10.3. Investment and Loan Borrowings Report as at 31 May 2025

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ATTACHMENTS	1. North Sydney Monthly Report May 2025 [**10.3.1** - 21 pages]
CSP LINK	5. Our Civic Leadership 5.1 Lead North Sydney's strategic direction

PURPOSE:

The purpose of this report is to provide details of the performance of Council's investments and loans for the month ending 31 May 2025.

EXECUTIVE SUMMARY:

- All investments have been made in accordance with the Local Government Act and Regulations and Council's Financial Investments Policy.

- For the month of May, the total investment portfolio (which includes Term Deposits, Floating Rate Notes and Bonds) provided a return of +0.33% (actual), or +3.97% p.a. (annualised), slightly under performing the benchmark AusBond Bank Bill Index return of +0.34% (actual), or +4.12% p.a. (annualised).

- Returns on investments exceed the May YTD budget by $82,720. This result includes fees paid to Council's investment adviser which total $13,500 year to date. The annual fee is $18,000.

- Investment income budget was increased by $1.2 million in the March Quarter Budget Review.

RECOMMENDATION:
1. THAT the report on Investments held at 31 May 2025, prepared in accordance with clause 212 of the Local Government (General) Regulation 2021, and the information on Loan Borrowings be received.

Background

Clause 212 of the Local Government (General) Regulation 2021, states that the Responsible Accounting Officer must provide Council with a monthly report detailing all funds invested under Section 625 of the Local Government Act 1993. This report must include certification that the investments have been made in accordance with the Act and the Regulations made thereunder, also the revised Investment Order issued by the Minister for Local Government and Council's Financial Investment Policy.

It is also prudent to report loan balances and compliance with borrowing orders issued by the Minister for Local Government and Council's Debt Management Policy.

Total Cash and Investment Balance and Reserves

The total cash and investment balances are $143,107,423 representing an increase of $6,552,278 from the previous month. Most of this balance is held in reserves to be spent on certain activities and projects. Reserves fall into one of two categories:

- external restrictions (Council is obliged by legislation, or contract, to spend the funds on certain projects and activities); and
- internal allocations (Council has resolved to spend the funds on certain projects and activities).

The following table details the reserves held. Council had an unrestricted cash balance of $17.2 million, a decrease of $4.4 million from the previous month.

While these funds are marked as unrestricted, they will be utilised in subsequent months to fund Council's activities, including salaries and wages, materials and contracts, repayment of borrowings, and other operational expenses.

As per the last approved budget, internally restricted reserves will be allocated to the North Sydney Olympic Pool project once the initially designated funds for the project are fully utilised.

External Restrictions and Internal Allocations	**May-25**
External restrictions	
Developer contributions – general	$51,675,884
Domestic waste management	$15,192,504
Unexpended Special Rates	$1,314,949
Unspent borrowings - North Sydney Olympic Pool redevelopment	$4,996,498
Specific purpose grants	$3,972,613
Other specific purpose contributions	$2,290,460
Total external restrictions	**$79,442,909**
Internal allocations	
Capital Works Reserve	$6,514,587
Community Housing - Capital Purchases	$1,010,101

External Restrictions and Internal Allocations	May-25
Community Housing - Major Maintenance	$490,657
Deposits, retentions, and bonds	$14,893,810
Employees leave entitlement	$7,127,000
Income Producing Projects	$547,982
I.T. hardware and software	$1,148,541
Olympic Pool Redevelopment	$9,717,472
Plant and vehicle replacement	$3,610,008
Bradfield Park TfNSW Lease Reserve	$785,157
Cammeray Park TfNSW Lease Reserve	$650,642
Total internal allocations	**$46,495,957**
Total Restrictions and Allocations	**$125,938,866**
Unrestricted Cash and Investments	$17,168,557
Total Cash and Investments	**$143,107,423**

Investment Portfolio

The following tables detail the performance of Council's investment portfolio (excluding cash deposits) to the benchmark for the month of May 2025 - and annualised for the year-to-date (including investments that have matured prior to that date).

