

# Challenger IM Credit Income Fund – Class A

ARSN 620 882 055 APIR HOW8013AU

## Monthly Report October 2024

Performance <sup>1</sup>	1 Month (%)	Quarter (%)	6 Months (%)	FYTD (%)	1 Year (%)	3 Years (%) p.a.	5 Years (%) p.a.	Since Inception (%) p.a. <sup>2</sup>
Challenger IM Credit Income Fund - Class A	0.88	1.96	3.92	2.66	8.97	6.38	-	6.17
Challenger IM Credit Income Fund - Class I <sup>3</sup>	0.88	1.96	3.92	2.66	8.97	6.38	5.13	-
Bloomberg Bank Bill Index	0.37	1.12	2.23	1.49	4.45	2.94	1.86	2.16
Active return	0.50	0.84	1.69	1.17	4.52	3.44	3.27	4.01

Data Source: Fidante Partners Limited, 31 October 2024.

<sup>1</sup>Returns are calculated after fees have been deducted and assume distributions have been reinvested. No allowance is made for tax when calculating these figures.

<sup>2</sup>The Inception date for Class A is October 1 2020.

<sup>3</sup>As at the date of this report two classes of units are offered: Class I which has been offered since the inception of the Fund on 3 October 2017 and Class A which has been offered since 1 October 2020. For information purposes, and to give a longer term view of the Fund's performance, the returns for the Class I are also provided in the Performance table and shows Class I's performance. The returns quoted for Class I have been adjusted to reflect the fees applicable to the Class A units.

**Past Performance is not a reliable indicator of future performance.**

### Fund Features

**Experienced team** - Boasting one of the longest track records in institutional private lending strategies, the team is uniquely positioned to exploit opportunities across both public and private lending markets. The team's breadth of experience allows the Fixed Income team to exploit market inefficiencies across all sectors in the global credit market.

**Risk management** - The Fund aims to reduce market risk by considering low cross-sectoral correlations and maintaining a relatively short spread duration. The team identifies complexity risks to provide income and what they consider to be attractively priced but hard to access liquidity, allowing the Fund to minimise more volatile currency and interest rate risks.

**Diversification** - The Fund invests across both public and private credit markets providing the opportunity to allocate to the most attractive sectors over time. The Fund targets a weighted average investment grade rating and the diversified set of asset classes in which the Fund can invest includes secured loans, securitised credit, corporate bonds and real estate debt.

**Strong governance** - The Fixed Income team's clients benefit from a robust governance framework including an independent credit risk management team within the Challenger Group.

### Fund Objective:

The Fund aims to achieve superior absolute returns over the medium to long term whilst offering capital stability and a steady income stream.

### Fund Details

Management Fee	0.60% p.a.
Strategy FUM	\$43.0 mil
Buy/Sell Spread	+0.18/-0.18%
Distribution Frequency	Quarterly
Redemption Terms	Monthly with 10% Fund level gate

### Key Statistics

Number of Issuers	130
Running yield (%) p.a	6.3
Modified duration (yrs)	0.09
Average Rating	BBB-
Portfolio Credit Spread Duration (yrs)	3.1
Non-AUD Denominated	28%
Private Credit Allocation	20%

## Monthly Commentary

### Performance Update:

The Fund was up 0.88% in October, a return of 0.50% over the Bloomberg AusBond Bank Bill Index Benchmark, and 0.38% over the Bloomberg AusBond Credit FRN index.

The main drivers of returns for the month were income generation (c. 0.50% contribution) and credit spread movements (c. 0.30% contribution).

Over the last 12 months the Fund has returned 8.90% outpacing the 5.86% return on the Bloomberg AusBond Credit FRN index, exceeding our goal of outperforming daily liquid credit by 1-2% per annum.

### Fund Positioning:

The With credit spreads resuming their moves tighter in the month our bias towards private markets remains intact. The current allocation to high yield or unrated credit is 27% which is projected to increase to 29% once our current pipeline of private investments is completed. The constraining limit is 35% and we expect to increase the allocation into the 30-33% range early in the new year if conditions remain unchanged.

Over the month the Fund's allocation to securitised credit declined to less than 15%, down from 17% a year ago. While valuations on mezzanine tranches of public deals are generally at the tightest end of post GFC ranges, we see pockets of opportunity in private warehouse markets and more esoteric collateral types.

Our allocation to Real Estate increased by 2% over the year and was re-mixed towards private markets. The pipeline for private real estate loans is strong, reflecting ongoing dislocation in the sector. Despite the weak fundamentals we see attractive opportunities in real estate lending markets. The Fund is targeting transactions that fall just outside of bank lending criteria which are coming at yields more than 2% wider than bank pricing and allow the team to negotiate strong creditor protections.

Asset quality within the Fund remains strong with only 1.4% of borrowers rated below B-. There are no private assets in the Fund valued below 90 cents in the dollar with all borrowers currently on all required payments of interest and principal.

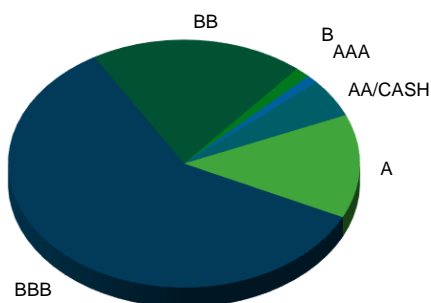
### Market conditions:

As the probability of a Republican victory in the US election increased over October, risk markets rallied strongly and credit was no exception. US high yield credit spreads were 9 basis points tighter in October but caught an even stronger bid post-election moving another 25-30 basis points tighter. This places high yield bond spreads at the tightest levels since 2007.

