Fund Update as at 31 March 2018
CC JCB Active Bond Fund (APIR: CHN0005AU)

Fund Benefits

Active Management:
JCB is a specialist fixed income manager with significant global investment management experience and expertise.

Access:
The Fund provides access to investment knowledge, markets, opportunities and risk management systems that individual investors may not be able to obtain on their own.

Diversification:
When bonds are held as part of a broader portfolio of different asset classes, diversification may assist in managing market volatility. Bond securities in general are considered a defensive asset class.

Income:
The income generated by bond securities is consistent and regular (usually semi-annual).

Fund Facts

Investment Manager	JamiesonCooteBonds Pty Ltd or JCB
Portfolio Manager	Charles Jamieson
Structure	AAA or AA rated bond securities issued in Australian dollars
Inception Date^	3 August 2016
Benchmark	Bloomberg AusBond Treasury (0+Yr) Index
Management Fee#	Base Fee of 0.45% p.a.
Administration Fee#	Administration Fee of 0.10% p.a.
Buy / Sell Spread	0.10% / 0.10%
Distributions	Semi-annual
Fund Size+	AUD $150 million

Fund Performance

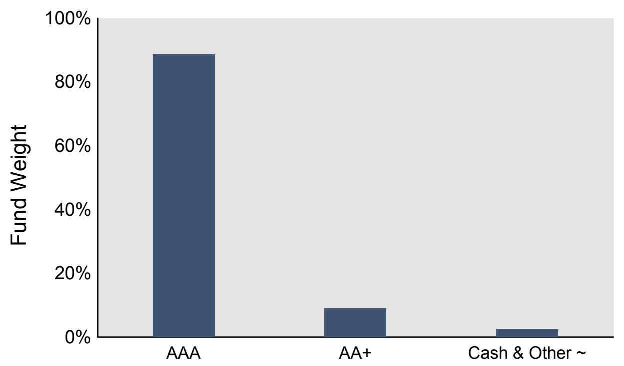
Returns	Fund*	Benchmark**	Active
1 Month	0.92%	1.19%	-0.28%
3 Months	0.82%	1.02%	-0.20%
FYTD	2.29%	2.21%	0.08%
1 Year	2.95%	3.31%	-0.36%
2 Years p.a.	-	-	-
3 Years p.a.	-	-	-
Inception p.a.	1.19%	0.45%	0.74%

Fund Overview

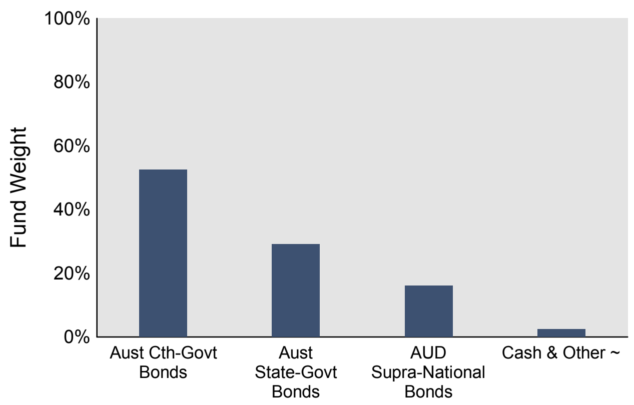
Characteristics***	Fund	Benchmark**
Modified Duration (yrs)	5.63	6.15
Yield to Maturity (%)	2.52	2.41
Weighted Ave. Credit Rating	AAA	AAA
Cash Weighting (%)	2.37	n/a

*** Refer to Definition of Terms.
Source: JamiesonCooteBonds Pty Ltd.

Credit Rating Allocation



Sector Allocation



Platform Availabilty

Asgard	BT Panorama	BT Wrap
HUB24	Macquarie Wrap	Mason Stevens
Netwealth	PowerWrap	

Further Information

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All figures disclosed include the net effect of GST and RITC. ^ Inception Date for performance calculation purposes. + Fund size refers to the CC JCB Active Bond Fund ARSN 610 435 302. * Performance is for the CC JCB Active Bond Fund (APIR: CHN0005AU), also referred to as Class A units, and is based on month end unit prices before tax in Australian Dollars. Net performance is calculated after management fees and operating costs, excluding taxation. This is historical performance data. It should be noted the value of an investment can rise and fall and past performance is not indicative of future performance. ** Benchmark refers to the Bloomberg AusBond Treasury 0+ Yr Index. ~ Cash & Other includes cash at bank, outstanding settlements and futures margin accounts.

