December 2020

SPECTRUM STRATEGIC INCOME FUND

FUND INFORMATION

Fund
Spectrum Strategic Income Fund

Responsible Entity
Equity Trustees Limited (RE)
ABN 46 004 031 298; AFSL 240 975

Manager
Spectrum Asset Management Ltd (Spectrum) ACN 096 442 198; AFSL 225 069. Spectrum is a Sydney based fund manager that focuses on income. Our strength is corporate debt. We take and manage credit risk with moderate interest rate risk.

Investment Objective
The Fund aims to generate higher returns than the RBA Cash Rate over the short to medium term with lower volatility than equities.

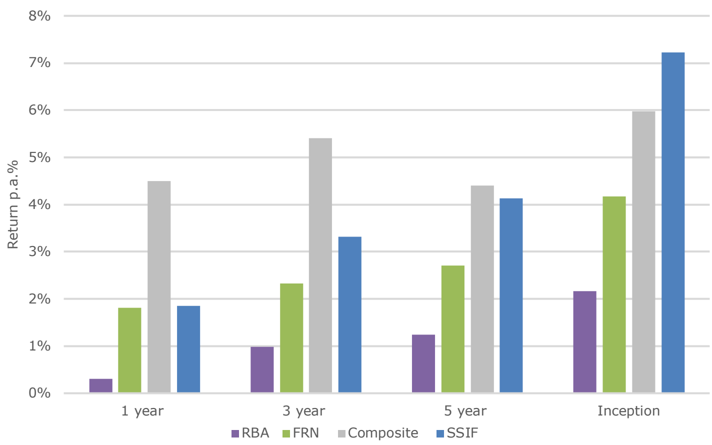
Investment Strategy
The Fund holds a diversified portfolio of debt and income securities with a view to minimising any loss of income and capital of the Fund. Issuers may be government bodies, banks, corporations and, to a limited extent, specialist financing vehicles. To maintain a diversified portfolio structure, certain limits are imposed on security type, credit risk, industry and issuers.

Target Return
RBA Cash Rate +1.50% p.a. net of fees.

Investment Highlights
- Experienced and active management team with a proven track record
- Quarterly distributions
- Low duration portfolio
- Diversified portfolio of AUD denominated corporate securities
- Consistent top quartile performance

APIR	ETL0072AU
Entry / Exit Price	$1.0693 / $1.0661
Fund Size	$75.67 m
Unit Pricing	Daily
Distributions	Quarterly
Inception Date	31 May 2009

PERFORMANCE COMPARISONS



FUND PERFORMANCE

	1mth	6mth	1yr	3yr p.a.	5yr p.a.	Incep p.a.
Net Return (%)	0.41	2.11	1.85	3.32	4.13	7.23
RBA Cash Rate (%)	0.01	0.10	0.31	0.99	1.24	2.16
Spread to RBA (%)	0.40	2.01	1.54	2.33	2.89	5.07
Income Distribution	0.51	0.96	3.29	3.44	3.34	4.01

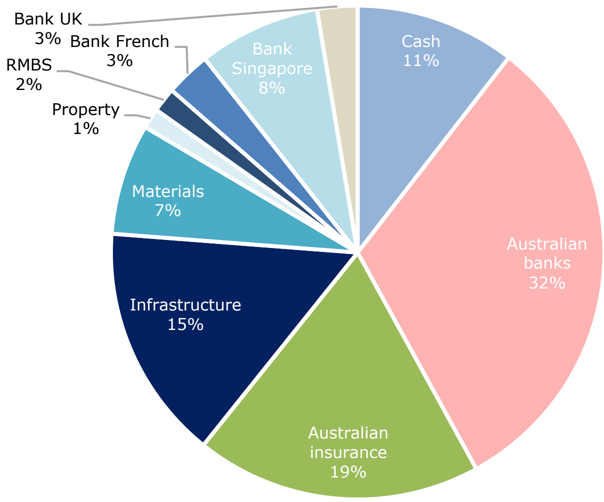
NOTE: Past performance is not a reliable indicator of future performance.

INCOME DISTRIBUTIONS

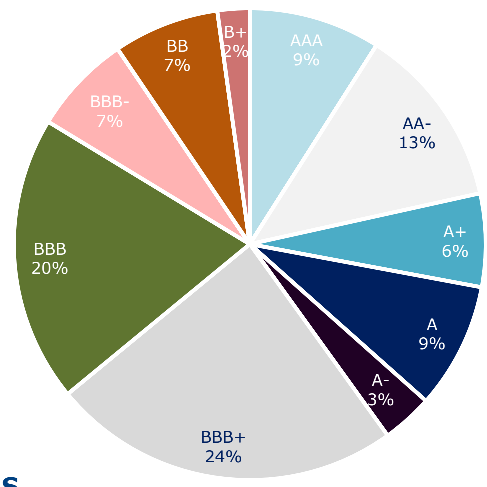
2020	Mar	Jun	Sep	Dec
Distributions (cents per unit)*	0.71	1.63	0.45	0.51

* Net Return after fees and expenses assuming reinvestment of all distributions.

