

Daintree Core Income Trust

APIR Code: WPC1963AU

Date: 10 January 2018



Investment Rating Report

Investment Rating:
Product Complexity:

STRONG
YELLOW – Complex Financial Product

Fund Details

Investment manager: Daintree Capital Management Pty Ltd

Inception: 5 June 2017

Investment structure: Unlisted Australian Unit Trust

Wholesale/Retail: Retail

Category: Global fixed interest

Investment style: Index unaware, global fixed interest

Management fee: 0.6% p.a.

Buy/sell spread: +0.05%/-0.05%

Responsible manager: Perennial Investment Management Ltd

Investment objective: The Trust aims to provide a steady stream of income and capital stability over the medium term, by investing in a diversified portfolio of fixed income and to provide a total return (after fees) that exceeds the RBA Cash Rate measured through a market cycle.

Review Summary

Strengths

- Experienced fixed income portfolio managers with a focus on active cash and credit management.
- Within the Core portfolio, the Manager has flexibility to move between cash and global fixed income securities with a target of generating 150 – 200 basis points above the RBA Cash Rate per annum
- The Manager utilises an overlay strategy that targets 30 – 50 basis points per annum. This strategy should prove to be very useful in minimising loss.
- Appropriate investment limits are in place including restrictions on taking leverage on the portfolio, currency risk exposure, sub-investment grade and the use of derivatives.

Risk Factors

- The creditworthiness of the Fund reflects the credit quality of underlying assets.
- Future dislocation in credit markets where bond prices fall may adversely impact unit value, although the manager can trade actively and the overlay strategy should provide additional protection.

Investment Rating & Product Complexity Indicator

A **STRONG** rating indicates a strong conviction that the Fund can deliver a risk adjusted return in line with the Fund's investment objective. We believe that investors will benefit from the strength of experience within the team, the flexibility of the investment process and ability to find global opportunities.

The **Product Complexity Indicator (PCI)** of **Yellow** is assigned for the Fund's units. This indicates that an investment in the Fund represents a **complex financial** investment. Monies invested in the Fund are pooled and used to purchase eligible assets on behalf of all investors in the Fund. The Manager is able to use derivatives (unleveraged) to move portfolio to reflect changes to global market conditions. The Fund will make a distribution to investors at the end of each month based on the distributable income of the Fund.

Performance & Risk Metrics*

Modified Duration (Yrs)	0.40
Spread Duration (Yrs)	3.64
Portfolio Yield (%)	3.77
Average Credit Quality	A+

Source Daintree Core Income Trust Performance Report December 2017

Fund Details

Fund name	Daintree Core Income Trust
Dominant strategy	Aim is to deliver a return of 1.5 – 2.0% (net of fees) above the RBA Overnight Cash Rate
Investment structure	Unlisted Australian unit trust
Fund category	Global fixed interest
Investment style	Index unaware, global fixed interest
Investment manager/Trustee	Daintree Capital Management Pty Ltd
Responsible managers	Perennial Investment Management Ltd (PIML)
Fund administrator	PIML
KEY FEATURES	DESCRIPTION
Fund inception	5 June 2017
Domicile	Sydney, Australia
Legal form	Retail unit trust
Geographic mandate	Global
Open	Yes
Lock-up	No
Management fee	0.6% p.a.
Performance fee	None
High Water Mark	N/A
Benchmark	RBA Overnight Cash Rate
Distributions	Monthly
FUM	A\$20 million (TBC)
Minimum subscription	A\$25,000
Subsequent subscription	A\$5,000 (or \$200 per month for a regular savings plan)
Application fee	0.05%
Redemption fee	0.05%
PRIMARY CONTACT	
Name and title	Mark Mitchell
e-mail address	mark.mitchell@daintreecapital.com.au
Telephone number	+61 419 474 016
Address	Level 27, 88 Phillip Street, Sydney NSW 2000
Website	www.daintreecapital.com.au

Investment Profile

HISTORY/BACKGROUND

Daintree Capital Management Pty Ltd (Daintree) was established in January 2017 by Mark Mitchell and is now a Perennial Investment Management Ltd (PIML) boutique asset manager. This transaction provided Daintree access to PIML's distribution, operational and compliance functions allowing the investment team to focus on managing investment portfolios.

