

# Shaw SMA - Hybrid Income Portfolio

Shaw and Partners Portfolio Strategies

## Monthly Review – November 2018

### Portfolio Overview

Strategy Inception Date: 2 Sep 2015  
 SMA Model code: SP0002  
 Minimum Investment Amount: \$5,000  
 Indicative number of securities: 10 - 30  
 Portfolio return objective: RBA Cash rate + 3% (gross)

### Portfolio Holdings - Top 5

ASX Code	Issuer	Security Type
NABPC	National Aust. Bank	Capital Note
MQGPC	Macquarie Bank	Capital Notes 3
CBAPD	Comm Bank	PERLS VII
WBCPG	Westpac Bank	Capital Note IV
WBPCF	Westpac Bank	Capital Note III

### Portfolio Characteristics

Expected Yield to Call/Maturity (incl franking):	5.6%
Expected Gross Running Yield (incl franking):	5.4%
Expected Cash Running Yield (ex franking):	4.0%
Expected Years to Maturity:	4.4
Number of Securities:	22
Floating Rate exposure	100%
Fixed Rate Exposure	0%

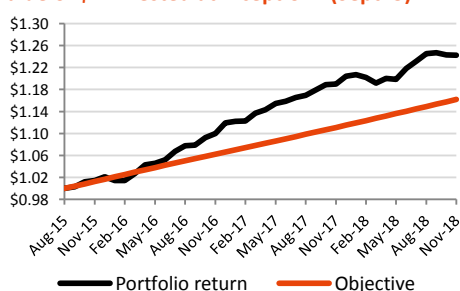
### Portfolio Short term Performance \*

Total Return	1 Mth	3 Mth	6Mth	1yr
Income Return (Gross)	0.13%	1.51%	2.69%	5.24%
Capital Return	-0.21%	-1.77%	0.91%	-0.84%
Total Portfolio Return	-0.08%	-0.26%	3.60%	4.40%
Portfolio Rtrn Objective	0.40%	1.10%	2.30%	4.60%
Excess Rtrn v Objective	-0.48%	-1.36%	1.30%	-0.20%

### Portfolio Long term Performance \*

Total Return	2yr	3yr	Incpt'n
Income Return (Gross)	5.36%	5.36%	5.41%
Capital Return	0.90%	1.63%	1.49%
Total Portfolio Return	6.27%	6.99%	6.90%
Portfolio Return Objective	4.60%	4.72%	4.70%
Excess Return v Objective	1.67%	2.27%	2.20%

### Value of \$1 Invested at Inception\* (Sept15)



### Market Returns

Return	1 Mth	3 Mth	1yr
ASX200 Accumulation	-2.21%	-9.28%	-0.96%
RBA Cash rate	0.13%	0.38%	1.50%

\*Returns are gross of franking credits

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### Portfolio Details

**Portfolio Name:** Shaw Hybrid Income Portfolio  
**Portfolio Inception Date:** 6-Sept-15 (underlying model portfolio)  
**SMA Model code:** SP0002  
**Indicative # of securities:** 10-30  
**Portfolio Return Objective:** RBA Cash rate + 3% (gross)  
**Shaw Model Managers:** Steve Anagnos / Cameron Duncan

### Investment Strategy

The objective of the Shaw Hybrid Income Portfolio is to provide a predictable level of income whilst minimising risk to capital. The target total portfolio return (gross) of the portfolio is 3% above the RBA cash rate. This return will be generated from a combination of cash (interest payments and dividends), franking credits and capital growth (realised and unrealised) from an actively managed portfolio strategy.

**Risk tolerance:** The portfolio aims to limit the risk of capital loss through security diversification and active portfolio management. It is suitable for investors that have a 3 year + investment horizon that can tolerate secondary market pricing and liquidity risks through the life of the securities, up to the respective first call/maturity date of each security.

### Investment Objectives

The Shaw ASX Hybrid Income Portfolio aims to provide investors with exposure to a highly transparent portfolio of ASX listed debt and preference securities that offer diversification benefits to both Australian Equities and cash/term deposit investor's allocations.