SECTOR ALLOCATION



CREDIT RATING



RATINGS

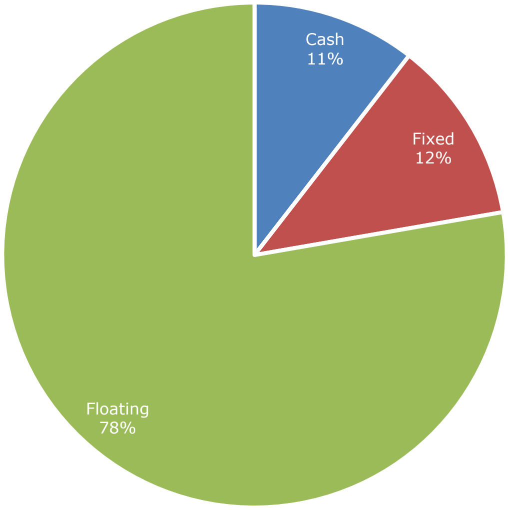
MORNINGSTAR ★★★★

★★★★★ Superior SQM RESEARCH

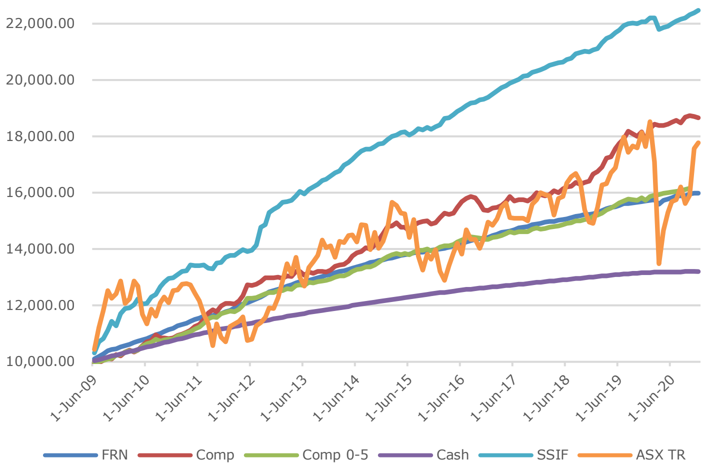
PLATFORMS

AMG Super	ausmaq	Australian Money Market
Bell Direct	CMC Stockbroking	Freedom of Choice
HUB24	mFund	nabtrade
netwealth	Powerwrap	uXchange

FIXED / FLOATING



GROWTH OF $10,000 SINCE INCEPTION



TOP TEN HOLDINGS

National Australia Bank	17.6%	Paccar	5.5%
Cash	10.5%	Verizon	4.6%
Suncorp Group Ltd	9.9%	Westpac Banking Corp	4.5%
AMP Group Ltd	9.5%	IAG Ltd	4.0%
DBS Group Holdings Ltd	8.0%	Ausgrid Finance	4.0%

MARKET COMMENTARY

One could easily look at December and believe that not a lot happened. In fact, the month of December was somewhat volatile. Equity markets rallied then sold off then rallied again. Government bonds rallied, then sold off when equity markets rallied then rallied again when equity markets weakened.

The U.S. election played its part in volatility but so too did Trump with his denials of losing the U.S. election, promoting the idea that the elections were a fraud and in true Trump speak created a continuing helter-skelter environment. And then to end the month we have more bad news on COVID-19.

So how did markets react to all this confusion? Markets responded to the prevailing news at the time and were somewhat in the guise of buy the rumour sell the fact. The capabilities of a rollout of any COVID-19 vaccine has been met with problems. Distribution and manufacture of the vaccines have proven to be a challenge. At current rates, any meaningful rollout of the vaccine will take significantly longer than expected. This sluggish rate will have an economic impact and to further cloud the issue we now know that there are two new strains which the vaccine is not all that effective against. The outlook remains somewhat confused.

What we do know however is that equity markets are likely to continue to rally and that means credit spreads will continue to tighten. Credit spreads will probably tighten but not significantly for investment-grade securities. Bank capital securities such as Bank sub T2 have the capacity to rally significantly as many are still trading as much as 6 times bank senior paper spreads. The hunt for yield or income will prevail and for many that will require the movement to much riskier investments. And this is what keeps us up at night. This increased risk adoption can lead to a non-linear response and especially so at times of heightened volatility. Investors seeking a return of say 7.5 % must now take almost three times more risk (as measured by standard deviation) than an investor would in 1995 (Newfound Research November 2020).

The comparable returns for the year are interesting. The S&P ASX 200 Total Return Index was up 1.4%. The CDX High Yield has moved from 305bp at the end of January, through to 850bp in March and closed the year at 295bp. For high yield, it is hard to see spreads tightening significantly and importantly is hard to see the current return on HY investments not becoming negative over time and especially so, as many of the High Yield Funds are also fixed-rate securities and are susceptible to an increase in interest rates (duration effect) and stalling credit spread movement or a lack of tightening credit spreads providing some capital gain.

It is hard to expect that the fixed-rate bonds can continue to perform and rally unless we go to negative rates. Fixed-rate bonds had a significant rally over the year. With bond yields at historical lows and with short bonds trading close to zero percent, it is hard to see how any significant return can be made. Duration at some point will impact fixed-rate returns.