PIML was formed in 2000 by John Murray and is now a joint venture between senior staff and IOOF. PIML manages approximately A\$5.0 billion on behalf of institutional and retail clients.

OBJECTIVE

The Fund is to provide a steady stream of income and capital stability over the medium term, by investing in a diversified portfolio of fixed income securities and cash to provide returns that outperform the Reserve Bank of Australia's (RBA) official cash rate by 1.5% - 2% p.a. after fees and usual expenses, over a rolling 12-month period.

FUNDS UNDER MANAGEMENT

As at 31 December 2017 had \$20.85 million in funds under management.

INVESTMENT UNIVERSE

The Fund has a global investment universe of fixed income assets, issued exclusively in developed markets. Securities considered includes bank bills, commercial paper, term deposits, corporate bonds, bank capital securities, structured credit, investment grade sovereign bonds and credit derivatives. The manager uses a screening process to bring the global mandate to a manageable size; this screen includes investment grade credit ratings and liquidity considerations.

The number of securities in the portfolio is expected to fluctuate over time but the portfolio is expected to generally hold between 100 to 150 securities from 80 to 100 issuers.

Derivatives are used to tilt the portfolio as part of the Manager's overlay program. We believe this overlay strategy is a considerable differentiator to the Fund's peer group as it provides the ability to assist in capital protection while providing additional returns.

The following table summarises the key investment guidelines within which the investment manager must manage the assets of the fund.

Table 1- Investment Target Weightings

Guideline	Description															
Modified duration	-1 yrs to + 3yrs.															
Minimum credit rating	BB-															
Minimum average weighted credit quality	A-															
Concentration limits to single issuer	<p>The table below details the total cumulative credit exposure to any single obligor and the maximum amount the portfolio can hold for different classes of security:</p> <table border="1"> <thead> <tr> <th>Issuer rating (internal)</th> <th>Asset allocation range</th> <th>Maximum exposure per issuer</th> </tr> </thead> <tbody> <tr> <td>AAA/AA+/AA/AA-</td> <td>0 – 100%</td> <td>10%</td> </tr> <tr> <td>A+/A/A-</td> <td>0 – 100%</td> <td>5%</td> </tr> <tr> <td>BBB+/BBB/BBB-</td> <td>0 – 50%</td> <td>3%</td> </tr> <tr> <td>BB+/BB/BB-</td> <td>0 – 10%</td> <td>1%</td> </tr> </tbody> </table>	Issuer rating (internal)	Asset allocation range	Maximum exposure per issuer	AAA/AA+/AA/AA-	0 – 100%	10%	A+/A/A-	0 – 100%	5%	BBB+/BBB/BBB-	0 – 50%	3%	BB+/BB/BB-	0 – 10%	1%
Issuer rating (internal)	Asset allocation range	Maximum exposure per issuer														
AAA/AA+/AA/AA-	0 – 100%	10%														
A+/A/A-	0 – 100%	5%														
BBB+/BBB/BBB-	0 – 50%	3%														
BB+/BB/BB-	0 – 10%	1%														
Allowable instruments	<p>Allowable instruments:</p> <ul style="list-style-type: none"> • 11 am Cash • Bank Bills • Bank Negotiable Certificate of Deposits • Commercial Paper • Sovereign, Semi-Government and Supranational Bonds • Interest Bearing Deposits • Corporate Debt Securities (Fixed and Floating) • Hybrid securities • Asset Backed Securities • Mortgage backed Securities • Other Structured Credit Securities (CLO, CDO, CBO) 															
Derivatives	<p>Allowable derivatives:</p> <ul style="list-style-type: none"> • Exchange Traded Options • Futures Contracts • Forward Rate Agreements • Interest Rate Swaps • Credit Default Swaps (Single names or indices) • Over the Counter Options • Swaptions • Inflation Swaps • Cross currency swaps • Currency Forwards <p>All long derivatives must have either cash backing or short dated securities maturing prior to contract expiry.</p>															
Currency hedging	AUD exposure 95-105%															

Currently the Fund has a modified duration of 0.4 years with a Portfolio Yield of 3.77% and an Average Credit Quality of A+ and with a high weighting to Australian issued securities.

