Elstree
HYBRID FUND (EHF1)

INVESTMENT UPDATE   FEBRUARY 2022

Welcome to the latest Elstree Hybrid Fund (EHF1) Newsletter.

Returns

Elstree Hybrid Fund (Chi-X: EHF1) produced a return of 0.21% in February, 0.02% better than the market return of 0.19%. Since the fund was quoted on 31 March 2021, it has returned 4.7% (after fees, including franking) which is above the benchmark return of 3.9%.

Returns of the Fund, the Elstree Hybrid Index and Bank Bill/Term Deposit returns are summarised in the performance table below.

Performance figures as of 28 February 2022:

Performance as of 28 February 2022	1 MONTH	3 MONTHS	1 YEAR (p.a)	3 YEARS (p.a)
ELSTREE HYBRID FUND NAV + FRANKING (EHF1)*	0.2%	0.8%	5.5%	
ELSTREE HYBRID INDEX (P.A.) **	0.2%	0.7%	4.4%	5.5%
BANK BILLS	0.0%	0.0%	0.0%	0.6%

* Elstree Hybrid Fund (EHF1) Investment Performance is returns after fees and after the value of franking credits.
** Elstree Hybrid Index include the value of franking credits and has no fees

Top Holdings & contributors to returns:

Security	Return contribution	Security	Return contribution
CWNHB	0.07%	NABPH	0.03%
CGFPC	0.04%	WBCPJ	0.02%
RHCPA	0.04%	ANZPI	0.02%

Market Commentary

There was a lot happening in investment markets in February: we had the collision of fears of non-transitory inflation, the bringing forward of expectations of cash rate increases for both the US and Australia, and Russia invaded Ukraine.

Most investment market participants would have expected weaker equity markets and stronger bond markets , but we saw the opposite. In general, investment markets are ignoring the Ukraine tragedy and all the headlines. Bond markets posted negative returns (higher inflation leads to higher interest rates, but they don't care about Ukraine as a permanent influencer) and equity markets were stronger (they think that the Ukraine chaos won't last long).

Hybrid markets were not that different: the 0.2% return was around income levels and there was little volatility during the month.

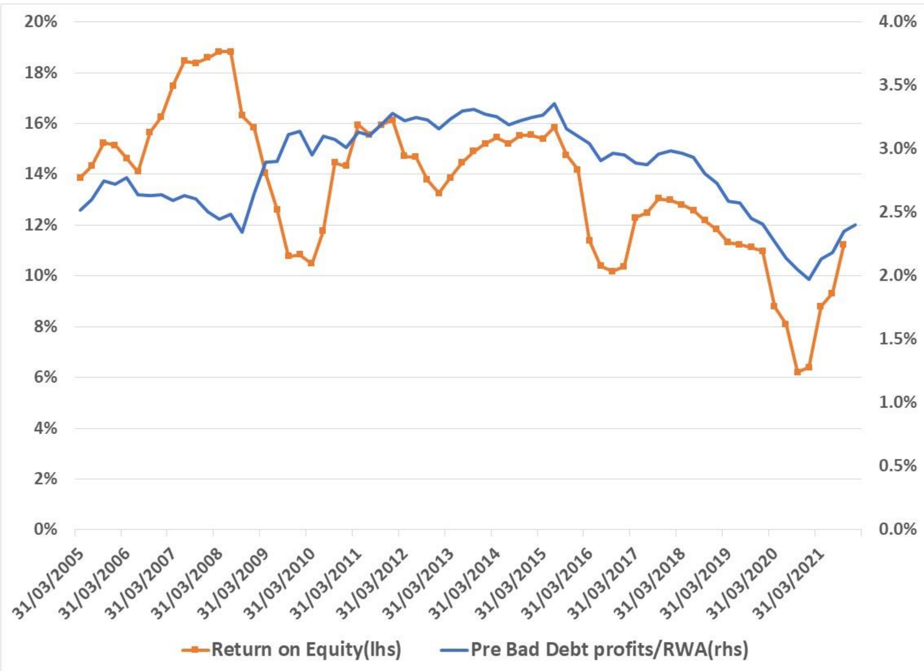
The most notable events were the two new hybrid issues by ANZ and CBA. These were the first major bank hybrid issues which took place under the DDO regulations which limit the ability of some investors to access the IPO. DDO turned out to be a non-event. Both issues were heavily oversubscribed with most investors getting allocations of around 20% of what they bid for. It's clear that investors are still voting with their wallet and with Term Deposit rates still around 0.25%,they are willing to take additional risk to achieve a higher yield.

