Quarterly Performance Review

u ethical Diversified Income Trust - Wholesale

Quarterly highlights December 2023

- Bank hybrid spreads ended the quarter marginally tighter across the investable universe, with an average of 0.9 in compression overall. However, spread movements were mixed across individual securities.
- Hybrid spreads widened with relatively broad increases across maturities however, by December-end spreads finished roughly in-line with levels seen at the beginning of October.
- Over the quarter, the Trust delivered a return of 0.66% (net of fees), underperforming the benchmark by -1.06%. This was attributed to negative movements in capital value.
- As 3M BBSW resets higher, increased coupon benefits in the next quarter are likely – with overall yields now ranging from 6-7%, the asset class remains attractive.

Investment objective

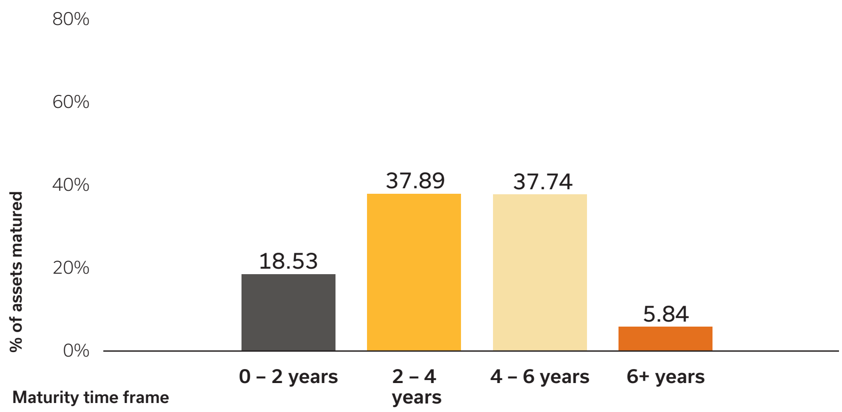
The U Ethical Diversified Income Trust - Wholesale aims to generate income in excess of short-term interest rates, while limiting harm and creating positive impact through the implementation of U Ethical's Ethical Investment Policy.

The Trust is a medium-risk investment option with a suggested minimum investment horizon of 3 to 5 years. It aims to outperform the benchmark after fees over a rolling three-year period.

Fund information

Portfolio manager	Amanda Lin
Chief investment officer	Jon Fernie
Inception date	1 July 2020
Total fund size ($M)	$39.16
Benchmark	3 Month Bank Bill Swap Rate + 2.5%
Buy/sell spread	0.20%/0.20%
Management costs	Estimated up to 0.70% p.a. (See Information Memorandum)

Maturity profile



Performance

	3 months %	6 months %	1 year % p.a.	3 year % p.a.	Since Inception % p.a.
U Ethical Diversified Income Trust - Wholesale†	0.66	3.28	2.73	3.99	4.05
Benchmark*	1.72	3.43	6.72	4.53	4.25
Relative performance	-1.06	-0.15	-3.99	-0.54	-0.20

Past performance is not indicative of future performance.

† Based on exit price with distributions reinvested, and are net of all fees
* 3 month Bank Bill Swap Rate +2.5%

u ethical

Market commentary

Global equity markets rallied over the December quarter with the S&P 500 Index rising more than 11%. Contributing to the momentum has been inflation trending lower and optimism central banks will cut interest rates in the first half of 2024. Economic growth has remained more resilient than expected with a 'soft landing' now expected for the global economy.

US core inflation remained steady in November at 4.0% and the federal funds target range has been maintained at 5.25-5.50% since July. On the back of more dovish commentary and forecasts, the US yield curve shifted down over the quarter with 10-year treasury yields dropping below 4%.

In Australia, inflation eased to 4.9% in October and remains above target levels driven by stickier services components. The Reserve Bank of Australia (RBA) increased the cash rate to 4.35% in November and next meets again in February. A tight labour market will remain a concern with the unemployment rate at 3.8%, but we are close to the interest rate peak domestically.

Corporate earnings have remained solid, although we expect more pressures to emerge as economic growth slows. While domestic consensus forecasts have declined over the last 12 months (excluding resources), globally we still see expectations as too high. Equity market valuations also look more stretched given the rally at the end of 2023.

Portfolio commentary

Over the quarter, credit spreads across major bank capital structures narrowed, with longer-dated senior and Tier-2 bonds seeing the majority of movement. AT1 spreads were mixed over the period, with widening seen in October/November and some subsequent marginal tightening in December. AT1s ultimately ended the quarter (in spread terms) roughly in-line where they began.

Broad corporate credit spreads by rating band saw divergent outcomes, with a more risk-on tone compressing BBB spreads by 8.8bps and widening AA- / AAA by ~2.21bps and 5.5bps respectively. This was in light of softening inflation prints and dovish tweaks to foreign central bank speak, showing a likely peak in global cash rates which aided sentiment toward credit risk. Overall, spreads remain elevated relative to historical levels.

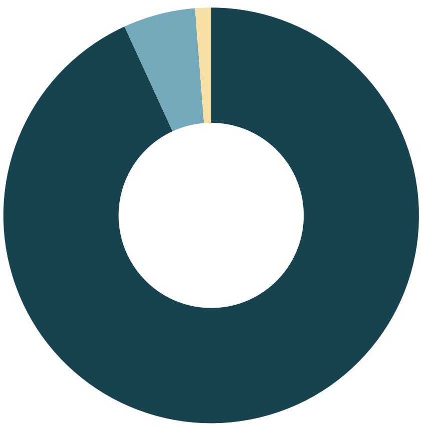
Major bank debt relative value weakened over the period, with Tier-2 floating rate margins narrowing by 15bps at the five-year tenor mark, bringing the T2/Snr Unsecured multiple down to 1.89x from the 2.08x level at the start of the quarter. This was broadly constructive for AT1 spreads given their widening seen in November and vicinity to Tier-2 debt, ultimately ending the quarter with a 0.9bp compression across the listed universe.

Over the quarter, the portfolio delivered 0.66% after fees and underperformed the benchmark by 1.06%. The absolute performance is attributed to -0.47% from capital price and 1.13% from Income.

Top 5 issuers

Top 5 issuers	%
Commonwealth Bank of Australia	37.96
Westpac Banking Corporation	23.87
Macquarie Group	12.80
Australia & New Zealand Bank Group	7.36
National Australia Bank	13.61
Total	**95.60**

Asset allocation by securities' type



	%
Capital Notes	93.41
Tier 2	4.25
Cash & Cash Equivalents	2.34
Total	**100.00**

U Ethical is an investment manager with a difference. We believe in creating a better world by investing with purpose—today and into the future.

With the creation of our first funds in 1985, we have become one of the largest ethical investment managers in Australia with over $1 billion in funds under management. We are also one of the few investment businesses in Australia to have been certified as a B Corporation. As a not-for-profit social enterprise, we grant the majority of our operating surplus to community programs.

U Ethical

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