

**December 2019**
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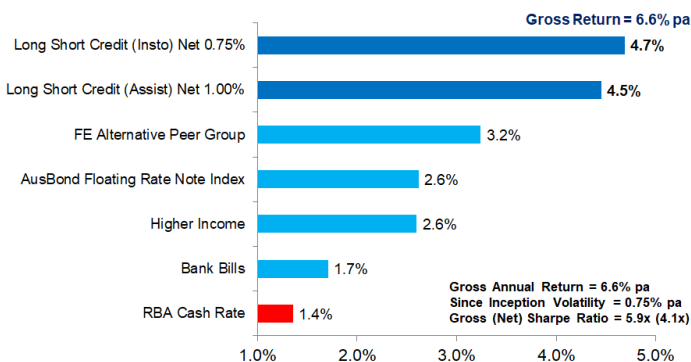
**Objective:** An absolute return fixed-income strategy focused on exploiting long and short mispricings in credit markets that targets returns above the Reserve Bank of Australia (RBA) cash rate plus 4% to 6% p.a. over rolling 3 year periods with volatility of less than 5% p.a. after Management Fees, Administration Fees and Performance Fees.

**Strategy:** We add value via active asset-selection using a range of valuation models with the aim of delivering superior risk-adjusted returns, or alpha, to traditional hedge funds. We primarily invest in senior and subordinated debt securities, hybrids and derivatives issued by Australian entities domestically, although we can invest in these securities when they are issued overseas, or by overseas entities (into Australia or offshore). The Fund can use gearing and targets holding the majority of its portfolio in investment-grade securities. It is managed by Coolabah Capital Investments.

Period ending 31/12/2019	Gross Return	Net Return (Insto.) <sup>†</sup>	Net* Return (Assist.) <sup>†</sup>	RBA Cash Rate	Gross Excess Return <sup>‡</sup>
1 month	0.58%	0.40%	0.40%	0.06%	0.52%
3 months	1.45%	0.99%	0.93%	0.19%	1.26%
6 months	2.91%	1.98%	1.87%	0.44%	2.47%
<b>1 year</b>	<b>9.70%</b>	<b>7.05%</b>	<b>6.82%</b>	<b>1.16%</b>	<b>8.54%</b>
2 years	6.30%	4.46%	4.21%	1.33%	4.97%
<b>Inception pa Aug. 2017</b>	<b>6.58%</b>	<b>4.69%</b>	<b>4.45%</b>	<b>1.36%</b>	<b>5.22%</b>

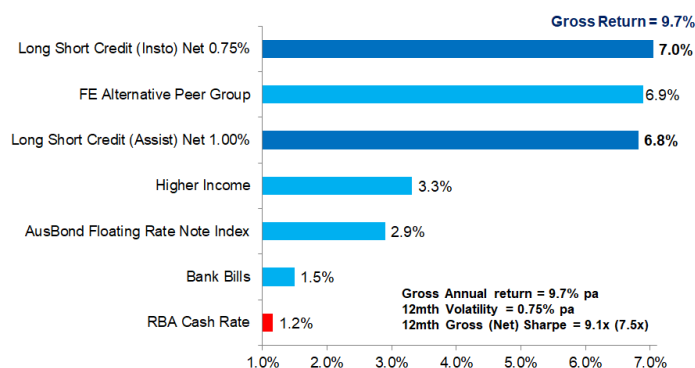
<sup>†</sup> The Assisted (Assist.) and Institutional (Inst.) columns represent different unit classes within the fund. Refer to the PDS for more information. <sup>‡</sup> The Excess Return columns represent the gross and net return of the fund above the RBA cash rate. \*On 1 April 2019 management, administration, custody and responsible entity fees were reduced from 1.5% to 1.0% per annum for Assist.