Bank Reporting season: a Hybrid perspective

Hybrids have more risk than bank deposits and bonds and most of that relates to the risk that a bank becomes "non viable" or even "less viable". Currently, Australian banks are further away from "non viability" or "less viability" than they have ever have been. They are in super condition and that lessens the risk of adverse events affecting hybrids. The latest round of quarterly results continues the improvement of the underlying banks seen since Covid (and even then they didn't lose money).

Profitability

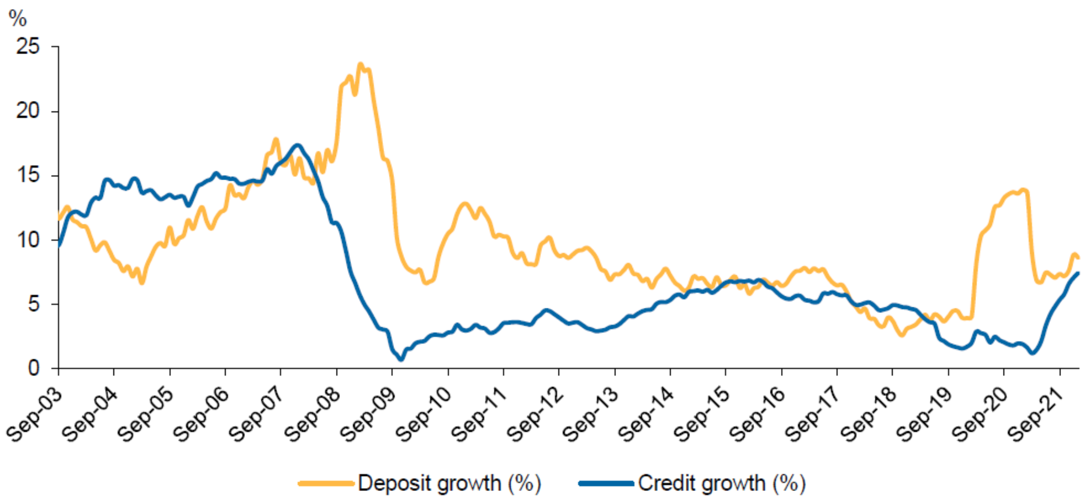
The chart below shows two profitability measures for the 4 major banks: Return on Equity and Pre provision profits as a % of Risk Weighted Assets (RWA). Australian banks are amongst the most profitable in the world and RoE's of >10% and Pre provision profits of >2% mean that bank equity is readily replaceable either through organic profit generation or new investors wanting to buy a slice of the quad-opoly (ANZ, CBA, NAB, WBC).



Funding

The only Achilles Heel of Australian banks used to be that they needed to borrow material amounts from international overseas borrowers where there is much greater funding risk compared to deposit funding. The banks have spent the last decade growing the proportion of deposit based funding. The chart below (source Macquarie) shows the trend with deposit growth outstripping lending growth for all but 1 of the last 13 years. The result now is that it looks like the banks have over $300b of excess deposits on their books. They are looking bulletproof.

Fig 8 Deposit growth vs credit growth (YoY%)



News & Media

Elstree Hybrid Fund (EFH1) has been mentioned in the following articles throughout the last six months, many of which are educational in nature.

livewire

- How Hybrids fit into 2021 Income Portfolios – Campbell Dawson I Elstree Hybrid Fund
- The Hitchhiker's Guide to Hybrids (Part 1) – Bella Kidman I Livewire Markets
- This is the secret to a diversified portfolio (Part 2) – Bella Kidman I Livewire Markets
- The forgotten asset class presenting exciting opportunities – Bella Kidman I Livewire Markets

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Firstlinks
a Morningstar company

- Fascinating Hybrid Journey Last Year – Campbell Dawson I Elstree Hybrid Fund

FINANCIAL STANDARD

- New Hybrid ETF on Chi-X – Staff Reporter I Financial Standard

MONEY|MANAGEMENT

- Support for Elstree Hybrid Fund – Staff Reporter I Money Management

ADVISERVOICE
Education and information for financial advisers

- Hybrids remain attractive alternative for income generation – Evergreen Ratings

More about Elstree Hybrid Fund (EHF1)

Elstree Hybrid Fund (Chi-X: EHF1) is an Exchange Traded Product or ETP. The fund is designed to allow retail investors to access the same successful and long-term investment strategy as our actively managed unlisted wholesale fund, the Elstree Enhanced Income Fund.

The Elstree Hybrid Fund is an ideal investment for investors seeking a cash or bank term deposit alternative investment that displays an acceptable and appropriate risk adjusted return outcome.

The Elstree Hybrid Fund has 'on market' liquidity provided by a market maker (Nine Mile). The iNAV which is estimate of the live NAV, is updated every 20 seconds.

Additional details can be found on the Elstree Hybrid Fund website or email Norman Derham or Michelle Morgan for further information.