

Aberdeen Standard Inflation Linked Bond Fund

Monthly factsheet - performance data and analytics to 31 March 2019



Investment objective

To provide investors with a level of long term protection against inflation. This is achieved through value added active investment in a quality diversified portfolio of primarily Australian inflation linked bonds and annuities. The Fund aims to outperform the Bloomberg AusBond Government Inflation Index 0-10 Yr Index over the suggested investment time frame (3 years plus).

Investment strategy

To aim to consistently add value by managing interest rate risk, choosing the best securities based on relative value and adjusting credit exposure to sectors and individual securities.

Performance (%)

	1 Month	3 Months	1 Year	Per annum		Since Inception ¹
				3 Years	5 Years	
Aberdeen Standard Inflation Linked Bond Fund net returns ²	0.47	1.70	3.55	2.16	3.19	6.89
Aberdeen Standard Inflation Linked Bond Fund gross returns ³	0.50	1.79	3.92	2.53	3.56	7.23
Bloomberg AusBond Government Inflation Index 0-10 Yr Index	0.94	2.18	4.24	2.52	3.46	6.88
Net returns ² vs index	-0.47	-0.48	-0.69	-0.36	-0.27	0.01
Gross returns ³ vs index	-0.44	-0.39	-0.32	0.01	0.10	0.35

1. This figure represents the annualised performance of the Fund from the first full month of operation.

2. Net performance figures are calculated using end-of-month exit prices, post standard fees, reflect the annual reinvestment of distributions and make no allowance for tax. If investing through an IDPS Provider, the total after fees performance returns of your investment in the Fund may be different from the information we publish due to cash flows specific to your portfolio and any fees charged by the IDPS Provider.

3. Gross performance figures are calculated using end-of-month exit prices, pre-fees, reflect the annual reinvestment of distributions and make no allowance for tax. These returns are provided for the purpose of wholesale investors only. Retail investors should refer to net returns.

Please note: Prior to 1 May 2009 the Fund was known as the Credit Suisse Inflation Linked Bond Fund.

On 1 July 2012 the benchmark for the Fund changed to the UBS Government Inflation Index (<10 years). Prior to 1 July 2012 the benchmark for the Fund was the UBSA Government Inflation Index.

On 29 September 2014 the benchmark was renamed due to the acquisition of UBS Australia bond indexes by Bloomberg Indexes.

Past performance is not a reliable indicator of future results.

Performance review

The Fund returned 0.50% in March (before fees), underperforming the benchmark by 0.44%.

Another month of strong absolute performance, but in relative terms the Fund fell behind the benchmark. The preference for inflation-linked securities against nominal bonds detracted from performance, as did positioning for higher yields. Over the month, both global yields and Australian implied inflation expectations fell as a pessimistic scenario was priced in. This is in stark contrast to equity markets and risk assets in general, which have retraced almost all the underperformance experienced over the fourth quarter of 2018. We see lower probability of a global recession and local disinflationary risk, and as such see value in holding inflation protection. We also used lower yields as an opportunity to reduce interest rate sensitivity in the portfolio.

Credit strategies were a negative for Fund performance over the month. Spreads to equivalent government bonds widened on most linker credit, with the biggest underperformer the JEM Southbank 2035's.

Market review

The recent dovish turn of global central banks resulted in some peculiar movements in asset prices

Sector holdings (%)

	Fund
Cash & Cash Equivalents	4.01
Government	61.01
Semi Government	9.34
Corporate	26.19
Supra/Sovereign	0.00
Financials	8.79
Non-Financials	11.16
Asset-Backed	6.24
CDS	0.00
Swaps	-0.55

Figures may not always sum to 100 due to rounding.

Interest rate exposure profile

	Modified Duration Contribution
0 - 6 Years	2.78
6 - 10 Years	1.57
10 - 15 Years	0.27
15 plus	0.00

Credit rating profile (%)

	Fund
AAA	76.86
AA	4.93
A	14.21
BBB	0.00
<BBB	0.00
A-1+	0.00
Cash	4.00

Figures may not always sum to 100 due to rounding.

Yield to maturity (%)

	Fund
Yield to Maturity (%)*	0.84

* Real yield that excludes expected inflation accrual

Key information

APIR Code	CRS0008AU
Benchmark	Bloomberg AusBond Government Inflation Index 0-10 Yr Index
Date of launch	July 1994
Income payable	30 June and 31 December
Management costs	0.48% pa of the net asset value of the Fund comprising: Management Fee 0.36% pa Indirect costs 0.12% pa
Buy/Sell spread	+0.15%/-0.25%
Fund size	A\$50.30m
Redemption unit price	\$1.0300

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during March; while bond markets focused their energy on the downside economic developments, risk assets reverted to the quantitative easing (QE)-era playbook of 'climbing the wall of worry'. The S&P 500 stock index increased by 2% while Chinese A shares jumped more than 4%. At the same time, interest rate volatility spiked as 10-year US and German bond yields fell by 0.31% and 0.25% respectively, delivering handsome returns to bondholders. This is what it sounds like when doves cry.