**Long Short Credit Annualised Returns (Net) vs Benchmarks**  
Since Inception 31 August 2017 to 31 December 2019



Source: RBA; Bloomberg; Coolabah Capital Investments  
 Disclaimer: Past performance does not assure future returns. Returns are shown after all trust fees. All investments carry risks, including that the value of investments may vary, future returns may differ from past returns, and that your capital is not guaranteed. To understand the Long Short Credit Fund's risks better, please refer to the detailed Product Disclosure Statement. The graph above shows the net returns since inception (Aug. 2017) after all fees attributable to the Long Short Credit Fund (source: Mainstream) and various benchmarks (source: Reserve Bank of Australia and Bloomberg). A fund is not a bank deposit and your capital is not guaranteed. This information has been prepared by Smarter Money Investments. It is general information only and is not intended to provide you with financial advice.

**Long Short Credit Returns (Net) vs Benchmarks**  
12 months to 31 December 2019

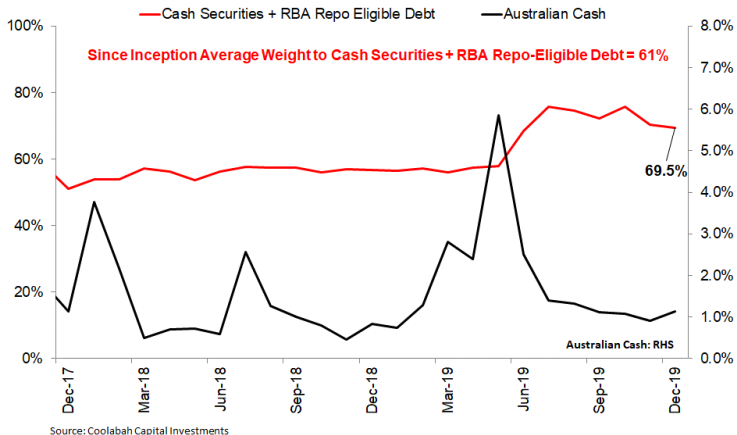


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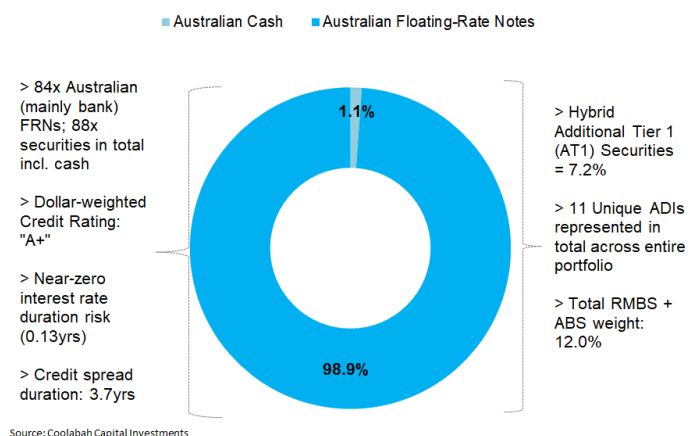
Note: all portfolio statistics other than running yield reported on gross levered value

% Monthly Returns > RBA Cash Rate + 1.0%	75.0%	Cash Securities + RBA Repo-Eligible Debt	69.5%
Portfolio Weight Cash Securities	1.1%	Portfolio Weight Hybrids	7.2%
Portfolio Weight Floating-Rate Securities	98.9%	Portfolio Weight ABS/RMBS	12.0%
Av. Portfolio Credit Rating	A+	Credit Spread Duration	3.7 years
No. Floating-Rate Notes/Bonds/Hybrids	84	Annual Volatility (since incep.)	0.75% p.a.
Total Number of Unique ADIs	11	Gross Sharpe Ratio (since incep.)	5.9 times
Av. Running Yield (Net)	3.72%	Permitted Gearing	Up to 66%
Modified Interest Rate Duration	0.13 years	<b>Awards:</b> FE Alpha Manager 2019: Christopher Joye; <b>Ratings:</b> Recommended (Atchison); Very Strong (Australia Ratings); Lonsec available to clients	

