seed FUNDS MANAGEMENT

Fund Dashboard

30 November 2024

6.56%
% Yield to Call
(Portfolio as bought)

6.07%
% Yield to Call
(Portfolio if bought today)

6.24%
Running Yield

4.6 Years
Weighted Average Term to Call

94%
Portfolio Floating Rate

0.54 Years
Interest Rate Duration^

33%
Top 5 Holdings As % of Fund*

42
Number of Holdings*

$293 million
Current FUM

Source: Seed Funds Management. As at 30 November 2024.

*Excluding cash.
^Maximum duration of 1.

Hybrid Income Fund Strategy Net Performance

30 November 2024

FIGURE 1.

	1 Month	3 Months	6 Months	1 Year	3 Years Annualised	5 Years Annualised	SI (Sep 15) Annualised
HYBRID INCOME FUND STRATEGY	**0.41%**	**2.15%**	**4.08%**	**8.52%**	**6.16%**	**5.25%**	**6.42%**
Hybrid Benchmark (Solactive*)	0.04%	1.78%	3.87%	6.88%	4.47%	3.97%	4.86%
RBA Cash Rate	0.36%	1.09%	2.19%	4.44%	3.09%	1.94%	1.76%

Figures to 30 November 2024. The performance table above represents The Hybrid Income Fund Strategy ("Strategy"). The Strategy commenced in September 2015 and has been continuously operated with identical investment parameters and processes by its portfolio manager, Nicholas Chaplin. The Strategy began in 2015 as the Paraclete Investment Fund until June 2022. The Hybrid Income Fund commenced in June 2022 operating under Evolution Trustees Limited as trustee. Investment management services were novated to Seed Funds Management Pty Ltd in March 2024. Accordingly, Seed Funds Management Pty Ltd receives a management fee for managing the Fund. Performance figures for the Strategy have been reviewed in accordance with ASRS 4400 "Agreed-Upon Procedures Engagements" by Hall Chadwick Corporate (NSW) Limited.

Monthly Commentary

November saw significant profit-taking activity in the listed hybrid market, accompanied by above-average volatility in this sub-asset class. Investors are carefully weighing the potential impact of APRA's proposed phase-out of bank Tier 1 capital instruments (bank hybrids), set to commence in 2027. Despite this uncertainty, some investors are opting to cash out of the tightly-trading hybrids to realise gains.

The Australian economy continues to demonstrate resilience, with the national unemployment rate holding steady at 4.1% in October—marking three consecutive months at this level. Business sentiment has reached its highest point in nearly two years, driven by robust sales and easing input cost pressures. Inflation appears to be under control, with the latest monthly outcome of 2.1% in October providing a stronger footing for the Reserve Bank of Australia (RBA). However, a growing portion of the market believes that any central bank rate cuts may need to wait until at least May 2025, by which time two consecutive quarters of CPI results within the RBA's target range may be achieved.

In a speech delivered in November, APRA Chairman John Lonsdale noted that the regulator intends to update the market on its proposal to phase out Additional Tier 1 bank hybrids before the end of December. Investors should watch for any mention of delays in APRA's timeline, as this could lead to short-term weakness in listed bank hybrid prices.

Key Portfolio Moves in November

The primary bond market was highly active in November, providing a significant advantage for our portfolio compared to the Hybrid benchmark index, which was limited to secondary market performance due to the absence of new hybrid issuances.

We participated in four key primary issues during the month: subordinated insurance bonds from QBE and Hollard Insurance, a subordinated bond from CBA, and a senior note issued by AMP Bank. These investments performed strongly after settlement, with issue prices of $100 rising to $103, $101.79, $100.82, and $100.83, respectively, by the end of the month. Additionally, we acquired the fixed-rate tranche of the QBE issue, which also delivered impressive gains, closing at $102.93.

The rapid price appreciation of these primary issues allowed our portfolio to outperform the index decisively. This was achieved while maintaining a better credit rating and a lower risk profile compared to the benchmark.

*Solactive Australian Hybrid Securities Index (Net)

We observed notable profit-taking in the listed hybrid market, as trading margins reached some of the tightest levels recorded for Basel-3 instruments.

Similarly, Tier 2 subordinated bonds saw a moderation in their recent strength, with some selling pressure emerging at higher price levels this month.