Yield curves flattened as Chinese PMIs (Purchasing Managers' Indices) remained sub-50, with the official manufacturing PMI coming in at 49.2 while the US manufacturing PMI fell from 54.9 in February to 53.0 in March – the lowest level since June 2017. Closer to home, Australian business confidence took a dive to -0.4 in March after a decent run of good vibes. 3-year Australian government bonds, which had been trading north of 2% as recently as December 2018, plummeted from 1.63% to 1.39% during the month as an increasing number of economists called for multiple interest rate cuts from the Reserve Bank of Australia (RBA).

Despite the stark fall in yields, credit spreads were very well behaved. US and Australian investment grade corporate credit returned around 0.3% over government bonds, so total returns were very strong at 2.5% and 1.5% respectively (the difference in total returns is principally due to the longer duration of the US investment grade corporate bond index). US high yield credit underperformed government bonds by 0.25% as spreads widened by around 0.13% – an interesting observation given the general risk-on tone. While it is obvious that the high yield universe is more acutely exposed to a slowdown in economic growth, it isn't very often that equities and high yield diverge to this degree.

The fall in all-in yields saw many global corporates rush back to the new issue market in the US, Europe and across Asia, but things remained a little quieter in Australia. Local issuance was dominated by state government and supranational entities, while a handful of corporates got involved. Chemicals-and-explosives player Incitec Pivot issued A\$450m of 7-year bonds with a coupon of 4.3%, while Stockland and Dexus defied the negative news about the local property market to issue bonds at respectable credit spreads. In the unrated space, Peet Ltd issued A\$75m of 5-year bonds at a coupon of 6.75%.

Outlook

We retain high conviction that the Australian economy will emerge unscathed from the various self-inflicted problems it has been navigating across housing, lending, and politics. However, the extended slowing in household income will weigh on activity in the near future and likely delay the timing of monetary tightening indefinitely. Furthermore, the risk that the RBA may have to cut rates has increased and depends on the trajectory of the global economy more so than the wealth effect from housing. Our outlook for employment is sufficiently positive to keep the unemployment rate steady, and with the labour market sitting at full capacity and wage growth slowly trending higher the RBA is likely to remain comfortably on hold with a neutral stance.

The US is in a state of flux, caught between a slowdown in activity from lofty levels and the risk of accelerating wage growth. A previous government shutdown, an unconvincing suspension in the trade war with China and generally stratospheric levels of policy uncertainty are also beginning to be felt in the survey data. Adding to that, our adjusted Phillips curve foreshadows a build-up in inflationary pressures in the months ahead. However, the risk is that deteriorating business sentiment will constrain investment and jobs growth sooner than wage pressures can build. We forecast a limited slowdown in our central case and see a recovery in the offing, as households and corporate USA have resilient balance sheets with which to navigate the current soft patch. In contrast to market expectations we forecast scope for an additional increase in the Fed funds rate later this year and in the meantime a highly data-dependent Fed China on the other hand is in the midst of activating stimulus—largely through infrastructure investment—that has not been sufficient to offset slowing in the manufacturing sector. The Eurozone awaits a rebound after various temporary factors clouded the signal-to-noise ratio in the economic data. The ECB is in the process of revising its outlook to upgrade the downside risks and in our assessment will also re-ignite targeted longer-term refinancing operations (TLTRO).

Credit endured an exceedingly tough 2018 and started 2019 at attractive valuation levels relative to the last few years. However, we do not believe that 'the last few years' is the optimal yardstick for assessing relative valuation in 2019 as these years encompassed globally-coordinated quantitative easing from major central banks and record low yield and credit spread levels, and as a result artificially suppressed default rates. We now have a Fed funds rate in the mid-2s that not only impacts core global yield levels (and in turn refinancing rates for corporates) but also the hedging costs for the large overseas buyers of US investment-grade credit that drove 2017s issuance boom. Global economic growth has slowed and our expectation is that US corporate earnings will continue to meaningfully decelerate in 2019. Taking these factors into account, valuations could best be described

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as fair, but the recent rally in spreads is starting to make this harder to justify. We continue to believe that approaching credit from a 'sell the rally' angle makes more sense than the 'buy the dip' mantra that was so powerful in 2016 and 2017. For these reasons, we will continue to dynamically dial up/down our active credit position with liquid instruments, while maintaining a greater proportion of higher-quality credit in funds (we have increased our allocations to AAA-rated state government and supranational bonds). Ultimately, given we expect default rates to stay low, a degree of credit overweight is warranted but at reduced scale.

Important information

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