Janus Henderson

TACTICAL INCOME FUND

Janus Henderson INVESTORS

As at May 2019

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

Investment Approach
The Fund is actively managed and designed to make tactical investment decisions between cash, longer duration fixed interest securities and higher yielding securities, through every step of the investment cycle.

Benchmark
Bloomberg AusBond Bank Bill Index and Bloomberg AusBond Composite 0+ Yr Index (equally weighted)

Risk profile
Low-medium

Suggested timeframe
3 years

Inception date
30 June 2009

Fund size
$3.3 billion

Minimum investment
$25,000

Management cost (%)
0.45 p.a.

Buy/sell spread (%)
0.00/0.00

Base currency
AUD

Distribution frequency
Quarterly

ARSN code
130 944 866

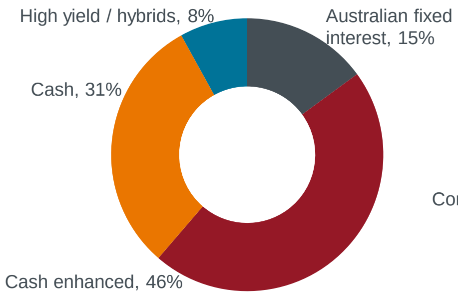
APIR code
IOF0145AU

ASX mFund
JHI02

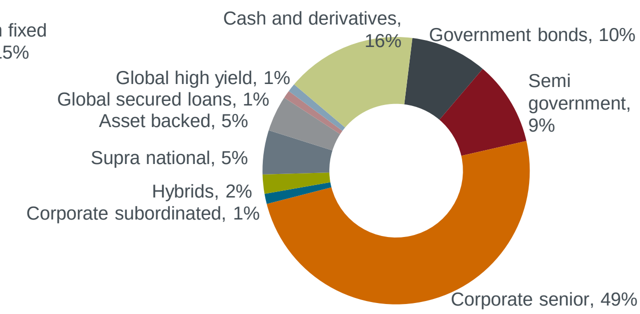
Performance	1 month (%)	3 months (%)	6 months (%)	1 year (%)	3 years (% p.a.)	5 years (% p.a.)	Since inception (% p.a.)
Fund (gross)	0.34	1.26	2.18	3.75	3.43	3.59	5.74
Fund (net)	0.31	1.14	1.95	3.29	2.97	3.13	5.27
Growth (net)	0.31	1.13	1.40	1.38	0.34	0.10	1.02
Distribution (net)	0.00	0.01	0.55	1.91	2.63	3.02	4.25
Benchmark	0.92	2.15	3.99	5.42	3.10	3.56	4.46
Excess return*	-0.61	-1.01	-2.04	-2.13	-0.13	-0.43	0.81

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

Asset allocation*

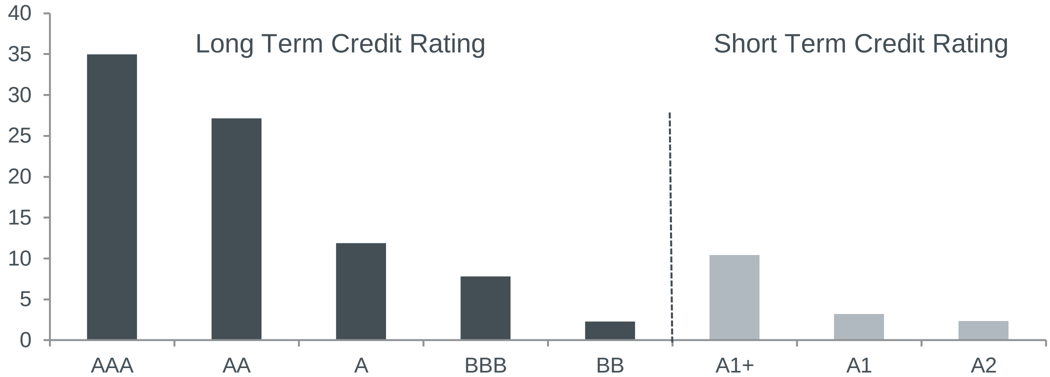


Sector allocation



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

Credit rating distribution (%)



Portfolio characteristics

Estimated Weighted Average Yield to Maturity (EWAYTM)[1]	2.00
Benchmark EWAYTM	1.49
Weighted average credit quality	AA
Number of securities (on a look through basis)	325

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

Modified duration	Years
Fund	0.56
Benchmark	2.76
Active position	-2.20

Benchmark duration is as at month end and therefore does not include rebalancing.