	May 2025	Annualised YTD
Actual Return	0.33%	3.97%
Benchmark	0.34%	4.12%
Variance	-0.01%	-0.15%

Asset Type	Market Value	Portfolio Breakdown
Term Deposits	$108,500,000	75.82%
Cash	28,607,423	19.99%
Fixed Bonds	$6,000,000	4.19%
Floating Rate Notes (FRNs)	$0	0.00%
	$143,107,423	**100.00%**

Council's average duration of term deposits, which comprised 75.82% of the investment portfolio, is approximately 122 days. The average duration aligns maturities with the expected outflows of the capital works program.

All funds have been invested in accordance with the Act and the Regulations made thereunder. Council's investment portfolio complies with the revised Investment Order issued by the Minister for Local Government, which places restrictions on the type of investments permitted. All investments accord with Council's Financial Investments Policy.

Council continues to seek independent advice for investments and are actively managing the portfolio to ensure that returns are maximised, considering diversification and risk. A complete analysis of the performance is covered in the Monthly Investment Reports

(Attachment 1) prepared by Council's investment advisor, Arlo Advisory. The report contains advice about optimal investment options but also notes that Council's scope to act on that advice is limited by its cash flow requirements. Council has considerable requirements for short term investments and deposits at call to fund its Capital Works budget including the North Sydney Olympic Pool project.

Summary of Returns from Investments (includes Fair Value adjustments)

The actual investment returns for the year-to-date 31 May 2025 are $82,720 more than the revised year-to-date budget.

Year	Original Annual Budget	Revised Annual Budget	YTD Budget	YTD Interest	YTD Actual FV adjustment	YTD Budget to Actual Variance
2024/25	$2,534,059	$5,234,059	$4,783,083	$4,867,399	-$1,596	$82,720
Previous Years						
Year	**Original Annual Budget**	**Revised Annual Budget**		**Final Result Interest**	**Final Result FV adjustments**	**Final Budget to Actual Variance**
2023/24	$2,490,000	$5,490,000		$5,425,310	$5,334	-$71,356
2022/23	$1,384,350	$3,340,000		$3,697,634	$4,647	$350,281
2021/22	$1,182,500	$1,362,500		$1,314,826	$64,865	$5,191

Floating Rate Notes (FRNs) are required to be revalued each month using the Fair Value (FV) method, which estimates the market value of the investment. Council's remaining FRN matured in February 2025, and there has been no movement in FV since then

Council will focus on shorter-term term deposits to meet cash flow needs

Financial Investment Policy

All categories are within the Policy limits for credit ratings. The portfolio remains well diversified, with credit quality rated as A, or higher. The maximum holding limit in each rating category and the target credit quality weighting for Council's portfolio are:

Long Term Rating Range (Standard & Poors)	Invested	Maximum Policy Holding	Distribution
AA Category	$120,107,423	100.00%	83.93%
A Category	$23,000,000	60.00%	16.07%
BBB Category	$0	35.00%	0.00%
Unrated ADIs (NR)	$0	10.00%	0.00%

Loan Borrowings

Council's Loan Borrowing Policy is the framework for Council's borrowing activities. This defines responsibilities and parameters for borrowing and related risk management activities.

The Policy's objective is to control Council's exposure to movements in interest rates through the application of fixed, floating, or a combination thereof, to maintain a risk averse strategy.

Loan borrowings are in line with the following principles:

a) That the capital cost of infrastructure be recognised over the period during which the benefits will be enjoyed.
b) That loan funds are a resource to fund the replacement and upgrading of existing infrastructure and fund the creation of new infrastructure.
c) That loan funds will be limited to:
    - acquisition or enhancement of income producing assets;
    - construction and/or upgrading of buildings; and
    - infrastructure assets that have a life expectancy of greater than 10 years.

Council has three debt facilities:

Alexander Street Carpark and On-Street Carparking Management System Loan

This is a fixed loan financing option, fully amortising the drawn down amount of $9,500,000 over 10 years, fixed interest rate, with quarterly repayments of interest and principal. The loan details are:

Loan amount:	$ 9,500,000.00			
Loan term:	10 years			
From:	31/07/2018			
To:	31/07/2028			
Interest rate:	4.02%p.a.(fixed)			
Repayment:	Quarterly			
Dates	**Principal Outstanding**	**Interest**	**Principal**	**Payment**
1/07/2024	$4,505,143.19			
31/07/2024	$4,261,152.46	$45,648.83	$243,990.71	$ 289,639.54
31/10/2024	$4,014,689.49	$43,176.57	$246,462.97	$ 289,639.54
31/01/2025	$3,765,729.20	$40,679.25	$248,960.29	$ 289,639.54
30/04/2025	$3,513,002.06	$36,912.40	$252,727.14	$ 289,639.54