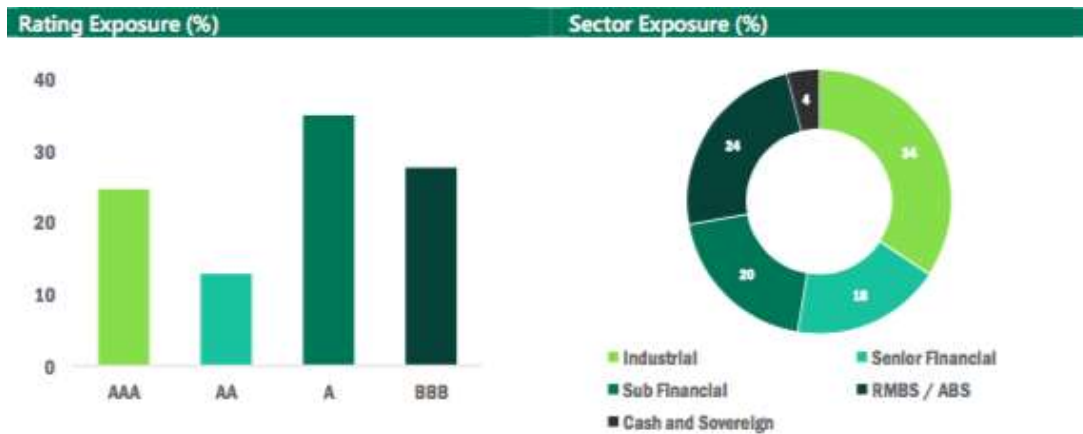
The proportion of cash and equivalents is 4%. The monthly distributions since inception (except for the first month) has been 0.15% and the Manager expects this to continue until at least May 2018.

ASSET SELECTION

As at 31 December 2017, the Fund had assets totalling \$20.85 million.

Fund Composition table illustrates the distribution of rating exposure of the Fund and the industry exposures within the portfolio

Fund Composition



Source: Daintree as at 31 December 2017

The overall credit quality of the portfolio since inception has been consistent with the guidelines of the Fund

Investment Philosophy

Daintree believes that financial markets are not completely efficient and sometimes they are driven by short to medium term irrational influences. The Manager applies a disciplined fundamental investment process that it believes allow it to take advantage of assets that it finds are mispriced. The Manager recognises that the fixed income markets globally are highly interrelated and believes that it is possible to reduce portfolio risk and enhance returns through diversified overlay strategies.

Investment Strategy

The Trust Manager manages the Fund with two portfolios; Core and an Overlay.

The Core portfolio invests in a diversified portfolio of predominantly global investment grade credit securities which meets Daintree’s investment standards. In managing the portfolio, Daintree applies a range of strategies that include duration management, (actively managing the maturity profile of the portfolio), sector rotation and individual security selection. All securities must carry a Standard & Poor’s rating (or equivalent) of BB- or higher at the time of purchase. The core portfolio targets a return of 150 – 200 basis points above the RBA Overnight Cash Rate on an annualised basis

