRU estimate of 4.5%.
We feel this is achievable, but it will require buy-in from the government, however for now there is little appetite for major fiscal policy support (apart from tax cuts) to buttress monetary policy initiatives. In New Zealand, the budget is expected to be in surplus, albeit small, in the coming years and the fiscal impulse will be positive, but not large in magnitude. So, we have antipodean governments displaying behaviour that is globally not unusual – fiscal rectitude. What is unusual is the healthy budget position of both countries which, along with record low sovereign borrowing costs, demands a more expansionary fiscal stance that removes some of the onus for economic stimulus from the central bank. We expect to see RBA Governor Phil Lowe in particular continuing to talk about the necessity for fiscal stimulus and hope that both the Australian and New Zealand governments heed this call.

While the "hard" data has been telling a reasonably consistent story for some time, the near-term outlook has become more subdued due to deterioration in key "soft" data points such as business and consumer confidence. The New Zealand Institute of Economic Research Survey of Business Opinion shows business confidence at the lowest level since the GFC. This supports the case for further easing from the RBNZ. In Australia, the Westpac Leading Index growth rate has been consistently negative over the last six months, a clear signal that economic growth is likely to remain below trend through the rest of 2019. Compound this with the propensity of mortgage holders to keep repayments stable even as rates fall, suggesting that one of the transmission channels of monetary policy will not be as effective as in the past. All in all, domestic factors in both Australia and New Zealand are likely to keep growth subdued.

The global economic outlook has softened considerably in recent months, with a diverse range of indicators suggesting trade disruption to be the primary culprit. The Baltic Dry Index has fallen sharply as demand for shipping capacity remains weak, while semiconductor shipments from Korea have also been soft. The price of oil, often seen as a barometer of economic health, has fallen dramatically in recent months even as tensions rise in the Persian Gulf and the Strait of Hormuz, through which one third of the world's seaborne oil transits. However, China and the United States have agreed to another trade truce, allowing discussions to restart. Market participants will keep a laser focus on any developments, but at the time of writing there remains several major points still to negotiate. We believe that markets continue to price in some type of eventual trade deal, with much more scope for downside should they hit further roadblocks, or the path to a deal begins to disappear into the distance.

Elsewhere, the economic data coming from the Eurozone in particular inspires little confidence in its ability to keep inflation anywhere near target, let alone consider rising interest rates. This reality has contributed to approximately US$13tn worth of bonds trading with a negative yield, predominantly in the Eurozone and Japan. Furthermore, there is the very real possibility that the ECB could restart QE this year, a scenario we believe few investors are positioned for. Thus, we think that European credit, and investment grade in particular, may turn out to be one of the better performing sub-sectors over the next six months.

Against this backdrop, we remain constructive on credit spreads for a number of reasons. Easy financial conditions will allow the already elongated cycle to be further extended. While there are pockets of high leverage in some sectors, corporate issuers' net borrowings have been easily absorbed by investors. Markets are suggesting that interest rates globally could remain at record low levels for the next 2-3 years, alleviating some of the concerns around a growing refinancing pipeline. The clamorous search for yield will also be supportive of credit spreads. Following the recent cut to the Australian cash rate in June, several banks reduced deposit rates on savings products by the full 25 basis points while only reducing mortgage rates by 17-18 basis points. As the returns on cash fall, more and more savers will be forced to supplement their income by taking more risk, including increased exposure to fixed income and credit.