Janus Henderson

TACTICAL INCOME FUND

Janus Henderson INVESTORS

As at October 2017

Fund objective
The Fund seeks to achieve a total return after fees that exceed the total return of the Benchmark by predominantly investing in a diversified portfolio of Australian income producing assets

Benchmark
Bloomberg AusBond Bank Bill Index and Bloomberg AusBond Composite 0+ Yr Index (Equally Weighted)

Portfolio Manager
Glenn Feben and Jay Sivapalan

Risk profile
Low-medium

Suggested timeframe
3 years

Inception date
30 June 2009

Fund size
$2.6 billion

Minimum investment
$25,000

Management cost (%)
0.45 p.a.

Buy/sell spread (%)
0.00/0.00

Distribution frequency
Quarterly

ARSN code
130 944 866

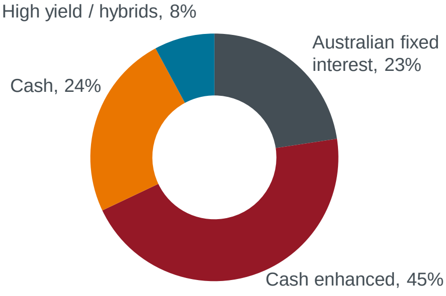
APIR code
IOF0145AU

ASX mFund
JHI02

Performance	1 month (%)	3 months (%)	6 months (%)	1 year (%)	3 years (% p.a.)	5 years (% p.a.)	Since inception (% p.a.)
Fund (gross)	0.55	0.92	1.79	3.10	3.62	4.31	6.17
Fund (net)	0.51	0.80	1.56	2.63	3.15	3.84	5.70
Growth (net)	0.51	0.08	0.42	-0.55	-0.19	-0.21	1.05
Distribution (net)	0.00	0.72	1.13	3.18	3.34	4.05	4.65
Benchmark	0.62	0.60	1.08	1.71	3.04	3.27	4.49
Excess return*	-0.11	0.20	0.48	0.92	0.11	0.57	1.21

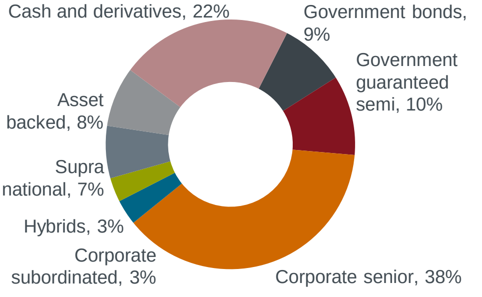
*Excess return is measured against net performance.
Past performance is not a reliable indication of future results.

Asset allocation*

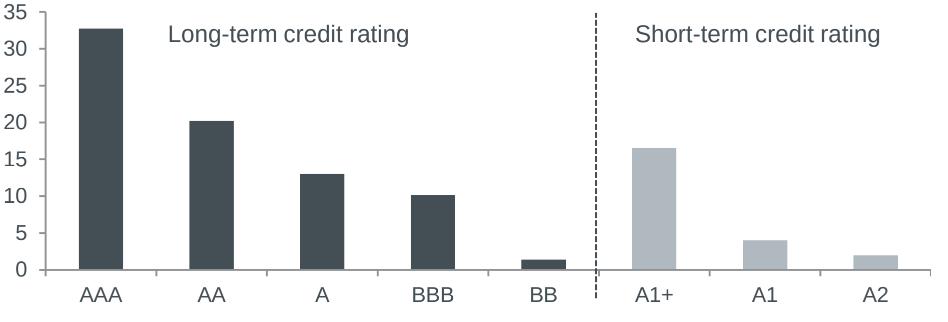


*Asset allocation shown as effective exposure of asset classes. Rounding accounts for small +/- from 100%.

Sector allocation



Credit rating distribution (%)



Portfolio characteristics

Estimated Weighted Average Yield to Maturity (EWAYTM)[1]	2.62
Benchmark EWAYTM	2.03
Weighted average credit quality	A
Number of securities (on a look through basis)	358

[1]Estimated Weighted Average Yield to Maturity is a measure of the average annual yield of all securities in the Fund.

Modified duration	Years
Fund	1.26
Benchmark	2.57
Active position	-1.31

TACTICAL INCOME FUND

(continued)

Head of Australian Fixed Interest
Glenn Feben

Portfolio Manager
Jay Sivapalan

Fund performance

Almost half of 2017's expected return from the Australian bond market was delivered to investors in October as a result of large falls in bond yields, boosting bond prices. The primary drivers included patchy data releases, including a softer than expected inflation reading locally and a lack of urgency offshore for monetary policy tightening. Money markets continued to push back the cash rate tightening profile, with the market now only priced for the first cash rate tightening to occur by early 2019 (previously by mid-2018). Yield movements, driven by market developments and the resulting volatility in bond returns, illustrates the influence that increasing interest rate risk (duration) embedded within bond markets is having on returns. Small movements in yields in either direction are able to influence returns by a greater degree. The 'risk on' tone over the month also saw non-government assets, such as corporate debt, rally further, with credit spreads narrowing.