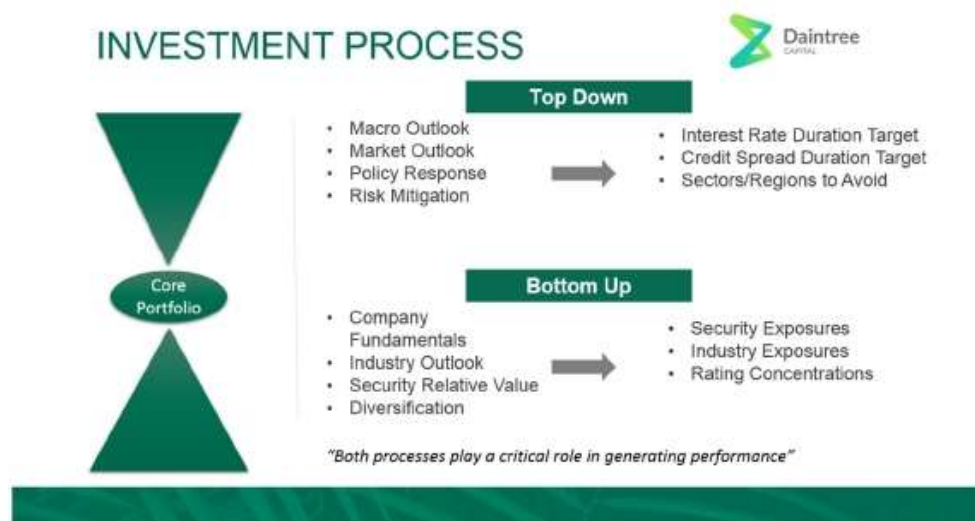
Derivatives may be used within the Overlay portfolio, for investment and risk management purposes, subject to the explicit restriction that they cannot be used to gear the portfolio exposure. The Overlay, acts not only to mitigate risk but also is expected to generate 30 – 50 basis points per annum.

The Trust invests in non-Australian denominated securities which may be fully or partially hedged back to the Australian Dollar.

Investment Process

For the Core Portfolio, the Manager applies a top down and bottom up investment process approach that considers macro-economic, market and central bank policies as factors that lead to the Manager to set duration and credit spread duration targets. This top down approach also guides the Overlay Portfolio. The top down factors are formally reset on a quarterly basis.

The bottom up process provides the Fund with individual securities, drawn from all developed market fixed income securities that pass through the Manager's filter process. Diagrammatically the Core Portfolio investment process can be represented in the diagram below

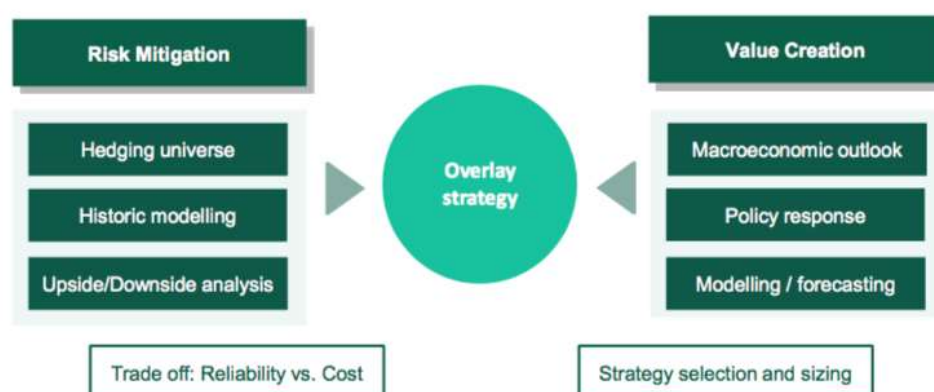


With respect to the Overlay portfolio, the Manager employs various strategies that are implemented using derivatives. The strategies used include:

- Duration, curve and other term structures;
- Inflation;
- Spread trades (cross-market);
- Momentum-based; and
- Quantitative.

The role of the Overlay portfolio is to provide add value – tilting the Core portfolio to take into account global market conditions that may be different than when quarterly top down views are decided, plus mitigating risk in the Core portfolio. Various factors are considered for both parts of this portfolio; these can be seen in the following diagram:

INVESTMENT PROCESS



For both Core and Overlay portfolios, the Manager has a demonstrated strong capability for research; at the individual credit level and at the macro level.

Credit research focus is on finding securities that demonstrates attractive risk/ return characteristics. During this process, the key considerations are default risk and potential price falls.

A credit analyst undertakes the preliminary review of the company or asset to determine its relative merits. The preliminary review process enables timely participation in new issues. A detailed review is undertaken, including the Manager's own internal rating of the security compared to issued ratings, the price of similarly rated securities within the market and a recommendation. The resultant report is presented to the credit committee. The asymmetric payoff structure of bonds means there is limited upside in trying to pick winners. Rather, the Manager seeks to find borrowers where there is a high degree of confidence that the principal will be repaid.