There is a growing universe of listed assets spanning Senior Debt, Subordinated Debt, Convertible Preference Shares, Convertible Notes and Income Securities (debt and equity). While these "Hybrid" securities each have their own characteristics, research and subsequent implementation and monitoring allows for strategies to extract risk adjusted return from this sector that aims to enhance a core portfolio of Australian Equities and cash.

### Portfolio Highlights

- The average median margin across financial hybrids widened 34bps over November to 3.59%, in keeping with the wider credit spreads and weaker equity indices experienced globally. The ASX S&P200 was 2.88% lower over the same period. Australian iTraxx 5 year CDS was 6.25bps wider over the period, closing at 86.7bps on the 30 November. **For the month of November the Total Portfolio Return was -0.08% and -0.26% for the quarter. The Total Return of the portfolio is below its objective for the month, quarter and full year.** Since inception the Total Portfolio Return is 6.90%, which is 2.20% over its return objective.
- November was a low income month**, with only 3 names trading ex-dividend: CGFPB, NABPB and WBCPD. The total income return (gross) was 0.13% for the month and 1.51% for the quarter, whilst the income return since inception is 5.41% p.a. The capital return for the month of November was -0.21% and -1.77% for the quarter. We will see income rise substantially in December as most of the securities trade ex-dividend.
- Both CBA and Westpac completed successful book builds for new AT1 hybrid issues over November.** Both issues were priced at a margin of 3.70% over the 3 month bill rate, and both issues having a tenor to first Optional Call Date of between 5 to 6 years. CBA allocated A\$1.25 billion on a firm basis in the broker firm offer, with Westpac also allocating A\$1.25bn. AMP's listed AT1 security – AMPPA - saw support after a difficult October, as bargain hunters moved in to an oversold situation. AMPPA's trade margin contracted from a wide 4.68% at the end of October to 4.48% at the end of November. The portfolio does not hold AMPPA at present.

## Portfolio Performance

The portfolio was established on 2 September 2015 and now has over 39 months of performance history, bringing up its 3 year milestone. The portfolio continues to be weighted towards bank hybrids based on the attractive risk/return trade-off following on from the large equity raisings undertaken by CBA, NAB and ANZ in 2015. Notwithstanding the continued strong performance of this asset class, we maintain the ability to meet the return objective of the Hybrid Income portfolio of 3% above the RBA cash rate.

For the 3-year period the total return of the portfolio is +6.90% p.a, whilst the income returns (gross) is +5.41% p.a, both ahead of their respective return objectives.

During the month we reinvested the portfolio holding in CBAPC into the New PERLS XI (CBAPG) offer. We also reinvested our smaller holding of WBCPD into Westpac Capital Notes 6 (WBCPI) offer and received an additional allocation in the Book build. We also reduced exposure to CBAPG and CGFPB to make way for the additional Westpac, focusing on these 2 names given the relative risk/return characteristics as compared with the other names in the portfolio.

During the month the best performers were MQGPC (+1.2%), CGFPB (+0.8%) and NABPB (+0.5%). The main detractors were NABHA (-1.4%), CBAPE (-0.7%) and CBAPG (-0.6%).

## Portfolio Outlook and Strategy

In terms of maturities in the sector, the \$700m SUNPD issue was redeemed on 22 November 2018, and AMP announced the redemption of the \$325m AMPHA, callable on the 18 December 2018. The next major bank hybrid approaching its optional call date is NABPB which has an optional call date in December 2020. The only listed bank AT1 security remains NABPE, which has its first call date on 20 September 2023. It is possible that issuers return at some stage to the ASX Listed Tier 2 market, particularly if APRA proceeds to its proposed changes to banks Total Loss Absorbing Capacity that is states will require another ~ \$75bn in capital, expected in the form of Tier 2 Subordinated Debt. This announcement in early November had the effect of widening Tier 2 spreads by up to 15bps. An increase in capital required infers that banks will have less senior debt to issue.

Hospitality and Transport lender Accesstoday (AXL) announced on 30 November a continuation of its voluntary suspension. AXL requires further time to complete the process of working with its lenders, finalising the strategic review and completing a successful equity raise. At November end, the portfolio's current weighting in AXLHA is currently ~ 1.60%.