The fall in yields provided a strong tailwind to bond market returns with the Bloomberg AusBond Composite 0+ Yr Index returning 1.09% over the month. The Janus Henderson Tactical Income Fund's (Fund) blended benchmark, the Bloomberg AusBond Bank Bill Index and Bloomberg AusBond Composite 0+ Yr Index (equally weighted) (Benchmark) returned 0.62% over the month.

The Janus Henderson Tactical Income Fund (Fund) returned 0.55% (gross) and 0.51% (net). Whilst moderately underperforming the Benchmark, this is a strong absolute return result given the Fund was able to participate in a part of the bond market's rally, principally as a result of interest rate strategies. The Fund's duration was managed between 1.5 years and 1.75 years for the majority of the month.

This month's relative performance is almost fully attributable to interest rate management, namely a defensive duration bias given the significant rally of the bond market. Towards the tail end of the month, the Fund's duration was reduced as bond markets moved from closer to 'fair value' to becoming gradually more fully priced, in our assessment. We have the Reserve Bank of Australia commencing a modest cash rate tightening cycle late next year, which the market is beginning to discount. Credit strategies added value, with an overweight allocation to credit in its various forms on a look through basis outperforming risk-free assets comfortably. Finally, each of the underlying funds that the Fund invests in outperformed their respective benchmarks to varying degrees, including the Australian Fixed Interest, Cash Enhanced, Cash and Diversified Credit Funds, which also contributed to performance.

Market review

Australian bond yields rallied over the month as patchy data readings and a softer than expected rise in the Consumer Price Index (CPI) led markets to push back monetary tightening expectations. Strong offshore data, a lack of tightening urgency from offshore central banks and expectations of US tax reform supported a vigorous 'risk on' tone, with domestic and global equity markets performing strongly and credit spreads continuing to tighten. Overall, the Australian bond market, as measured by the Bloomberg AusBond Composite 0+ Yr Index, gained 1.09% over October, with capital gains adding to the income return.

Both 3 and 10 year government bonds began the month on their highs before both ended the month 17 basis points (bps) lower at 1.98% and 2.67%. Unlike the previous month, domestic factors appear to have dominated market pricing with Australian yields moving in the opposite direction to US yields. The US economy grew by a stronger than expected 0.75% over the September quarter and 2.25% over a year ago, well above its 1.8% long term trend rate of growth. Despite softer prices data, markets are assigning a high probability to another tightening by the US Federal Reserve (Fed) at the end of the year. Against this backdrop, US 2 and 10 year government bond yields ended the month 12 and 4bps higher at 1.60% and 2.37%.

Domestic data readings were generally solid with business conditions easing back slightly from very high levels. Both business and consumer confidence continued to improve, suggesting that recent gains in the labour market were having a positive effect. Employment rose by a solid 19,800 over September and the unemployment rate edged down to 5.5% from 5.6%. Forward labour market indicators suggest that the rate of improvement in the jobs market (371,500 jobs added over the last 12 months) was set to moderate. Both the ANZ Job Ads and DEWR Skilled Vacancies series were flat over September.

On the outright weaker side was consumer spending data. Retail sales fell 0.6% over August against market expectations for a 0.3% gain. July's flat result was revised down to a 0.2% fall, but this weakness follows earlier strength and subsequent improvements in consumer sentiment and ongoing jobs growth which point to a modest rebound.

TACTICAL INCOME FUND

(continued)

Janus Henderson INVESTORS

Looking ahead, we see economic growth lifting from around 2.7% in 2017 to around 3% in 2018 and 2019.

The key release for the month and the one that shifted expectations the most was the September quarter CPI. Headline inflation rose by a less than expected 0.6% over the quarter and by 1.8% over a year ago. While electricity prices climbed by 8.9% and added 0.2 percentage points to the quarterly gain, this was at the lower end of expectations. Underlying inflation measures were also slightly below the market consensus, with the average of the Reserve Bank of Australia (RBA) statistical measures up 0.4% over the quarter and 1.9% over a year ago.

Against this backdrop, money market yields rallied somewhat with 3 and 6 month bank bills ending the month 2bps and 3bps lower at 1.69% and 1.88% respectively. Markets continue to see little chance of a policy move this year, with the yield on the December 2017 30-day interbank cash rate futures contract ending the month at 1.495%. Softer than expected CPI data did see a shift in tightening expectations, with markets pushing back the timing of the first tightening from August 2018 to February 2019.

