

# Yarra Australian Bond Fund

## Net returns as at 31 December 2024

	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception % p.a.
Yarra Australian Bond Fund <sup>^</sup>	0.64	-0.19	3.41	-0.47	0.05	2.12	4.75
Growth return <sup>#</sup>	-0.46	-1.27	0.50	-1.91	-1.83	-1.20	-0.16
Distribution return <sup>#</sup>	1.10	1.09	2.91	1.44	1.88	3.33	4.92
Bloomberg AusBond Composite 0+YR Index	0.51	-0.26	2.93	-0.79	-0.18	1.97	4.67
Excess return <sup>#</sup>	0.13	0.08	0.48	0.32	0.24	0.15	0.08

**Past performance is not a reliable indicator of future performance. Taxes payable by investors have not been taken into account.** The figures shown have been provided for illustrative purposes – they are unaudited and subject to change. The total returns shown are prepared on an exit to exit basis – they include all ongoing fees and expenses and assume reinvestment of all distributions.

<sup>#</sup>Growth returns are measured by the movement in the Fund's unit price, ex-distribution. Distribution return is the proportion of the total return which is paid to unitholders by way of distribution. It does not include distribution amounts deemed as capital distributions. Excess return is the difference between the Fund's net return and its benchmark (Bloomberg AusBond Composite 0+YR Index).

<sup>^</sup>Effective August 2021, the Fund was renamed from the Nikko AM Australian Bond Fund to the Yarra Australian Bond Fund. There was no change to the Fund's investment team, philosophy or process.

\*Inception date: July 2000.

### Portfolio review

After fees and expenses, the Fund returned 0.64% to outperform the benchmark by 13 basis points (bps). This brings the Fund's 2024 calendar year-to-date return to 3.41%, outperforming the Index return of 2.93% by 48 bps.

The Fund started the month with an overweight duration position of 0.77 years and ended the month at 0.69 years. Bond yields were mixed over the month, and the yield curve ended the month steeper, as concerns over inflation risks in the United States continued. The Reserve Bank of Australia (RBA) held key policy rates at 4.35%, as widely expected; however, there was a clear shift in tone in the central bank's rhetoric, opening up the possibility of a rate cut in 2025 if data continue to trend in the right direction. On the other hand, the November labour data continued to show strength, with an increase in jobs and a fall in participation, causing the unemployment rate to drop to 3.9%. Our expectation is that the RBA will begin to cut interest rates in early 2025, based on slow economic growth and inflation trending towards the RBA's target band.

The Fund continues to be positioned to benefit from a steeper yield curve (widening gap between the 3-year bond yield and the 10-year bond yield), and this was a key contributor to performance this month as the curve steepened. It remains our view that once the RBA begins its rate cut cycle, the curve will further steepen.

Sector positioning favours an overweight to spread, primarily in senior financials, residential mortgage-backed securities, and high-grade corporates with maturities out to 5 years. We believe the trend of semi-government spread widening has peaked, prompting a reallocation into the sector. We remain overweight longer-dated semi-government bonds with

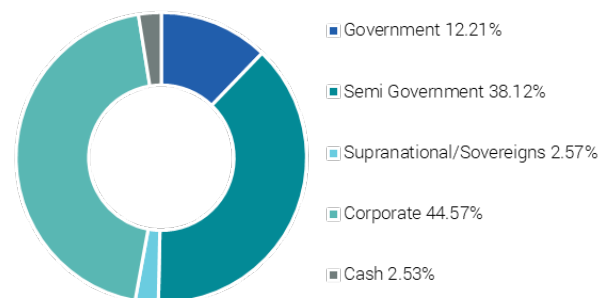
maturities between 12 and 15 years; however, some weakness in those maturities was a slight detractor to performance over the month.

### Fund Overview

Characteristics	Fund	Benchmark	Difference
Modified Duration (yrs)	5.59	4.91	0.69
Corporate Spread Duration (yrs)	1.14	0.31	0.83
Total Spread Duration (yrs)	4.49	2.39	2.10
Yield to Maturity (%)	4.90	4.37	0.53
Average Coupon (%)	3.88	2.93	0.96
Weighted-average Credit Rating <sup>#</sup>	A+	AA	-

<sup>#</sup>Standard & Poor's

### Portfolio Asset Allocation



### Risk Characteristics

3 Year Volatility (p.a.)	6.75%
3 Year Tracking Error (p.a.)	0.81%

## Market Commentary

The Australian bond market, as measured by the Bloomberg AusBond Composite 0+ Yr Index, posted a return of 0.51% in December. At the start of the month, the market's primary focus was on the US, with ongoing concerns about inflation under the Trump administration. The Federal Open Market Committee (FOMC) disclosed in its latest dot plot that Federal Reserve members now anticipate fewer rate cuts in 2025 and 2026.

The bond yield curve steepened by 11 basis points (bps), widening the spread to 54 bps. The yield on 3-year government bonds dropped by 9 bps to 3.82%, while the 10-year bond yield rose by 2 bps to 4.36%. Short-term bank bill rates ended the month lower, with 3-month rates falling by 1 basis point to 4.42%, and 6-month rates dropping by 17 basis points to 4.49%. Meanwhile, the Australian dollar continued to depreciate against the US dollar, closing the month at USD 0.62, as the market reassessed the potential scale of rate cuts by the Fed and the timing of potential rate easing domestically.