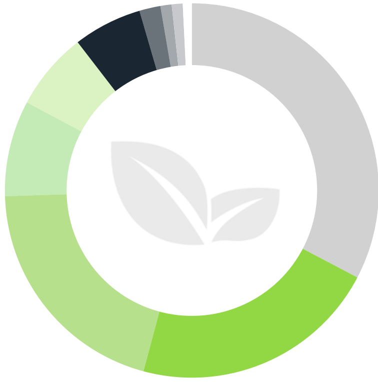
In response, we were comfortable realising gains in the secondary market, reducing positions in both listed hybrids and wholesale subordinated bonds. However, later in the month, we capitalised on oversold opportunities in the hybrid market, selectively increasing our positions in certain lines.

To enhance our Tier 2 subordinated bond holdings, we financed these purchases by trimming our exposure to senior bonds that had performed well. As a result, Tier 2 bonds now account for 54% of our portfolio.

Portfolio Holdings

(as at 30 November 2024)

FIGURE 2.



APRA To Update Market On Bank Hybrids Before Year End

On 22 November, APRA Chairman John Lonsdale announced in a public statement that the regulator would provide an update on its proposal to phase out bank hybrids by the end of the year.

There has naturally been criticism and debate about APRA's potential actions following months of consultation with the market. If APRA phases out bank hybrids and does not replace them with an appropriate alternative, it risks weakening the Australian banking industry for depositors, bondholders, and shareholders. APRA’s mandate is to regulate Australian banks to protect depositors, and such an action could directly conflict with this purpose. Global ratings agency Standard & Poor’s has already stated that if APRA proceeds with this plan, it could result in a downgrade in the credit ratings of subordinated notes issued by Australian banks. Given this criticism, what course of action should APRA pursue?

If the aim remains to phase out bank hybrids, APRA should focus on incentivising the issuance of Upper Tier 2 (UT2) capital bonds. These are long-dated but callable subordinated bonds, which have all-cash coupons that must be paid. Similar to current issues of Tier 2 subordinated notes, UT2 bonds are issued in the wholesale market and do not include any franking credits.

UT2 is subordinated to the current Tier 2 issues, commonly referred to as Lower Tier 2. With longer tenors and natural subordination, UT2 would likely be issued at margins similar to current hybrid margins. This structure would provide a viable replacement capital security, avoiding retail issuance and franking credits, while delivering robust capital support for the issuing banks and their depositors. Including UT2 in the capital structure would prevent Australian banks from being disadvantaged by the loss of hybrid capital, offering an alternative that aligns with the expectations of the Australian government and its prudential regulator.

We trust that APRA is carefully considering the potential impact of this proposal on the strength of Australian banks. Introducing the UT2 alternative could provide an effective way to meet regulatory objectives while ensuring the financial stability of banks and safeguarding the interests of depositors.

Trump Bump

Donald Trump’s recent victory in the US presidential election has driven strong gains across global markets, as his incoming administration is anticipated to benefit equity markets, the US economy, and the US dollar. Trump will officially assume office on 21 January. In the meantime, it will be crucial to monitor geopolitical developments, particularly how the new administration addresses issues related to Ukraine and the Middle East. The potential for market disruptions stemming from geopolitical tensions remains elevated.

The Seed Funds Management team extends warm wishes for a very Merry Christmas and a Happy New Year to all our investors. We hope 2025 brings health, happiness, and prosperity to everyone.

seed
FUNDS MANAGEMENT

Expert Management

The HIF provides access to highly skilled specialist management, with extensive expertise in regulated capital products including hybrids, subordinated debt and mutual equity.

Senior Portfolio Manager

Nicholas Chaplin is an authority in the Hybrid and capital issuance market having structured, originated, distributed, and educated on many issues since 1998.

Over his career he has originated over $200 billion in hybrid & capital issues. From 2009 to 2021, Nick was Head of Hybrid & Structured Capital at NAB and prior to that he was Head of Hybrid Origination at Westpac.

Portfolio Manager
Chair, Investment Committee

John Corr has worked in the finance industry for 40 years and is a highly regarded authority in portfolio risk management. He has experience in banking, broking, proprietary trading and funds management.

John was a founder and CIO of Aurora Funds Management.

Unit Pricing:	Daily
Applications:	Daily
Distributions:	Monthly
APIR Code:	EVO3184AU
Management Fee:	0.55% per annum
Performance Fee:	Not Applicable
Website:	Click here
Offer Document:	Click here
How to Apply:	Click here
Contact Details:	Click here

Fund Information

The Hybrid Income Fund strategy was established in September 2015.

Hybrid Income Fund (HIF) actively invests in a diversified portfolio of financial capital with a heavy weighting to Australian-regulated capital instruments. The underlying securities include hybrids (Tier 1 capital notes and convertible preference shares), Tier 2 bonds, subordinated debt, senior debt, mutual capital instruments and cash. The Fund typically holds ~40 positions whose underlying issuers are banks, insurance companies and non-bank lenders.