Hybrids over the year exhibited some positive aspects and over the course of 2021 should produce some solid returns with some volatility. We expect that the NABHA will be redeemed either in February or May. Other bank T1 securities will provide opportunities as those approaching maturity are often mispriced. The listed T1 securities for example are pricing about 20bp wider than their unlisted peers.

PORTFOLIO MANAGEMENT

Investment Strategy

Over the coming months, we expect several themes to unfold. We expect that demand for Bank T2 sub-debt to increase as the securities with their spreads are trading at an excess of 6x senior bank paper. Corporate spreads continued to tighten over December. With many corporates now trading with a yield of less than 1%, the challenge will be to find value and that is why we currently favour Bank sub-T2 papers. Some hybrids offer reasonable returns and especially those that are trading at significant premiums over their bank sub T2. We see this mispricing as an opportunity.

With interest rates at record lows and if we do not see interest rates going negative then fixed-rate securities will produce negative returns if interest rates rise. The Fund is floating rate and will not be significantly impacted by an increase in interest rates. The Fund does own some fixed-rate securities and the duration of these securities is relatively short.

Currently, the duration of the portfolio is being reduced, and as a result, the portfolio risk will reduce. The portfolio will also benefit materially if interest rates were to move higher. Because of the absolute focus for the Fund through investing predominantly in floating rate securities, the fund benefits as rates move higher. Floating rate note coupons are reset every three months and an increase in rates will see higher coupons being paid. The portfolio is not immunized to any credit spread widening, however that widening could be offset to some degree by the higher coupon rates. In a rising interest rate environment, floating-rate notes are often keenly sought by investors and funds alike as they provide some protection and positive returns.

We continue to focus on NABHA as we expect the security could be called early 2021. The NAB AGM was held on the 18th December and received shareholder approval to redeem the security. The security may be called as early as mid-January allowing the security to be redeemed in February.

We are watching the developments in AMP with interest. We expect that with the bid by ARES Capital to buy AMP that another bidder could enter the fray. We don't believe that ARES would want the bank. If the bank is sold to another bank, we expect that the sub-debt will tighten significantly. Currently, the Bank has excess capital and any suitor

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probably would not want excess capital unless that capital can be deployed elsewhere. The AMP preference shares do have change of control clauses and as such we expect that in the event of a takeover the preference shares would be redeemed. Currently, the sum of the parts in AMP is more than where AMP is currently being valued. It appears as reported in the AFR that Ares Capital does not want the AMP Bank and that a consortium is being put together by outside parties to purchase the bank.

The outlook for continued increasing equity returns bodes well for credit securities. If the current mantra of central banks is to maintain liquidity, then equity will perform and so too credit. We expect to see continued demand for corporate credit.

To take advantage of the current outlook the portfolio has to be managed strategically and tactically. The Fund's strategy is to invest opportunistically as our maturity profile allows. This means that we have the option of maintaining a large cash base to invest if there is a market dislocation or reinvesting the proceeds. This also means that investments are being made opportunistically. On any spread widening the Manager is looking to improve the creditworthiness of the Fund over time and improve the diversification and credit quality whilst investing in securities that are expected to have lower volatility during a period of dislocation or rising interest rates. This means we will be when possible investing in corporates with solid cash flows or opportunistically in hybrids that have in our view some chance of capital gain due to mispricing.

The portfolio has now returned nine positive months at a time since the drawdown suffered in March. The rolling effect of the year's past performance will roll off and if the Fund holds current performance or improve on current monthly returns levels the performance of the Fund will increase significantly. As interest rates stall at current levels, the Composite Index will cease to provide significant performance due to duration. The Composite Index may well be challenged to maintain a positive return over the coming months.

Of concern is how the high yield funds will perform over the coming year and could be nearing an end of cycle. High yield will be challenged to provide a meaningful return over the coming year. After seeing a spread in March 2020 of swap+800 and with current spread of approximately 300 it is hard to see how any meaningful return can be achieved. Given the current level of high yield spreads one could see a trading range of 270 to 320 bp over the coming year. As much of high yield is also fixed-rate any increase in interest rates will have a significant on impact returns unless spreads can tighten significantly over the year.

Since its inception, the Fund has negatively correlated to the Bloomberg All Maturities index. It is interesting to note that the 1-year return for the ASX 200 is 1.44% and the Fund's return over the same period is 1.85% with significantly lower volatility.

SSIF vs Correlation to	1yr	3yr	5yr	10yr	Incep.
FRN Index	84.3%	79.9%	72.0%	54.2%	60.2%
Composite Index	29.0%	39.3%	38.9%	9.2%	-8.8%
ASX 200 Total Return	85.5%	74.3%	60.8%	40.5%	39.3%

Fund Metrics	
Tracking error to FRN Index 5 years	0.58
Tracking error to FRN Index since inception	2.96
Largest drawdown since inception	1.86%
Total drawdowns since inception	8.7%
Average drawdown	-0.51%
Number of negative months since inception	17
Number of positive months since inception	122
Best monthly return	4.49%
Consecutive Positive Returns	9

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