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(continued)

Co-Head of Australian Fixed Interest
Glenn Feben

Co-Head of Australian Fixed Interest
Jay Sivapalan

Fund performance

May was an exceptionally strong month for developed economy bond markets as fears of a global trade war escalated. Sentiment shifted decisively from ‘risk-on’ to ‘risk-off’, with equity markets falling heavily and credit spreads widening. With economic data that was generally softer than expected and little sign of inflation, markets moved aggressively to factor in the prospect of monetary easing, most notably in the US and Australia. This fuelled a significant rally in bond yields that, in Australia’s case, saw yields fall to new historic lows. Supporting this rally was a speech by Reserve Bank of Australia (RBA) Governor Lowe, where he effectively endorsed the need for further monetary easing.

The Australian bond market, as measured by the Bloomberg AusBond Composite 0+ Yr Index, gained 1.70%, with the bulk of this coming from price appreciation arising from lower yields. The Bloomberg AusBond Bank Bill Index and Bloomberg AusBond Composite 0+ Yr Index (equally weighted) (Benchmark) returned 0.92% over the month.

Reflecting the defensive interest rate stance of the Janus Henderson Tactical Income Fund (Fund), it materially under-performed the Benchmark, returning 0.34% gross and 0.31% net. With bond yields at such low levels, our performance focus remains on producing consistent, positive returns in the short-term whilst protecting investors’ capital from the negative impact of higher bond yields over the medium to long-term.

Market review

Australian government bond yields continued to rally as markets moved to price in near-term monetary easing. The longer end of the curve benefitted from flight-to-quality flows as trade tensions flared and expanded to include US/Mexico relations. Sentiment shifted from ‘risk-on’ to ‘risk-off’, with equity markets falling heavily and credit spreads widening.

Three and 10 year government bond yields drifted lower in the lead up to a speech by the RBA Governor on the outlook for the economy and monetary policy. In that speech the Governor signalled that the RBA would consider the case for lower interest rates at its June meeting. Yields subsequently rallied, with the long end boosted late in the month by the US decision to apply tariffs on Mexico. Three and 10 year government bond yields ended the month 18 and 33 basis points (bps) lower at 1.10% and 1.46% respectively.

Money market yields reacted to the RBA signalling by bringing forward the timing of the first easing to June. Three and six month bank bill yields fell by 14bps and 21bps to end the month at 1.42% and 1.41%. Markets are now fully pricing in a second easing by September and assigning around a 75% chance of a 0.75% cash rate by May 2020.

On the political side, the Coalition government defied the polls and retained government. From an economic perspective, partial demand indicators point towards another quarter of sub-trend growth in the upcoming March quarter national accounts. While net exports are poised to add to growth, a 0.1% fall in Q1 real retail sales suggest that consumption remains weak.

The labour market appears solid but forward indicators point to some moderation. Jobs rose by a stronger than expected 28,400 in April, with the participation rate climbing to a cyclically high 65.8%. However, as not all new entrants were able to find employment, the unemployment rate rose from 5.0% to 5.2%. A lift in the underutilisation rate from 13.3% to 13.7% suggests that there is still spare capacity despite 322,900 people finding employment over the last year.

Forward labour market indicators point to a moderation in labour demand, with the April NAB Business Survey consistent with employment growth of around 14,000 per month, a rate which will make it difficult for the unemployment rate to fall further. Wages growth remains moderate, with the March quarter Wage Price Index gaining 0.5% for an unchanged yearly rate of 2.3%. The Fair Work Commission announced a 3% lift in the minimum wage, down from 3.5% the previous year, but well above the prevailing rate of wages growth.