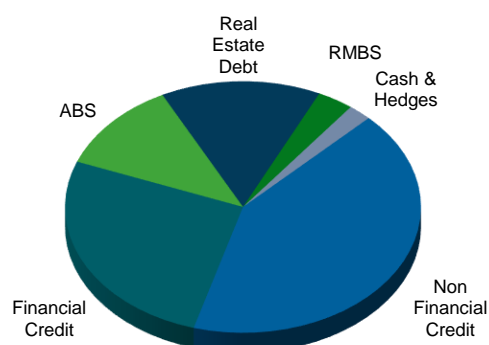
## Performance Statistics

Standard Deviation (ann.)	2.1%
% of Down months	7.0%

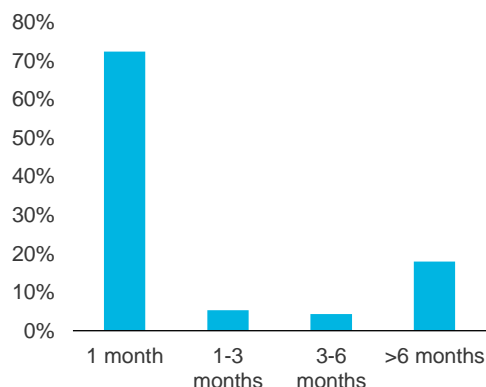
## Fund Credit Quality



## Fund Asset Allocation



## Fund Liquidity Exposure



Offsetting the move in credit spreads has been sharp increases in interest rates which has led to drawdowns in fixed rate indices. The ICE BofA Australia Broad Market Index declined by over 2% in October as yields increased from 4.15% to 4.6% at month end (4.7% at the time of writing).

The move in interest rate markets has limited the amount of spread compression in investment grade markets. US IG spreads tightened by only 0.05% over the month with credit spreads still well wide of the previous tight levels in 2021 and 2017.

US third quarter earnings season kicked off in October. At the time of writing 462 out of the 500 S&P500 constituents had reported delivering 5% sales growth and 7% earnings growth. These levels have been a positive surprise and represent no meaningful slowdown from where earnings have been tracking in prior periods.

European markets have lagged the strong risk on tone in the United States with spreads over 30 basis points wider than the tight levels for 2024 and 100 basis points wider than the post GFC tight pricing from 2017. The strength in the dollar has led to cross currency basis collapsing in Europe suggesting the level of spreads in Euros might not be a true reflection of where spreads are for an investor hedging back to Australian dollars.

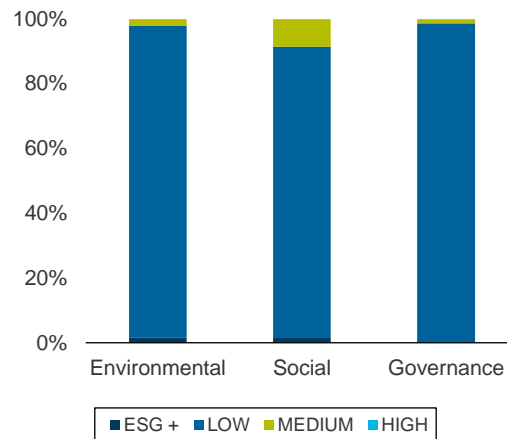
Domestically the major banks provided updates through to the end of the September quarter. Impairments were generally stable with moderate lending growth, stable net interest margins and some expense pressure. CBA continues to trade at over 3 times book value making it the most expensive bank in the world. Even with no analysts having a buy on CBA and a consensus price which is over 30% below current levels, there seems to be no stopping the demand.

Domestic securitised markets took a pause during the month with a lighter calendar for issuance but have opened up post the US election. Senior AAA and high yield mezzanine tranches tightened slightly over the month while investment grade rated mezzanine edged slightly wider.

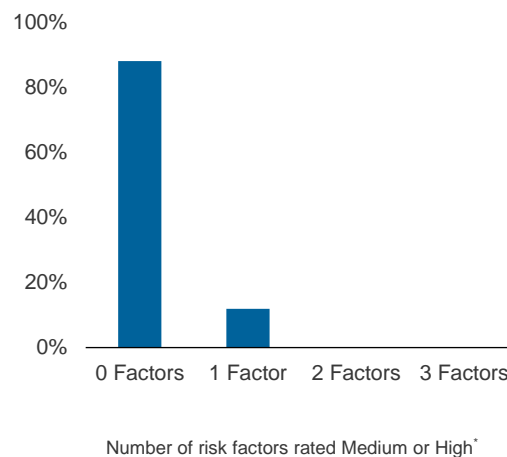
This stood in contrast to financials which found a strong bid, particularly in Tier 2 paper which rallied 20 basis points over the month. The strong performance relative to corporate and securitised credit was somewhat of a surprise given expectations of further Tier 2 supply following APRA's proposal to phase out Additional Tier 1 capital replace with Tier 2 and CET1.

Private market activity has picked up significantly as we approach year end. The long-anticipated default of Rockpool, a well-publicised private borrower, was front page news and caused no small degree of hand wringing. Like the default of Pluralsight in the United States, a single default does not imply outsized risk in the asset class but rather a normalisation of the credit environment. It does raise important questions regarding how assets are valued and held within funds but just as the low default environment of 2021/22 didn't imply perfection, these individual defaults don't imply disaster.

### ESG Profile



### ESG Risk Layering



\* Percentage of deals which have multiple risk factors rated Medium or High. For example, 2 might be Environmental and Governance risk rated Medium.



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