Yarra Australian Bond Fund

Net returns as at 28 February 2025

	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^	1.01	1.78	4.67	0.70	-0.34	2.05	4.77
Growth return#	1.01	0.67	1.73	-0.76	-2.21	-1.28	-0.12
Distribution return#	0.00	1.11	2.94	1.46	1.87	3.32	4.88
Bloomberg AusBond Composite 0+YR Index	0.93	1.63	4.18	0.32	-0.59	1.89	4.68
Excess return#	0.08	0.15	0.49	0.38	0.26	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.

#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).

^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 1.01% to outperform the benchmark by 8 basis points (bps).

The Fund began the month with an overweight duration position of 0.67 years and ended the month at 0.71 years, which contributed to performance. Government bond yields were volatile due to ongoing news about US tariff policies and global concerns. 3-year government bond yields fell by 8 basis points from 3.82% to 3.74%, while 10-year government bond yields dropped by 14 basis points from 4.43% to 4.29%. As a result, the yield curve flattened.

The global focus continues to be on the US's interactions with other nations, especially regarding trade and security policies. Tariffs on Canada, Mexico, and China are expected to proceed, with all three countries likely to retaliate. This is likely to create ripple effects across the US economy, including inflationary pressures and a steeper yield curve, which would increase borrowing costs in the US. Consumer confidence in the US continues to decline, with the most recent survey showing a drop to 98.3 (down from 105.3 previously), as inflation expectations rise due to tariff policies. While the US unemployment rate has dropped to 4%, the full impact of the Department of Government Efficiency (DOGE) actions has yet to be reflected in the data.

Locally, the Reserve Bank of Australia (RBA) made its first interest rate cut since 2020 but expressed caution regarding the risks of rising inflation, suggesting that the battle is not over yet. The consumer price index (CPI) has remained within the target range of 2%-3%, with the headline annual inflation rate at 2.4% for Q4 2024. The RBA's preferred measure Trimmed Mean CPI was slightly higher at 3.2%. The Australian labour market remains strong, with the unemployment rate sitting at 4.1% at the end of January. Given these conditions, the RBA is likely to remain cautious when considering any further rate cuts.

The Fund continues to be positioned to benefit from a steepening yield curve (a widening gap between the 3-year and 10-year bond yields). However, this was a detractor to performance this month as the curve flattened. We still believe the curve will steepen further as the RBA continues to normalise interest rates from the current restrictive levels.

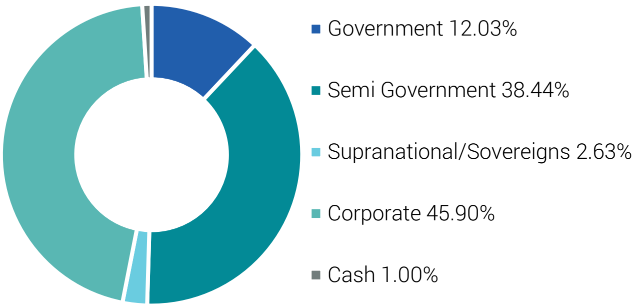
In terms of sector positioning, we favour an overweight exposure to spread products, primarily in senior financials, residential mortgage-backed securities, and high-grade corporates with maturities up to five years. The semi-government sector recovered this month as dip-buyers took advantage of the previous month's sell-off. Our overweight allocation to the semi-government sector was therefore a contributor to performance this month as spreads contracted. We will look to take advantage of market movements and gradually reduce our overweight position to near benchmark levels.

Fund Overview

Characteristics	Fund	Benchmark	Difference
Modified Duration (yrs)	5.54	4.82	0.71
Corporate Spread Duration (yrs)	1.10	0.30	0.79
Total Spread Duration (yrs)	3.99	2.38	1.60
Yield to Maturity (%)	4.77	4.27	0.50
Average Coupon (%)	3.83	2.94	0.89
Weighted-average Credit Rating#	A+	AA	-

#Standard & Poor's

Portfolio Asset Allocation



Risk Characteristics

3 Year Volatility (p.a.)	6.70%
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 0.93% in February. Australian government bond yields declined amidst considerable global volatility triggered by US tariff talks. The 3-year bond yield fell by 8 basis points to 3.74%, while the 10-year bond yield dropped 14 basis points to 4.29%. This led to a flattening of the bond yield curve by 6 basis points, narrowing the spread to 55 basis points. Short-term bank bill rates followed a similar trend, with 3-month rates decreasing by 13 basis points to 4.12%, and 6-month rates dropping 10 basis points to 4.21%. The Australian dollar remained stable against the US dollar, closing the month at USD 0.62.

The Reserve Bank of Australia (RBA) cut its cash rate by 25 basis points to 4.1% during its February meeting, in line with market expectations. This marked the first rate reduction since November 2020, driven by a continued slowdown in underlying inflation. The central bank expressed growing confidence that inflation is steadily moving towards the midpoint of its 2-3% target range, citing the impact of higher interest rates in balancing aggregate demand and supply. However, the RBA also pointed out an uncertain economic outlook, highlighting a slower-than-expected recovery in private demand and doubts about the sustainability of the household spending recovery that began in late 2024.