Credit markets were not immune from the ‘risk-off’ sentiment experienced in other markets, with the Australian iTraxx Index widening 13bps and finishing May at a spread of 79bps. The return of the Coalition government, as well as APRA announcing some potential easing of lending restrictions, had a muted impact on major bank credit spreads, but hybrid securities benefitted from the removal of the possible changes to franking credits. Primary markets were quiet compared to the previous month, but the one highlight was NAB issuing $1bn of new subordinated bonds at a credit spread of 215bps.

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Following the RBA Governor's speech, we brought forward the timing of our two rate cuts and now look for the RBA to move at its June and August meetings.

Market outlook

Following the RBA Governor's speech, we brought forward the timing of our two rate cuts and now look for the RBA to move at its June and August meetings. It appears as though the economy (which has slowed from above trend growth rates in the first half of 2018 to below trend rates from mid-2018 onwards) is about to get a complementary policy boost made up of:

- 50bps of monetary easing;
- a relaxation in macro prudential settings;
- tax cuts worth around 0.5% of GDP (similar impact to two rate cuts); and
- a 3% boost to the minimum wage following the latest Fair Work Commission decision.

These in aggregate provide a near term pro-cyclical pulse that should help underpin activity at a time when the housing sector is cooling. We see some merit in the RBA pausing after a June move to give it time to assess whether some of the more recent slowing had a 'deferral component' as economic agents waited to see the outcome of the election. It appears as though activity levels have picked up in key property markets and stabilisation in house prices would see an end to the negative wealth and confidence effects from falling house prices.

By bringing easing forward, the RBA have reduced the risk of having to ease more later. The growth outlook over the second half of 2019 should also benefit from a return to normal seasonal conditions and the end of the drag to growth from the completion of large LNG projects.

While we see the near-term risks tilted to the low side given current trade tensions, markets largely pricing in 75bps of easing by mid-2020 takes the shorter end of the curve to being fully-priced in our view and susceptible to any post-election pick-up in sentiment/activity and 'less pessimistic' RBA signalling. That said, with the end of the current easing cycle still a long way off, the scope for a material sell-off at the shorter end is limited.

Further out along the yield curve, we see the yield on a 10 year government bond of 1.49% (at the time of writing) as being modestly expensive, pricing in low terminal rates by historical standards and offering investors little reward for taking on term risk.

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(continued)

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Extraordinarily low risk-free yields and sound underlying fundamentals are expected to provide a strong basis for high-grade credit sectors to continue to outperform.

Investment strategy

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

Interest rates:

With Australian bond yields already priced for the RBA cash rate to fall to 0.75% later this year, they are clearly at risk of re-tracing if this fails to eventuate. As indicated, this exceeds our expectation and therefore we feel they offer poor compensation for taking duration risk. We think a best case outcome over the next 3-5 years is that Australian bonds produce returns that broadly reflect the current level of yields, which at month end stood at 1.56%, as measured by the Bloomberg AusBond Composite 0+ Yr Index. In this context, our bias is to maintain duration at current levels (0.55 years), with the potential to reduce further if yields continue their decline.

Sector allocation:

Extraordinarily low risk-free yields and sound underlying fundamentals are expected to provide a strong basis for high-grade credit sectors to continue to outperform. We remain well invested in high credit quality floating rate notes with a defensive bias as valuations had tightened and in acknowledgement that the global growth backdrop has become more uncertain. Having been largely absent from the Residential Mortgage-Backed Securities (RMBS) market over the past couple of years, a recent spate of new issuance and indications that the price decline in the housing sector may be near an end is prompting us to take a closer look at this sector. AAA rated tranches are providing a current yield of around 2.5% which looks relatively attractive when assessed against other investment opportunities. Our exposure to higher yielding credit sectors, such as secured loans and high yield debt, remain small, with no exposure to emerging market corporate debt.

Further information
www.janushenderson.com/australia