Loan Funded Capital Projects:

Project 1: Upgrading the Car Park in Alexander Street, Crows Nest
$5 million loan was sourced to fund project.
Current length of Loan as per the Long-Term Financial Plan (LTFP): 10 years to 2028

Project 2: Upgrading of On-Street Parking Management System
$4.5 million loan was sourced to fund project.
Current length of Loan as per LTFP: 10 years to 2028

Note: This On-Street Parking Management System is now redundant, having been replaced in July 2024.

Loans for North Sydney Olympic Pool Redevelopment

In February 2022, Council established a $31 million TCorp loan facility to partially fund the redevelopment of North Sydney Olympic Pool. Drawdown on the facility was processed on 28 April 2022. The funds were restricted and released, as required, to fund project cash outflows. At 31 May 2024, these loan funds had been fully expended.

This loan is a fixed loan financing option, fully amortising the drawn down amount of $31,000,000 over 20 years, fixed interest rate with semi-annual repayments of interest and principal. The loan details are:

Loan amount:	$31,000,000.00			
Loan term:	20 years			
From:	28/04/2022			
To:	28/04/2042			
Interest rate:	4.24%p.a.(fixed)			
Repayment:	Semi-Annual			
Dates	**Principal Outstanding**	**Interest**	**Principal**	**Payment**
01/07/2024	$28,935,444.66			
30/10/2024	$28,391,663.57	$613,431.43	$543,781.09	$1,157,212.52
29/04/2025	$27,836,354.32	$601,903.27	$555,309.25	$1,157,212.52

In July 2024, Council established a $20 million TCorp loan facility to fund further budget requirements of the redevelopment of North Sydney Olympic Pool. Drawdown on the facility was processed on 27 July 2024. The funds were invested with a maturity profile to match cash flow requirements of the project. The funds were restricted and are being released, as required, to fund project cash outflows. As at 31 May 2025 $5 million remained restricted.

This loan is a fixed loan financing option, fully amortising the drawn down amount of $20,000,000 over 10 years, fixed interest rate with semi-annual repayments of interest and principal. The loan details are:

Loan amount:	$20,000,000.00			
Loan term:	10 years			
From:	26/07/2024			
To:	26/07/2034			
Interest rate:	5.29%p.a.(fixed)			
Repayment:	Semi-Annual			
Dates	**Principal Outstanding**	**Interest**	**Principal**	**Payment**
27/07/2024	$20,000,000.00			
28/01/2025	$19,228,419.44	$529,000.00	$771,580.56	$1,300,580.56

The $10 million loan was approved to meet additional funding requirements for the North Sydney Pool. The loan was approved by TCorp and the agreement was signed by Council on 30 May 2025. The facility will remain available until 30 November 2025, with the drawdown planned for the next financial year.

Consultation Requirements

Community engagement is not required.

Financial/Resource Implications

Council has increased its interest and investment income by $2,700,000 from the original budget, including an adjustment of $1.2 million in the March Quarter Review. After these adjustments, the returns are aligned with the budget. The increase is mostly due to higher-than-expected cash balances resulting from the timing of the Capital Works program.

Legislation

Section 625 of the Local Government Act (NSW) allows councils to invest money that is not currently required for any other purpose. It further specifies how councils may invest. It specifies investments must be in accordance with the local government minister's orders. Clause 212 of the Local Government Regulation (NSW) 2021 requires that the Responsible Accounting Officer must make a monthly report to Council, setting out all details of money invested under Section 625 of the Local Government Act.

Sections 621 to 624 of the Local Government Act give councils the ability to borrow money and specify some further regulations on that borrowing. Council's staff consider it prudent to provide monthly reporting of loans.