Fund Objective

HIF aims to provide returns that exceed the Hybrid Benchmark on a net basis over the suggested investment timeframe (five+ years). The Fund has a meaningful track record of exceeding its target after fees through active management with low volatility and access to franking credits.

Our Product Universe

The universe for the Hybrid Income Fund portfolio includes prudential capital instruments issued by Banks, Insurers, and non-bank financial corporations as well as other instruments from these issuers such as senior bonds. Prudential capital includes hybrids and subordinated bonds (sometimes referred to as Tier 1 and Tier 2 securities respectively). Senior bonds add significant additional liquidity to the portfolio as well as adding important product diversity.

The Investment Strategy

The investment manager intends to apply a tactical approach in terms of which securities it invests in and the timing of such investments with a focus on delivering a robust risk adjusted yield through market and interest rate cycles.

The investment manager will:

- Manage interest rate risk by holding predominantly floating rate instruments;
- Provide portfolio diversity by security type, credit risk, duration and issuer;
- Aim to distribute franking credits;
- Aim to provide regular income.

Platform Availability

HUB24 FNZ MASON STEVENS netwealth
Powerwrap APEX præmium AUSTRALIAN MONEY MARKET

Unit Price and Core Data

The unit price on 30 November 2024 was $1.0736. This is inclusive of the November distribution which will be paid in early December. The unit price is published daily on our website here. The ex-distribution unit price on 30 November 2024 was $1.0725.

As at 30 November, the weighted average yield to call of the portfolio was 6.56%. This is the yield of the portfolio to its collective call dates based on the prices at which each security was purchased. The running yield of the portfolio was 6.24%.

Franking credits provide an additional return which will depend on the investor's own tax situation. Currently, 17% of the portfolio is receiving full franking value. The remainder is receiving full cash returns. Franking credit exposure is reduced with additional investment in Tier 2 securities or senior bonds as these are debt instruments for tax purposes.

Fund returns are made up of three key aspects: 1) regular distributions (either taken as cash or reinvested according to your preference, 2) franking credits associated with these distributions, and 3) changes in the capital value (unit price) over time.

We continually measure the relative value of the prime asset classes of the fund and adjust weightings actively. On 30 November, the fund was holding 31.4% Tier 1 instruments (including both listed and wholesale), 54.2% Tier 2 instruments, 13.5% senior bonds, and 0.9% cash. Figure 2 on Page 2 depicts these current allocations.

The average credit rating of the portfolio is investment grade at BBB.

Glossary

The following details are provided to assist in understanding of terms used in this report:

Credit Spread Duration: Measures the sensitivity of a bond's price to changes in its credit spread. This measure reflects the potential change in the bond's value in response to a 100-basis point (1%) change in the credit spread. For example, if credit spreads tighten by 100 bps for a portfolio with a credit spread duration of 2.5 years, it will result in a + 2.5% return assuming all else is equal.

Interest Rate Duration: The weighted maturity of a fixed-income investment's cash flows, considering all coupon interest payments and the maturity date - used in the estimation of the price sensitivity of fixed-income securities for a given change in interest rates i.e. shorter duration bonds are less sensitive to interest rate movements than long bonds.

Running Yield: The ratio of interest to the current market price of the bond, stated as a percentage. For example, a bond with a current market price of $100 that pays $6 per year in interest would have a running yield of 6%.

Yield to Call: A yield on a security calculated by assuming that interest payments will be paid until the call date, when the security will be redeemed at the call price.

Yield to Maturity: A yield on a security calculated by assuming that interest payments will be made until the final maturity date, at which point the principal will be repaid by the issuer. Yield to maturity is essentially the discount rate at which the present value of future payments (investment income and return of principal) equals the price of the security.

General Disclosures

The material contained within this Report (The Report) has been prepared by Seed Funds Management Pty Limited (ABN 25 675 247 506) (Seed), a Corporate Authorised Representative (no 001308397) of its related body corporate, Seed Partnerships Pty Ltd (ABN 32 606 230 639) the holder of AFSL No. 492973. It is issued by the Responsible Entity of the Fund, Evolution Trustees Limited (ABN 29 611 839 519, AFSL 486217) (Evolution). Seed receives a management fee for managing the Fund.

Figures referred to in The Report are unaudited.

The Report is not intended to provide advice to investors or take into account an individual's financial circumstances or investment objectives. This is general investment advice only and does not constitute advice to any person. Neither Evolution nor Seed guarantee repayment of capital or any particular rate of return from the Fund. Neither Evolution nor Seed gives any representation or warranty as to the reliability, completeness or accuracy of the information contained in The Report.

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