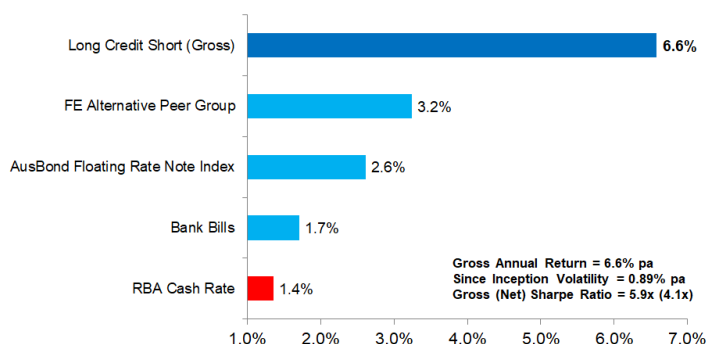
**LSCF Portfolio Weights: Cash Securities + RBA Repurchase Eligible Debt**  
End of Month, December 2019



**Smarter Money Long Short Credit Fund Portfolio Composition**  
(Gross Levered Statistics):  
31 December 2019



**Long Short Credit Annualised Returns (Gross) vs Benchmarks**  
Since Inception 31 August 2017 to 31 December 2019



The since inception gross (net insto.) return of **6.6% p.a. (4.7% p.a.)** is the total return earned by the fund since 31 August 2017, including interest income and movements in the price of the bond portfolio after all fund fees paid by institutional investors. Each investor's return will vary depending on their fee regime, investment date, and any top-ups/withdrawals they make. **The annualised volatility estimate of 0.75% p.a.** is based on the standard deviation of net daily returns since inception, which are then annualised.

Portfolio Managers	Christopher Joye, Ashley Kabel, Stephen Parker, Darren Harvey ( <a href="#">Coolabah Capital Investments</a> )		
APIR Code (Assisted)	SLT2562AU	Fund Inception	31-Aug-17
ISIN	AU60SLT25623	Distributions	Quarterly
Morningstar Ticker	41597	Unit Pricing	Daily (earnings accrue daily)
Asset-Class	Alternatives/Hedge Funds	Min. Investment	\$1,000
Target Return	Net 4.0%-6.0% > RBA cash	Withdrawals	Daily Requests (funds normally in 3 days)
Investment Manager	Smarter Money Investments	Buy/Sell Spread	0.00%/0.10%
Sub-Manager	Coolabah Capital Investments	Mgt. Fee (Assisted) ++	0.75% p.a.
Responsible Entity	EQT RE Services Ltd	Admin. Fee++	0.25% p.a.
Custodian	Mainstream	Perf. Fee	20.5% of returns over RBA cash rate

++ On 1 April 2019 management, administration, custody and responsible entity fees were reduced from a total of 1.5% to 1.0%



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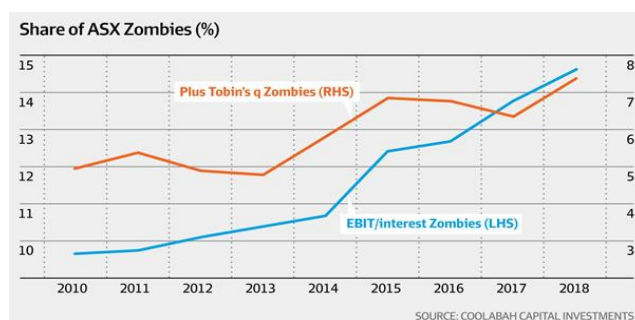