Recommended Lonsec Research

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Market Review & Outlook

(1) Riding out the market storm and finding true 'defend and protect' assets;
(2) U.S. monetary policy now into 'restrictive' territory. Buckle up as U.S. Fed Chair Powell looks set to hold the course;
(3) Credit becomes a major concern for institutional clients as funding rates explode higher;
(4) Global data velocity remains sharply negative;
(5) Australian mortgage rates rise in further 'out of cycle' rate rises.

(1) RIDING OUT THE STORM OF GLOBAL MONETARY TIGHTENING

With the first quarter behind us, investment markets, policy, and in particular human investment behaviour are changing rapidly. The U.S. Federal Reserve (the Fed) has lifted interest rates once again (i.e. lifting the global cost of capital) in the first of three expected hikes of 2018, taking policy from accommodative to restrictive in nature. A restrictive monetary policy has immense implication for all asset classes as the global cost of capital rises. What JCB has learned from previous cycles is that moving into restrictive policy settings is generally an inflection point of the rate rising cycle where asset owners start to worry about what's over the next economic hill. With U.S. policy looking as though it will be additionally restrictive going forward and funding rates rising quickly, liquidity can be drained from the financial system which has not ended well in previous cycles.

(2) U.S. MONETARY POLICY NOW INTO 'RESTRICTIVE' TERRITORY AND CORPORATE CREDIT FEELING THE STRESS

After completing its sixth rate hike of this cycle, the Fed policy has now entered 'restrictive' territory with the upper bound rate of 1.75% being above that of the Fed preferred inflation measure, being the core PCE inflation rate (current reading for February year on year is at 1.60%).

Monetary policy has a significant lag (some 18 months) to fully work through into the real economy. In setting monetary policy, the Fed is trying to estimate where future inflation might be, adjust policy to reflect that prediction, whilst knowing that today's actions have a significant lagged effect. This is more of an art than science and has been historically prone to error over time. The markets' expectations remain for additional hiking over the year, which could further drain liquidity from the financial system and tighten financial conditions via higher funding costs.

Whilst the Fed has been following a steady program to lift interest rates, LIBOR rates have shot markedly higher due to Trump's tax package (LIBOR is the rate at which banks lend to each other and are often viewed as a financial stress indicator – with higher interbank lending rates being reflective of market stress). Three month LIBOR rates are now above 2.30%, having risen from a low of 0.23% in 2014. This higher LIBOR rate drives interest rates on more than $350 trillion of debt and derivatives contracts higher at a time when half of the investment-grade corporate bond market in the U.S. is at the weakest possible investment grade rating of BBB. Low credit quality along with significantly higher funding costs is a toxic mix.

(3) CREDIT BECOMES A MAJOR CONCERN FOR INSTITUTIONAL ASSET OWNERS AS FUNDING RATES EXPLODE HIGHER

Bond markets are often over analysed and needlessly over complicated. Essentially there are three major components to a bond market:

i) Duration – When you get your money back
ii) Volatility – How you get your money back
iii) Credit quality – If you get your money back

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Higher funding rates (led by the Fed and LIBOR increases) have given investors concern with regard to the quality or the 'if' component of credit. Despite a healthy rally over the month of March in Government Bond yields, many corporate credit bonds failed to participate at all, with some actually losing value as a re-adjustment of their perceived credit quality was re-priced into such securities.

JCB wrote about the asymmetry of credit in previous months, however, we have been surprised by the speed at which such moves are playing out. In speaking with many institutional asset owners over the last quarter, such re-pricing of credit risk has been a major concern after a decade of accommodative monetary policy. This has given rise to some complacency in credit risk allocations and we understand many institutional investors are now re-assessing that allocation.