Credit markets had another good month with strong investor demand in a low rate environment and expectations of US tax reform helping drive spreads tighter. The Australian iTraxx 5 Yr Index closed the month 8bps tighter at 65bps. Indicative of the underlying demand for yield was the issuance of 5 year Westpac paper which went at 82bps over swap, 30bps tighter than a similar issue in January. Other highlights included the inaugural bond deal from the recently privatised NSW energy company, Ausgrid, which was met with strong demand from domestic investors keen to add a new name to their portfolios.

Market outlook

We suspect that the most recent inflation reading and a broader questioning by central banks about the nature of the relationship between labour markets, wages and inflation means that the RBA will continue to keep policy on hold for the time being. While the global economy is enjoying a cyclical recovery with further narrowing in output gaps, the RBA has already indicated that a rise in global rates has no automatic implication for domestic policy settings.

Even though inflation data was on the lower side of expectations, the scope for further policy easing remains remote given the RBA's concerns about financial stability and its flexible timeframe for reaching its inflation objective. Furthermore, the considerable divergence in the inflation data between tradeables and non tradeables inflation will give the RBA pause for thought. While earlier currency strength and lower fuel prices are depressing tradeables inflation, the yearly rate of non-tradeables inflation lifted to just over 3% in the latest CPI. Although early days, the latter is indicative of some tightening in labour market conditions or ability of firms to pass on higher costs.

Looking ahead, we see economic growth lifting from around 2.7% in 2017 to around 3% in 2018 and 2019. Against the backdrop of solid major trading partner growth and with public infrastructure work yet to be done at around 6% of nominal GDP, the economy is reasonably well placed to manage the end of the most recent housing boom. Consumption growth is expected to grow at a moderate pace and net exports are set to benefit from further expansions in LNG export capacity.

While the RBA has time on its side, we agree with the Governor that the next move in rates will be up. Our base case view remains for an initial burst of 50bps of tightening between November 2018 and February 2019. Thereafter, we look for the RBA to pause and follow up with another burst of 50bps of tightening over 2020 if the growth and inflation outlook unfolds as expected. We suspect that against the backdrop of large stocks of debt being held by the household sector, the neutral cash rate sits around 2.7% rather than the RBA's estimated 3.5% level.

Consistent with our expectations for a modest and drawn out tightening cycle, we see fair value for a 3 year Australian government bond in the 2.05% to 2.10% range. At the time of writing, the 3 year Australian government bond was yielding 1.98% and we would regard any rallies from current levels as offering a potential opportunity to move towards more defensive interest rate strategies given the underlying momentum in both the global and domestic economy.

At the longer end of the curve, we see 10 year Australian government bond yields (at the time of writing) at around 2.67% as being at the expensive end of our fair value range. While structural factors should limit the extent of any sell-off at the longer end, investors also need some compensation for the risk that given current pro-cyclical policy settings, inflation may turn out to be higher than expected. Furthermore, as central banks begin to taper their asset purchase programs and/or reduce the size of their balance sheets, a force holding down yields at the longer end will be subsiding. We would see further rallies from current levels as an opportunity to move towards more defensive interest rate strategies.

TACTICAL INCOME FUND

(continued)

Janus Henderson INVESTORS

Given our assessment that credit markets are entering a mature phase in the cycle, we continue to allow exposures to investment grade credit to drift lower.

Investment strategy

The following is a summary of the key strategies in the Fund:

Interest rates:

As bond yields have drifted lower over October with market expectations of a cash rate tightening cycle now pushed back into early 2019 (previously commencing in 2018), our bias has been to re-introduce defensive duration strategies. At current market pricing, bond yields sit around our assessment of 'fair value' to slightly expensive. At the time of writing, duration relative to the Benchmark has been pared back and our bias is to reduce further should bond yields continue to fall.

Sector allocation:

Investment grade credit – Given our assessment that credit markets are entering a mature phase in the cycle, we continue to allow exposures to investment grade credit to drift lower. We didn't participate in a number of primary market issues as they were well bid and pricing simply was on the tighter side of 'fair value' and in some cases against relative value.

Higher yield / hybrid allocation – Over the month, allocations to this area of the market continued to drift lower. The Fund accesses high yield via its holding in the Janus Henderson Diversified Credit Fund (previously named Income Focused Fund). The Diversified Credit Fund now has the ability to gain part of its high yield exposure from global strategies such as global high yield, secured loans and emerging market corporate debt. Over October, some allocation was directed to these global high yield strategies in order to diversify away from Australian bank capital notes.

Further information
www.janushenderson.com/australia