Global risks remain significant, driven by geopolitical tensions and policy uncertainties, particularly due to the unpredictability of the new US administration. While aligning with the global easing trend ahead of the federal election and with rates still within the restrictive range, the RBA board has expressed caution regarding further policy cuts.

Domestic data released throughout February indicates a resilient Australian economy. The Australian economy expanded by 0.6% quarter-on-quarter in the fourth quarter of 2024, up from a 0.3% increase in the third quarter. This marked the 13th consecutive period of quarterly growth and the fastest pace since the fourth quarter of 2022. On an annual basis, GDP grew by 1.3% in 2024. Australia's seasonally adjusted unemployment rate rose to 4.1% in January 2025, up from 4.0% in December, in line with market expectations. Retail sales in Australia rose by 0.3% month-on-month in January 2025, reversing the 0.1% decline recorded in the previous month and in line with market expectations.

Expectations of lower interest rates appear to be translating into improved buyer sentiment, with CoreLogic's national Home Value Index recording a 0.3% increase in February, reversing the brief three-month downturn that had pushed the national measure of home values down by 0.4%. The February rise, though modest, was widespread, with every capital city, except for Darwin (-0.1%) and Regional Victoria (flat), posting a monthly increase in values.

Top 10 Issuers

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

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 significantly decreased since its peak in 2022, higher interest rates have helped to bring aggregate demand and supply closer to balance.

However, part of the recent decline is expected to be temporary, with inflation likely to rise again as cost-of-living relief unwinds. The RBA's latest forecast predicts underlying inflation will return to the target midpoint by 2026. The RBA's preferred inflation measure, Trimmed Mean CPI, rose 3.2% year on year in Q4 2024, encouragingly the slowest increase in three years, but still above the central bank's 2-3% target.

Recent economic data, including moderate GDP growth and consumers depleting their pandemic savings, points to a slowing economy. As a result, the RBA eased rates by 25 basis points at its most recent meeting in February, in line with market expectations, but rates remain at very restrictive levels. The RBA was quick to point out that, given the ongoing global volatility and their belief that the fight against inflation is not yet over, further rate cuts are not guaranteed. They are likely to adopt a cautious approach regarding any future rate cuts.

Recent mixed data readings seem to have subsided, with most indicators now signalling a gradual slowdown in the economy, suggesting the RBA is making good progress towards its desired soft landing. Market expectations now point to further rate cuts in the short to medium term, although these may be shallower than previously anticipated. While the data suggests a resilient consumer and inflation moving in the right direction, we remain cautious about potential upside risks.

In contrast to Australia's prolonged battle with reducing inflation, several developed economies have successfully brought inflation under control and begun easing their monetary policies. The European Central Bank, Bank of Canada, Bank of England, and the US Federal Reserve have all lowered interest rates. Like the RBA, these central banks are now facing uncertainty around the effects of any trade war escalations and the potential repercussions on their domestic economies.

A Trump-led Republican government was largely seen as positive for the US economy, thanks to pro-business policies that could drive growth. However, concerns have since emerged over the potential inflationary impact and its impact on economic growth, particularly due to tariff increases targeting key trading partners like China, Mexico, and Canada. This has heightened tensions and could risk a trade war between the world's two largest economies, with global markets, including Australia, likely to feel the impact. Such a scenario could disrupt supply chains, increase costs, and destabilise the global economy.

Ongoing instability in the Middle East and the Russia-Ukraine conflict could also affect cash and bond yields. Since taking office on January 20, President Trump has signed a record number of executive orders, reshaping US priorities both at home and abroad. These unprecedented moves aim to dismantle existing policies and institutions, paving the way for his MAGA agenda while appealing to his populist base.

China, Australia's largest trading partner, will need to manage not only potential flare-ups in the trade war with the US but also its own domestic economic issues. The country has set a 2025 GDP growth target of around 5% and announced a broader fiscal stimulus package to tackle economic challenges, including the ongoing trade tensions with the US. The government has raised its budget deficit target to 4% of GDP, the highest level since 2010, and plans to issue 1.3 trillion yuan in special treasury bonds to drive growth. Inflation expectations have been reduced to 2%, the lowest in more than 20 years, reflecting weak domestic demand.

To address economic stagnation, China aims to boost domestic consumption, ease local government debt, and stabilise the real estate market. The government also acknowledged the impact of rising US tariffs and stressed the importance of dialogue with the US amid deteriorating trade relations. Despite these measures, analysts are concerned that the 5% growth target may be overly optimistic given weak consumer spending and ongoing economic challenges.

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	
Responsible Entity Yarra Funds Management Limited	**Management Cost** 0.30% p.a.
APIR Code TYN0104AU	**Buy/Sell Spread** +0.05% / -0.05%
Portfolio Manager Darren Langer	**Distribution Frequency** Quarterly
Fund Size A$401 mn as at 28 February 2025	**Benchmark** Bloomberg AusBond Composite 0+YR Index
Minimum Investment A$10,000	

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