New issuers are also reviewed by the credit committee. If any concerns that were not uncovered in the preliminary review are subsequently uncovered as part of the credit committee process, such that risk/return characteristics are different than initially thought, the security may be sold down. However, the Manager states that this is extremely rare.

Credit analysts use a number of sources; including rating agencies, brokers, company representations and filings and third-party research. The output is a rating of both the issuer and the security and an estimated loss in the event of default for a security. Once an issuer is approved for inclusion within the portfolio, the credit analyst continues to monitor the issuer for any changes to its credit profile.

Economic and market research focuses on qualitative assessment of growth and inflation in developed economies; with a view to forecasting monetary policies. The Manager prepares a weighting of bullish, bearish and a current scenario with the aim to assess future market interactions. Forecasts are monitored daily, but formally set on a quarterly basis.

The Core portfolio seeks to have an average credit rating of A+ and to be diversified across issuers, sectors and regions. For a security to be added it needs to ensure that the portfolio constraints are not breached and to be additive to the portfolio from a risk return perspective.

With respect to the Overlay portfolio, the Director, Interest Rates and Currency is primarily responsible, however other team members can provide insights. The economic and market research is an important tool for developing ideas. A likely response to such research is that there are short to medium term anomalies within a market that changes the risk/return expectations. Mostly the Overlay portfolio is expressed using derivatives. The selection and timing of strategies is the prerogative of the Portfolio Manager.

Investment Team

The team has two portfolio managers, and three full-time analysts. It is the strength of the investment team and the portfolio managers in particular that provides confidence to Australia Ratings' assessment.

PORTFOLIO MANAGERS

MARK MITCHELL, Portfolio Manager & Director – Credit

Mark Mitchell established Daintree Capital in January 2017 and has over 23 years' industry experience both in Australia and the USA, specialising in fixed income securities analysis and portfolio management.

Prior to establishing Daintree Capital, Mark was the Head of Credit and Portfolio Manager for over seven years at Kapstream Capital. There, he was ultimately responsible for the development and implementation of the credit research processes and portfolio management until the time he left in October 2015. Over this time, Kapstream grew from \$350m to over \$10bn in assets under management. Prior to his time at Kapstream, Mark was a Portfolio Manager/Senior Credit Analyst specialising in global credit securities at Colonial First State Global Asset Management between March 2001 and September 2008.

Before moving to Australia, Mark achieved nearly a decade's work experience in the USA across a range of sectors including high yield, bank loans, commodities, futures and listed equities.

Mark holds a Bachelor of Science (Finance) from DePaul University (Chicago) and is a CFA Charterholder.

JUSTIN TYLER, Portfolio Manager & Director - Interest Rates & Currency

Justin Tyler is a founding partner of Daintree Capital and joined the firm in May 2017. Justin is responsible for interest rate and currency decisions at Daintree.

Justin has over 17 years of experience in the industry. Justin is a specialist in Inflation and Interest Rates. Prior to his current place of employment, Justin has spent over 10 years specialising in fixed income analysis and investment banking. Justin is a CFA Charterholder. He also holds a Graduate Diploma in Applied Finance and Investment from the Securities Institute of Australia.

There is also support from 3 full-time credit research and quantitative analysis professionals.

Risk Management and Compliance

The Responsible Entity has the primary responsibility for monitoring compliance by the Investment Manager with the Fund's PDS and Investment & Governance Mandate. Compliance with the Investment Mandate is also achieved through pre-trade and post trade monitoring by the compliance department at PIML, as well as post-trade monitoring by the custodian

The Responsibility Entity has a compliance committee and a dedicated compliance manager.

Detailed compliance procedures are in place which include notification of significant events or breaches to the compliance committee and the Board, notification requirements, compliance reviews, risk management checklist and audit requirements. The Fund's assets are independently valued on a daily basis by the Fund Administrator.

