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October 2024

Fund Review

**Janus Henderson Diversified Credit Fund**

**APIR: IOF0127AU**

FUND

The **Janus Henderson Diversified Credit Fund** (the “Fund”) is managed by Janus Henderson (‘the Manager’) and was incepted in October 2012. Janus Henderson is a global asset manager with a presence across asset classes.

The Fund is an actively managed portfolio of Australian and global higher yielding fixed interest securities that seeks to provide investors with a diversified exposure. The Manager’s approach is to determine the overall level of credit and duration risk in the Fund by taking a top-down approach, which considers trends in credit fundamentals, market dynamics and current valuations.

INVESTMENT OBJECTIVE

The investment objective of the Fund is to achieve a total return before fees that exceeds the total return of the Bloomberg AusBond Bank Bill Index (‘the Benchmark’) by 2.00% p.a. over rolling three-year periods (note the benchmark was changed in 2017 from the Bloomberg AusBond Credit FRN 0+ Yr Index).

GOVERNANCE AND COMPLIANCE

Responsible Entity

Janus Henderson (‘the RE’) is the Responsible Entity of the Janus Henderson Diversified Credit Fund. This is a related party RE and thus has the potential to lead to conflicts of interest, pleasingly there has been no adverse findings since the inception of the relationship.

Compliance

The Responsible Entity’s Compliance Committee is responsible for overall compliance as part of its function in forming long-term alliances and supporting a stable of investment management businesses.

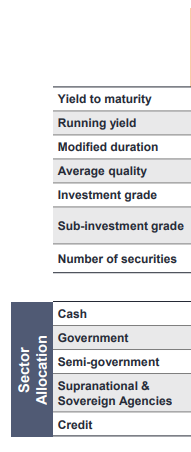
FUNDS UNDER MANAGEMENT

* Janus Henderson Firmwide AUM = $540.5bn
* Janus Henderson Fixed Income AUM = $108bn
* Janus Henderson Diversified Credit Fund AUM = $1bn

Janus Henderson is a large global manager and is responsible for a substantial amount of AUM. The manager has AUM diversified across asset classes and sub-asset classes and has grown in a sustainable manner. Additionally, the manager has a high degree of representation across client types and client locations. There are no concerns regarding business risk and FUM flow.

PRODUCT FEATURES

A close-up of a calendar

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The Fund is open to investors and available on platforms with ample capacity for investment. The total fee load of 55bps is considered reasonable and at the lower end of the peer group.

BUSINESS

Janus Henderson was founded in 1969 as an investment manager based in Denver, Colorado. Today, Janus Henderson Group PLC is a publicly traded company on the New York Stock Exchange (NYSE: JHG), boasting a market capitalisation of over $6 billion. While diluted ownership can sometimes be viewed less favorably, Atchison finds reassurance in the company's stability, with a legacy spanning over 90 years and roots tracing back to 1934.

The Australian Fixed Income business offers a comprehensive range of specialised Australian and global debt solutions, both as a manufacturer and manager. Built on a foundation of active management, the team firmly rejects passive fixed income strategies. The Australian Fixed Income desk is regarded as a well-supported and highly profitable franchise.

INVESTMENT TEAM

The Australian fixed interest team is located in Melbourne and headed by Jay Sivapalan, a seasoned professional with 26 years of industry experience and 23 years with the manager. Sivapalan is considered a highly capable and experienced leader of the team. The team consist of nine investment professionals including four portfolio managers, one macroeconomist, three analysts and an ESG specialist.

Jay Sivapalan and Shan Kwee are the dedicated portfolio managers for the diversified credit fund. Each of the nine team members brings specialised expertise, contributing insights and participating in collective decision making. However, Sivapalan holds ultimate decision-making authority, which is viewed positively as it fosters accountability compared to more diluted decision-making practices seen among peers.

Janus Henderson's competitive advantage lies in the team's ability to leverage insights from its global fixed income, equity, and alternative asset teams. This collaborative approach enables the manager to efficiently cross-pollinate ideas and perform thorough "sense checks," enhancing decision-making and creating a well-rounded investment team.

Key Person Risk

Given the collaborative nature of the process and team, key person risk is assessed to be lower than peers. However, Sivapalan is seen as the steward of both the process and team, meaning his departure would trigger a reassessment of the investment case.

INVESTMENT PHILOSOPHY AND PROCESS

Investable Universe

The Fund has a diversified and deep opportunity set across Australian, global and emerging market fixed income securities. The Fund’s credit allocation is primarily Australian senior corporate debt (roughly 60%). Global and sub investment grade credit allocations are limited to 50% of the Fund.

The Manager uses derivatives extensively to implement the investment process and decisions. Derivatives allow the manager to manage duration, hedge risks and provide a low-cost alternative to buying the underlying securities.

Philosophy

By investing in quality corporate debt, credit investing can deliver higher levels of income and higher returns than traditional defensive strategies, and at lower levels of volatility and risk of capital loss than investing solely in equities, hybrids, loans or high yield securities may offer.