**ALPHA MANAGER 2019**  
Christopher Joye



**Portfolio commentary:** Coolabah Capital Investment's zero duration Smarter Money Long Short Credit Fund (LSCF) strategy returned 0.40% net of fees (0.58% gross) in December, outperforming the RBA cash rate's 0.06% and the AusBond Floating-Rate Note (FRN) Index's 0.15%. **During the 12 months to December 2019, LSCF returned 6.82% to 7.05% net of fees (9.70% gross), substantially outperforming the RBA Cash Rate (1.16%), the AusBond FRN Index (2.90%), and the FE fundinfo Alternatives peer group (6.89%).** LSCF's superior performance over the last year has been driven by the portfolio managers consistently exploiting mispricings in both the primary (new issue) and secondary (existing assets) markets. These mispricings are partly systematic as a function of the inherent inefficiency of the cash credit asset-class and also attributable to external shocks that shift spreads materially wide of Coolabah Capital's proprietary estimates of fair value. Although LSCF's performance in 2019 compared to the RBA cash rate (7.1% annualised net of fees for LSCF vs the 1.2% cash rate) might appear surprisingly high, it reflects the fact that the assets acquired by the portfolio managers have paid spreads well above their modelled fair value estimates. **Since its inception, over two years ago on 31 August 2017, LSCF has delivered 6.58% per annum gross (or between 4.45% and 4.69% per annum net of fees), compared to the RBA Cash Rate (1.36%), the AusBond FRN Index (2.62%) and the FE Analytics Alternatives peer group (3.24%), with much lower than expected annual volatility of 0.75% (measured using daily returns or 1.75% using monthly data), which is significantly below the LSCF's official volatility target of less than 5% per annum. This has therefore translated into a high risk-adjusted return (measured daily), or Sharpe Ratio, of 5.9 times (gross).** On a gross, fully-leveraged basis, the LSCF ended December with a weighted-average credit rating of "A+"; modified interest rate duration of 0.13 years; and a portfolio weight to bonds/hybrids of 98.9% (inclusive of an 7.2% exposure to ASX hybrids and a 12.0% exposure to RMBS/ABS). While LSCF's return volatility since inception has been low, as a daily liquidity product with assets that are marked-to-market using executable prices, volatility does exist. This contrasts with illiquid credit (e.g. loans and high yield bonds) wherein assets that have very high risk can appear to have remarkably low volatility, which is, in fact, just a mirage explained by the inability to properly value these assets using executable prices.

**Strategy commentary:** In December Coolabah Capital Investments' credit portfolios performed well, although the really big story is the smashing interest rate duration, or fixed- as opposed to floating-rate bonds, copped over the month. A portfolio of AAA rated Aussie government bonds lost 2.07% of its value — that is more than its annual yield — in December while the benchmark fixed-rate AusBond Composite Bond Index fell 1.64% as local and global growth expectations started mean-reverting. This little noticed event is, in fact, the single worst monthly result for the Composite Bond Index since way back in September 1994 when the index fell -2.28%! Older heads will remember 1994 as the bond market bloodbath when the Fed surprised markets by rapidly increasing its cash rate. The massive December 2019 loss for duration has, however, come after a truly stellar run. Even accounting for the draw-down last month, the Composite Bond Index is still up 7.26% in 2019. For institutional clients we run Coolabah's Active Composite Bond Strategy, which is benchmarked against this index, and it returned 11.51% in 2019 before fees (it is not available to retail and fee terms are confidential, hence the need to quote gross) and substantially outperformed in December as well. This time around central banks are unlikely to want to emulate the Fed's efforts in 1994 given their contemporary commitment to forward guidance and keeping rates low for long (notwithstanding that US wages growth is converging back to pre-GFC levels). **So, while duration may continue to struggle, this should be a healthy retracement rather than complete Armageddon unless our expected elevated-inflation cycle materialises more quickly than the longer-term horizon we have previously proposed.** Another fascinating feature of December is the fact that fixed-rate bonds and shares were yet again positively, not negatively, correlated with the All Ordinaries Accumulation Index, which is the main local equities benchmark, falling 1.9%. Like the Composite Bond Index, this was small beer in the context of the calendar year performance with domestic shares delivering 24.06% including dividends. We've been a lonely voice that has for years argued that using duration as an equities hedge is a dicey strategy, especially during inflationary periods when the correlation has historically been positive (both Goldman Sachs and Milliman have verified this over the last 100+ years). Set against this backdrop, Aussie floating-rate credit performed well. In contrast to the losses in fixed-rate bonds, the AusBond Floating-Rate Note (FRN) Index rose 0.15% in December while the hybrid market stormed 0.38% higher before franking. Over the last 12 months, the FRN Index returned a solid 2.90% compared to the 1.16% yield offered by the RBA cash rate. The ASX hybrid market had another cracker, providing 6.34% in total return terms before franking. **December played out as we had projected with a distinct diminution in geo-political risks as China and the US agreed a largely meaningless phase one trade deal that was nonetheless lapped-up by markets keen to avoid left-tail risks while BoJo's electoral victory in Britain provides a powerful mandate for the Brexit deal he has agreed with the EU. In December we [updated our popular analysis on the rising proportion of zombie companies on the ASX](#), that is companies that cannot service their debts if interest rates rise. The latest results are enclosed below.**