Risk management is core to the investment process and to the philosophy of the Manager. As would be expected there are appropriate risk tools and procedures to manage not only credit risk but also derivative and counterparty risk.

Performance

The Fund has, in its short history consistently outperformed: its benchmark, which is the RBA cash rate plus 1.5% per annum after fees and its peer group.

Performance	Three Months	Six months
Performance After Fees (%)	0.94	1.80
RBA Cash Rate (%)	0.38	0.80
Relative Performance to RBA Cash Rate (%)	+0.56	+1.00
Performance Before Fees (%)	1.09	2.15
Distribution Return	0.45	0.80
Growth Return	0.64	1.35

Source: Daintree Core Income Trust Performance Report December 2017

Transparency & Reporting

The Manager has provided Australia Ratings with the required information in a transparent fashion. Investors receive monthly performance reports and annual audited financial statements.

Third Party & Service Advisors

Fund administrator	Perennial Investment Management Limited (PIML)
Custodian	National Australia Bank Limited
Auditor	KPMG
Portfolio software	Bloomberg AIM

Information Sources

- Daintree FSC due diligence questionnaire
- Product Disclosure Statement (PDS) May 2017

Investment Rating Scale

The Australia Ratings Analytics' investment rating is an opinion on how well we believe a fund will perform against a range of risks.

Rating	Definition
Superior	Indicates the highest level of confidence that the fund can deliver a risk adjusted return in line with the investment objectives of the fund.
Very Strong	Indicates a very strong conviction that the fund can deliver a risk adjusted return in line with the investment objective of the fund.
Strong	Indicates a strong conviction that the fund can deliver a risk adjusted return in line with the investment objective of the fund.
Competent	Indicates that the fund may deliver a return in line with the funds relevant benchmark.
Weak	Indicates a view that the fund is unlikely to deliver a return in line with the investment objective of the fund and/or meet the returns of its benchmark.

Product Complexity Indicator

A Product Complexity Indicator (PCI) highlights the complexity of an investment by its terms and conditions' structure and transparency that may affect the investor's return.



Credit Rating & Product Complexity Methodology

Australia Ratings Analytics' methodology for its investment rating and research can be downloaded from its website.

Contact details

Daniel Liptak, Director

Email: daniel.liptak@australiaratings.com

Australia Ratings Analytics

Level 2, 420 Collins Street, Melbourne Vic. 3000

Telephone: (03) 8080 6684

Web: www.australiaratings.com

Disclaimer

This report has been prepared by Australia Ratings Analytics, Australian Financial Services Licence no.494552 (Licensee). Except to the extent that any liability under statute cannot be excluded, the Licensee, its employees and authorised representatives do not accept any liability for any error or omission in this report or for any resulting loss or damage suffered by the recipient or any other person. This report is for information purposes only. It is neither an offer to sell nor a solicitation of any offer to purchase any securities in any company, in particular Daintree Core Income Trust, should not rely on this document. Any investment involves a high degree of risk. All opinions and views expressed constitute judgment as of the date of writing and may change at any time without notice and without obligation. Such information may be based on certain assumptions and involve elements of subjective judgment and analysis. Actual results may differ.

This material is intended for information purposes only and does not constitute investment advice, or a recommendation or an offer or solicitation to purchase any fund or company securities, in particular those of Daintree Core Income Trust. There has been no independent review of the information presented in this report. This report is private and confidential and is intended exclusively for the use of the person to whom it has been delivered by Australia Ratings Analytics. This report does not constitute an offer to sell or a solicitation to invest in any jurisdiction where the offer or sale would be prohibited or to any person not possessing the appropriate qualifications.

This report is not to be reproduced or redistributed to any other person without the prior written consent of Australia Ratings Analytics. Australia Ratings Analytics receives payment consideration to undertake research reports. Australia Ratings Analytics does not have an interest in the securities of Daintree Core Income Trust discussed in this report.

Financial Services Guide

A copy of the Australia Ratings Analytics' Financial Services Guide can be obtained at www.australiaratings.com/fsg. A copy can also be provided by calling (03) 8080 6684.