The Shaw and Partners Hybrid Income Portfolio is designed to help diversify the risk and return outcome of a traditional Equities/Debt/Cash an income goals portfolio. Over the last few years Hybrid Securities have increasingly been used in income goal portfolios.

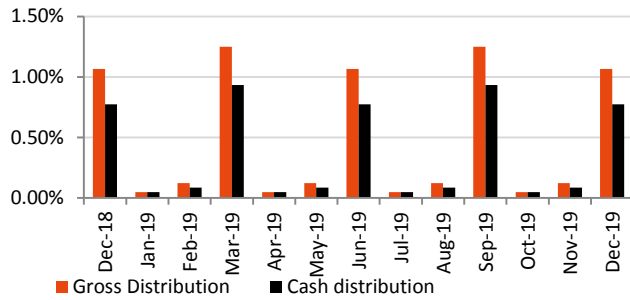
Our in-house expertise in this sector has allowed us to use this sector/investment universe as a dedicated Asset Class blending with other income producing assets with the aim of maximising the probability of achieving investors income goals.

*The Shaw and Partners Hybrid Income Portfolio is a fully managed account (SMA) whose inception date was 12 May 2016. The strategy employed by this portfolio was conceived in August 2015 and first published as the Shaw and Partners ASX Listed Debt and Hybrid Moderate Income Portfolio commencing 2 September 2015. Although this was a model portfolio, it was published on a monthly basis and was used by Shaw and Partners Advisers as a way of managing hybrid income portfolios in conjunction with the Investments team. It provided weights for each security in the portfolio and trade recommendations as at month end. The performance shown in this report is that of the model portfolio from 2 Sep 2015 to 30 June 2016 and the Shaw SMA from 1 July 2016 onward.*

*The Shaw and Partners' Investment Team actively manage the Portfolio and makes changes to security weights on an ongoing basis (including inclusions/exclusions, and reweighting's of investments). The performance stated within this report reflects all changes that have occurred within the Portfolio since inception and have been documented by each month's monthly performance reports that have been distributed into the Shaw network and the wider investment marketplace. Investors' individual portfolio performance will differ to the performance of the Portfolio based on timing of investment, client's specific risk profile and subsequent stock selection, associated transaction and management fees, and tax consideration of the portfolio and underlying investments. Investments can go up and down. Past performance is not necessarily indicative of future performance.*

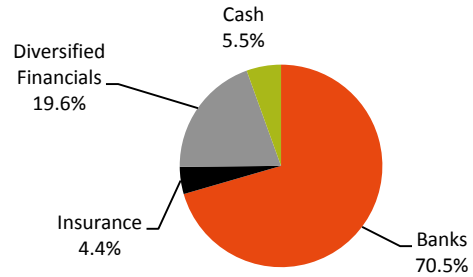
ASX Code	Security	Last Price	Frank'g	Running Yield		Yield to C/M	Call Date/ Maturity	Years	Issue Margin
				Gross	Cash				
NABPC	Nat Aust Bank Capital Note**	\$101.30	100%	5.36%	3.75%	5.20%	23-Mar-20	1.3	3.50%
MQGPC	Macquarie Group Capital Note III	\$103.30	45%	5.62%	4.78%	6.11%	16-Dec-24	6.0	4.00%
CBAPD	CBA - PERLS VII CPS**	\$97.65	100%	4.83%	3.38%	6.06%	12-Dec-22	4.0	2.80%
WBPCG	Westpac Capital Note IV	\$104.50	100%	6.55%	4.58%	5.85%	20-Dec-21	3.0	4.90%
WBPCF	Westpac Capital Note III**	\$100.01	100%	5.80%	4.06%	5.58%	22-Mar-21	2.3	4.00%