The Reserve Bank of Australia (RBA) kept its cash rate at 4.35% during its final meeting of 2024, marking the ninth consecutive meeting without any change to borrowing costs, the decision was in line with market expectations. The central bank noted that while headline inflation has significantly eased and is expected to remain low for some time, underlying inflation remains too high, with a target of reaching the 2-3% range by 2026. The board expressed increased confidence that inflation is gradually moving towards the target. Recent data on economic activity has been mixed but aligns with forecasts. Regarding household consumption, any recovery may be slower than anticipated, resulting in continued modest output growth and a sharper decline in the labour market. The RBA emphasised that its decisions would continue to be guided by incoming data and the evolving risks, including geopolitical uncertainties.

Domestic data released throughout December continues to point to a resilient Australian economy. Australia's seasonally adjusted unemployment rate fell to 3.9% in November 2024, down from 4.1% in the previous three months, and well below market expectations of 4.2%. This marked the lowest unemployment rate since March. Gross Domestic Product (GDP) increased by 0.3% in the September quarter. Government spending and public capital investment were the primary contributors to this expansion. Although marking the twelfth consecutive quarter of growth, Australians are facing a per capita recession, with six consecutive quarters of decline in real GDP per capita. Over the year, Australia's economy grew by 0.8%, falling short of the expected 1.1% expansion, this was the slowest rate since the December quarter of 2020, which was impacted by COVID-19. Retail sales in Australia rose by 0.60% in October 2024, which was ahead of market expectations.

The household saving to income ratio rose to 3.2% in September, with gross disposable income growing faster than consumption, though it is still well below historical averages. The latest data does suggest households saved rather than

spent the Stage 3 tax cuts introduced in July 2024.

CoreLogic's Home Value Index (HVI) ended the year on a negative note, with values falling by -0.1% nationally in December, following a peak in October and flat growth in November. This marks the conclusion of a surprisingly strong and resilient growth period from February 2023 to October 2024, despite high interest rates, cost of living pressures, and reduced borrowing capacity.

## Top 10 Issuers

Security	Rating
Queensland Treasury Corporation	AA+
Commonwealth Government Bonds	AAA
New South Wales Treasury Corporation	AA+
South Australian Govt Financial Authority	AA+
Treasury Corporation of Victoria	AA
New York Life Global Funding	AA+
Paccar Financial	A+
Suncorp	AA-
Westpac Bank	AA-
Athene Global Funding	A+

All of the above portfolio securities are Australian dollar denominated issues and include fixed interest and FRNs.

## Market Outlook

The RBA remains dedicated to restoring price stability by bringing inflation back within its 2-3% target range. While inflation has decreased substantially since its peak in 2022, with higher interest rates effectively bringing aggregate demand and supply closer to balance, underlying inflation measures are still around 3.5%. This is some distance from the 2.5% midpoint of the inflation target. Their most recent forecast anticipates underlying inflation returning to the midpoint of the target range by 2026. Recent economic data, such as weak GDP numbers and consumers depleting their pandemic savings, indicate clear signs of economic slowdown. This has prompted a shift in tone from the RBA, with the Statement on Monetary Policy moving away from the "not ruling anything in or out" stance and becoming more open to reducing rates if the data continues to trend in the right direction.

The volatility in recent data, including an unexpectedly low unemployment figure in November, has led to fluctuations in market expectations regarding the timing and scale of rate cuts. Additionally, the impact of a weakening Australian dollar is another factor to consider. In our view, while the data indicates a weakening consumer and inflation moving in the right direction, we remain cautious of potential upside risks.

In contrast to Australia's ongoing struggle with inflation, several developed economies have successfully brought inflation under control and started easing their monetary policy. The European Central Bank, Bank of Canada, Bank of

England, and US Federal Reserve have all reduced interest rates.

The prospect of a Trump-led Republican administration is generally seen as a positive for the US economy, especially with potential pro-business policies that could stimulate growth. However, concerns have emerged around the potential inflationary impact of these policies, particularly the raising of tariffs, particularly those targeting China. Such a move could escalate tensions and potentially lead to a trade war between the world's two largest economies. The repercussions of such a scenario could be far-reaching, with global markets, including Australia, likely to feel the impact. A trade war could disrupt supply chains, increase costs, and create uncertainty that would affect not only trade relations but broader economic stability worldwide. Ongoing instability in the Middle East along with the ongoing war between Ukraine and Russia, could still significantly influence the trajectory of cash and bond yields as we close out the year.

China, Australia's largest trading partner, has introduced new stimulus measures to revive its struggling property sector and address weak domestic demand. Despite repeated announcements of stimulus measures in the second half of 2024, Chinese leader Xi Jinping continues to project optimism, but the economy remains sluggish. When these policies fall short, the stock market declines, and Xi tries again. In his keynote speech during the Central Economic Work Conference held in mid-December, Xi claimed that "the economy is stable and making progress," with the key 2025 policy goal being to "boost consumption" through "moderately loose monetary policy" and "more active fiscal policy."

While the headline amount of the fiscal stimulus package is expected to be significant, investors should closely monitor how the funds will be allocated, as it may not prove as stimulative as anticipated. A large portion of the funds is likely to be directed toward restructuring local government debt. These local governments are burdened with substantial debts due to heavy investments in areas ranging from infrastructure to education but lack the necessary revenue streams to support these expenditures.

## Fund Objective

The Fund aims to outperform the Bloomberg AusBond Composite 0+YR Index over any three-year rolling period, before fees, expenses and taxes.

Key Facts	
<b>Responsible Entity</b> Yarra Funds Management Limited	<b>Management Cost</b> 0.30% p.a.
<b>APIR Code</b> TYN0104AU	<b>Buy/Sell Spread</b> +0.05% / -0.05%
<b>Portfolio Manager</b> Darren Langer	<b>Distribution Frequency</b> Quarterly
<b>Fund Size</b> A\$387 mn as at 31 December 2024	<b>Benchmark</b> Bloomberg AusBond Composite 0+YR Index
<b>Minimum Investment</b> A\$10,000	

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