The Manager believes active management of credit can add robust and repeatable risk-adjusted returns for investors seeking a consistent income stream.

Idea Generation & Research Process

The team takes a highly active approach to asset allocation and sector rotation within fixed interest credit markets, placing a strong emphasis on macroeconomic outlook. This top-down assessment of economic, credit and market conditions drive the idea generation and research process.

The research process is divided into three key components: quality, capital preservation, and value. The manager conducts an internal credit quality assessment on specific issuers, evaluating factors such as industry and financial risk, management strength, and ESG considerations. If an issuer passes this assessment, it is added to an approved list, becoming part of the investment universe available for analysts. From this list, analysts perform a detailed credit valuation, analysing various risk components to determine a fair value for potential investments. Securities that meet all the criteria—quality, capital preservation, and value—are included in the portfolio when they align with the team's current sector allocation. This ensures that investments are not only fundamentally sound but also strategically positioned within the broader market context.

The Manager’s process has a clear focus on limiting drawdowns and risk management through the in-house credit quality assessment. Given the size of the team and their ability to leverage insights from Janus Henderson's global fixed income and equity teams, the focus on top-down sector allocation within credit is seen as both pragmatic and highly adaptable to the fund’s investment universe.

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Portfolio Construction

The Portfolio is constructed in a differentiated manner, being 70% direct investment and the remaining 30% allocated as a fund of fund’s structure. The direct investment sleeve is driven by the top-down sector and allocation views and is unconstrained in terms of credit quality, although average credit rating is expected to be BBB through the cycle. The manager aims to maintain duration between zero to one.

The 30% Fund of Fund allocation is used to allocate to markets in which they do not have a clear look through. For example, they may allocate to an emerging market debt fund within Janus Henderson to achieve broader diversification. This approach is seen as pragmatic and allows for a more risk aware approach to portfolio construction. The manager will conduct a thorough due-diligence process on the funds they allocate to. They do have the ability to invest in funds outside of Janus Henderson, however, to date they have only allocated in house. There are some concerns around the exclusive allocation to Janus Funds, which could present an agency issue, however, performance to date has not elevated the concern.

Risk Management

The manager is highly risk-aware and employs an internally developed risk framework known as 'MATAR' (Maximum Adverse Total Annual Return). This framework guides asset allocation decisions and provides a disciplined approach during stressed market conditions and shifting correlations. The model encourages the portfolio to embrace greater risk when credit spreads and interest rates are high, while discouraging risk-taking when either is low.

A key focus of the assessment is to mitigate left-tail risk, which is particularly crucial for credit managers. Recognizing well-rewarded risks is essential, especially when traditional volatility metrics may underestimate potential tail risks. This proactive risk management approach helps ensure that the portfolio is better positioned to navigate adverse market scenarios. An example of this in action is through the COVID drawdowns the diversified credit fund only drew down 6% showing a much higher downside protection than peers.

All FX exposure is hedged.

PORTFOLIO CHARACTERISTICS

Portfolio Turnover

In fluctuating markets, the manager adopts a high turnover strategy, actively adjusting the portfolio. Conversely, in stable markets, a low turnover approach is utilised, maintaining positions with less frequent trading. This approach is seen as dynamic and appropriate.

Liquidity

The portfolio provides monthly distributions and daily liquidity.

Leverage

The Manager may employ leverage through derivatives; however, this is kept at a low level.

PERFORMANCE – As at 31/08/2024

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Performance Opinion

The Fund has failed to meet its performance objective of 2% outperformance over rolling three-year periods. However, pleasingly performance outcomes have been positive and above the benchmark over all time periods. This has been driven by prudent asset allocation and security selection.

The fund is expected to outperform during stable or improving economic conditions, particularly when credit spreads tighten, and the risk of defaults remains low. In such environments, the portfolio can capitalise on favourable market conditions, enhancing returns through its exposure to high-quality credit assets. In the fixed income sleeve within a model portfolio this will blend best with less credit risky strategies to help neutralise the exposure.

It should be noted that credit strategies can often exhibit a correlation with equity markets given the risk exposures they are both prone to. As such, this should be considered when applying this fund to a model portfolio. It should provide better diversification in a portfolio that has a lower growth allocation. Atchison is aware however that the degree and direction of this correlation can be influenced by several factors.

CONCLUSION

* The Fund is part of a major global business with access to fruitful resourcing. This is seen as a competitive edge allowing cross pollination of ideas and sharing of resources. It is seen as especially helpful for this fund given the reliance on top-down views.
* The Australian fixed income desk is well resourced and led by a highly capable and experienced portfolio manager.
* The process is clear, well established and time proven. The focus on capital preservation and credit assessments of each individual issuer is viewed favourably. The manager places a high degree of focus on risk management and utilises proprietary systems.
* The portfolio construction process and the utilisation of a fund-of-funds approach is differentiated and allows for a more diversified approach into more credit risky markets.
* Performance outcomes have been positive and above benchmark in all time periods. In the fixed income sleeve within a model portfolio this will blend best with less credit risky strategies to help neutralise the exposure.

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