**Chart 1: Expected Distribution Payment Profile**



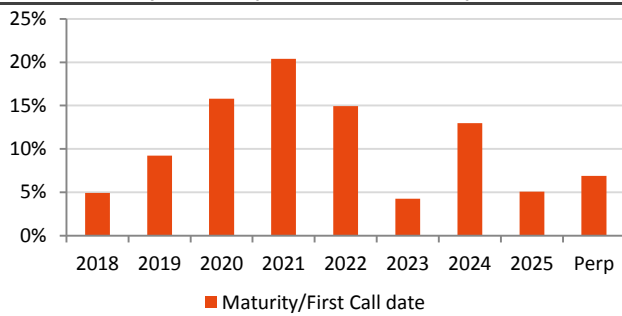
Source: Shaw and Partners

**Chart 2: Industry / Sectors**



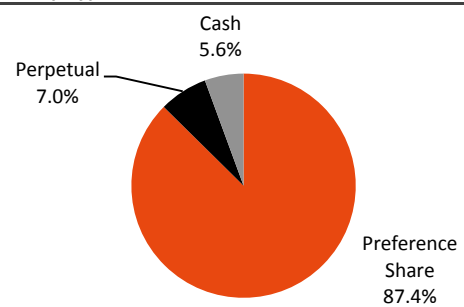
Source: Shaw and Partners

**Chart 3: Maturity/First Call profile of securities in portfolio**



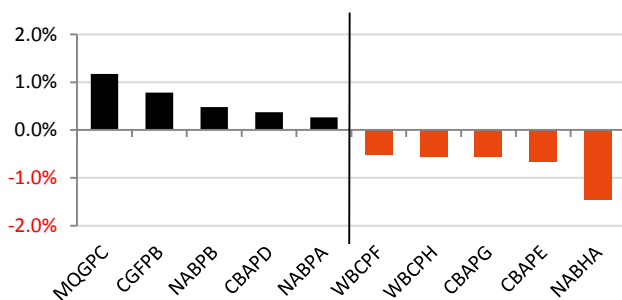
Source: Shaw and Partners

**Chart 4: Security Type**



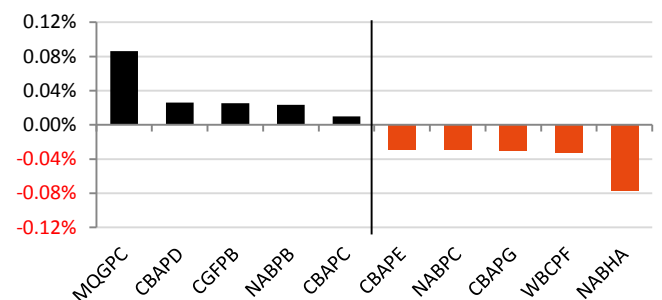
Source: Shaw and Partners

**Chart 5: Performers & Detractors - Top 5 / Bottom 5 (1 month Total Return)**



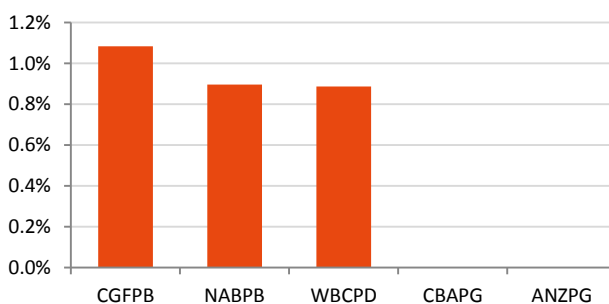
Source: Shaw and Partners

**Chart 6: Attribution to return - Top 5 / Bottom 5 (1 month Total Return)**



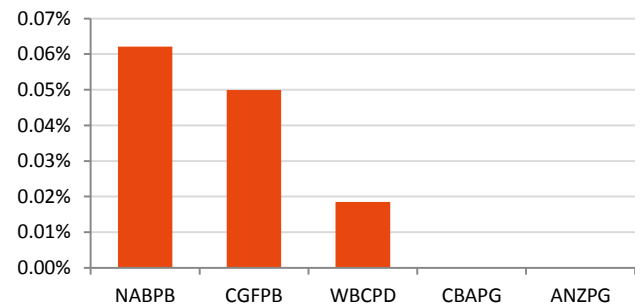
Source: Shaw and Partners

**Chart 7: Top Performers (1 month Gross Income Return)**



Source: Shaw and Partners

**Chart 8: Top Attribution (1 month Gross Income Return)**



Source: Shaw and Partners

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