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ALPHA MANAGER 2019  
Christopher Joye



**Strategy commentary cont'd:** The first, broader measure of a zombie requires it to have been listed on the ASX for more than 10 years and to have an interest coverage ratio (ICR) that is less than 1 for three consecutive years, where the ICR is defined as the ratio of earnings before interest and tax (EBIT) to the interest repayments on the company's debt. A second narrower measure adds the requirement that the zombie also has very low growth potential with a ratio of the company's market value of its assets to their replacement cost (proxied by "Tobin's q") that is less than the median of their industry sector. This approach replicates the methodology developed by Ryan Banerjee and Boris Hofmann at the Bank for International Settlements (BIS) in 2018. Tobin's q is calculated as the sum of the market value of the company's assets and liabilities divided by the sum of the book value of its equity and debt. Our quants have also added a few new proprietary filters to further improve the accuracy of our analysis. Interestingly, the results for Australia are almost identical in terms of both the directional trend and the actual share of zombies to the BIS's findings for developed countries, which suggests that the rise of zombies is a global phenomenon. **We conclude that almost 15% of all ASX stocks are zombies based on our broader definition, which shrinks to about 7.5% if we impose the extra requirement of low expected growth. Crucially, these shares are both rising fast: the number of observed zombies on both definitions has increased 50% since 2010. The emergence of an expanding cohort of zombies casts into sharp relief the trade-offs of hyper-stimulatory monetary policy. Dan Andrews, the Commonwealth Treasury's Chief Adviser on Macroeconomic Modelling & Policy, emailed us regarding this work following its publication in the AFR. "Your results are consistent with a new paper of mine that shows an increasing survival of low productivity incumbents from circa 2012," Andrews wrote. This [treasury research](#) corroborates one of our central theses: that unconventional monetary policy is thwarting the creative destruction inherent in capitalism that reallocates scarce labour and capital away from unproductive businesses to more innovative firms. Andrews and his co-author David Hansell find that Australia fares well on a global basis in terms of its ability to ensure productive companies attract more human talent than less productive peers. And they show that because of this, labour productivity is 20% higher than it would be if workers were randomly distributed. The bad news is that the speed with which high productivity companies expand and low productivity businesses contract has been slowing over time with this dysfunction especially evident since 2009. The treasury economists also verify our data scientists' research documenting a growing number of zombies by presenting "evidence that low productivity incumbent firms are increasingly likely to survive". In fact, the rising influence of zombie-like companies accounts for about one-quarter of the slowdown in overall productivity growth since 2012. And since higher productivity firms pay higher wages, the zombieification of industry "provides a new insight into why aggregate wage growth over recent years has been weaker than expected". Reducing interest rates boosts employment, investment and economic growth in the short term. But to the extent that this is generating fake growth, and capitalism's creative destruction is being thwarted by allowing bad businesses to survive when they would otherwise die, central banks could be undermining future productivity and growth outcomes. Don't forget to listen to Coolabah Capital's popular Complexity Premia podcast. You can listen on your favourite podcast app, or you can find it on [Apple Podcasts](#) or [Podbean](#) here.**



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