Earlier this year credit compensation (credit spreads) hit pre-GFC levels, leaving little room for error moving forward. The quality of many credit contracts in international markets has weakened significantly, with record numbers of covenant lite bond issuance securities coming to market. With weak covenance common place, little historical compensation and now restrictive monetary policy – it is no wonder this shoe is now dropping at this stage of the cycle.

(4) GLOBAL DATA VELOCITY REMAINS SHARPLY NEGATIVE

Global data remained broadly healthy over March, however the velocity of the data continues to decay with G10 economic data surprises now turning negative. The data has declined from a reading as high as +60 in late 2017. Markets are adjusting to the trend in data, not the absolute reading themselves. Whilst some of this decay is seasonal, the sharp rise in funding rates and LIBOR over early 2018 is no doubt having an effect in the real economy. The GFC was the result of lifting the funding burden on the world's biggest ever debt bubble (in the U.S. by 4.25% during 2004 to 2006). In response to the bust of the GFC, the world essentially doubled down on that already record debt burden. Much of this newly minted debt was effected at an essentially zero (and in some instances negative) interest rate policy, which was very cheap to fund at that time.

Fast forward to now, and we are told by Central Bankers that we can raise rates by approximately 3% in the U.S. on 2x the outstanding debt burdens but employment, growth and inflation will remain essentially unchanged. JCB believes that is a highly improbable outcome. Higher funding costs do bite, it is just a matter of when and by how much, and at that point the 'if' in bond markets becomes incredibly crucial.

(5) AUSTRALIAN MORTGAGE RATES RISE IN 'OUT OF CYCLE' RATE RISES, FURTHER DELAYING ANY RBA MOVE

As we have seen previously, additional U.S. rate hikes are flowing through into Australian mortgage rates via 'out of cycle' hikes for domestic borrowers, with the majority of mortgage rates trending higher. Westpac lifted mortgage rates by up to 0.40% for both owner occupiers and investors, and Suncorp Bank announced rate hikes on all its variable rate home loans.

JCB continues to believe that this additional rate pressure is likely to persist as the Fed continues to raise rates, leaving the RBA with little to do over the coming year as the economy experiences a mild tightening of conditions. Such mortgage rate rises (combined with additional funding pressure between banks) is effectively more than a complete 0.25% rate hike for the economy, which continues to experience little inflation velocity and maintains excess capacity in the labour market.

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Fund Review

For the March quarter, the CC JCB Active Bond Fund (the Fund) returned 0.82%, underperforming the Bloomberg AusBond Treasury (0+Yr) Index by 0.20%.

The Fund delivered strong absolute performance in March, returning +0.92% in a month when many asset classes suffered decay. Our lower beta positioning caused a mild drag versus the index into the rally. However, JCB remain on course to deliver the Fund's objective through the investment cycle. The Fund retains an overweight position in the front end of the Australian yield curve where we feel the risk/reward is most compelling over time. A powerful curve flattening also caused some drag versus the index in March. JCB would look to increase the size of this position into additional flattening, should this opportunity present itself.

JCB has been surprised at the speed at which funding costs have risen domestically and such moves have generated increased volatility to all spread based products. It isn't entirely logical for Australian funding rates to follow that of the U.S. LIBOR moves, so we feel some of the pressure is related to the end of quarter balance sheet 'window dressing' by domestic banks. This requires significant attention and monitoring moving forward. Our spread-based position remains allocated at the very short end of Semi Government and Supranational curves leading to much lower portfolio risk in keeping with our investment process.

Definition of Terms:

Modified Duration - is a systematic risk or volatility measure for bonds. It measures the bond portfolio's sensitivity to changes in interest rates.
Yield to Maturity - is the total return anticipated on the portfolio if the bond holdings were held until their maturity.
Weighted Average Credit Rating - is a measure of credit risk. It refers to the weighted average of all the bond credit ratings in a bond portfolio.

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