Monthly Investment Review

May 2025

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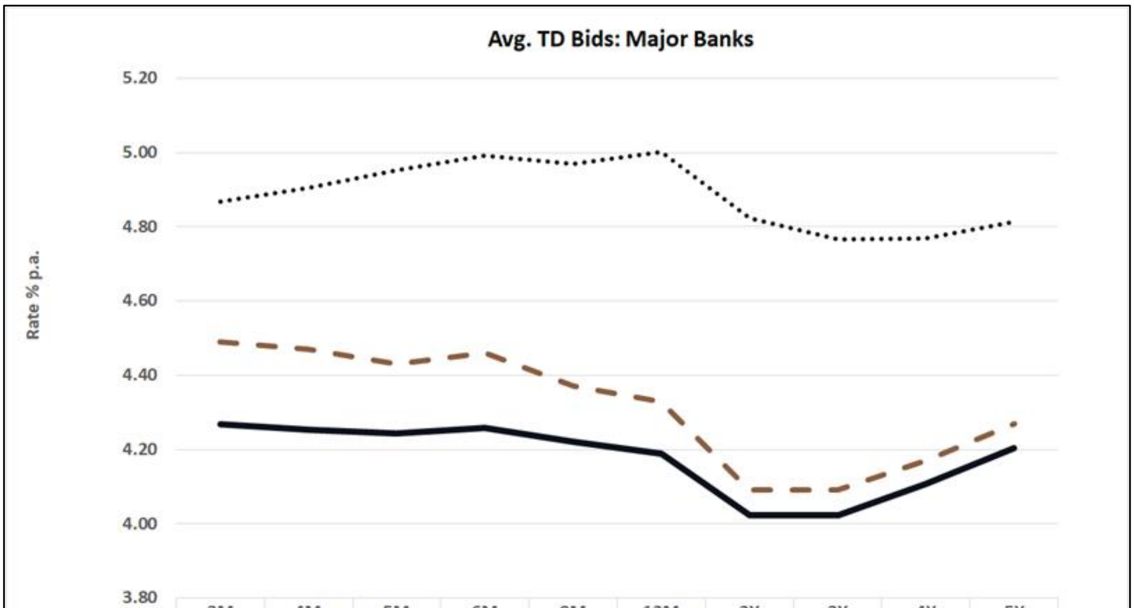
Market Update Summary

Financial markets rallied in May in the 'risk-on' environment with tariff negotiations seemingly heading in the right direction. Shares provided strong returns, whilst bond yields rose (valuations fell), with the market softening their expectations of a severe (US and global) recession, whilst marginally parring back the timing and the number of additional rate cuts to be delivered by central banks.

In the deposit market, over May, at the very short-end of the curve (less than 6 months), the average deposit rates offered by the domestic major banks fell by around 20bp compared to where they were the previous month (April), after the RBA delivered another rate cut. At the longer-end of the curve (1-5 years), the average rates have fell by ~7bp compared to where they were in April, with the market factoring up to another three rate cuts over the next 12 months.



	3M	4M	5M	6M	9M	12M	2Y	3Y	4Y	5Y
May-2025	4.27	4.25	4.24	4.26	4.22	4.19	4.02	4.02	4.11	4.20
Apr-2025	4.49	4.47	4.43	4.46	4.37	4.33	4.09	4.09	4.17	4.27
Nov-2024	4.87	4.91	4.95	4.99	4.97	5.00	4.82	4.77	4.77	4.81

Source: Imperium Markets

With additional rate cuts and a global economic downturn priced in over 2025, investors should consider diversifying and taking an 'insurance policy' against a potentially lower rate environment by investing across 1-5 year fixed deposits and locking in rates above 4% p.a. (small allocation only).

North Sydney Council' Portfolio & Compliance

Asset Allocation

As at the end of May 2025, the portfolio was mainly directed to fixed term deposits (~86%). The remaining portfolio is directed to fixed bonds (~4%) and overnight cash accounts (20%).

Senior FRNs are now trading at a 'fair value' on a historical basis, and new issuances should be considered on a case by case scenario. For fixed interest investments, staggering a mix of fixed deposits between 12 months to 5 years remains a more optimal strategy to maximise returns over a longer-term cycle.

With additional interest rate cuts and a global economic downturn being priced in 2025, investors can choose to allocate a small proportion of longer-term funds and undertake an insurance policy against additional rate cuts by investing across 1-5 year fixed deposits, locking in and targeting yields above 4% p.a.

However, noting the significant capital outflows expected in the near term, Council is currently largely restricted to investing into very short-term investments (under 6-12 months). This is suitable to invest in short-dated fixed term deposits or high yielding cash accounts.

Term to Maturity

Overall, the portfolio remains lightly diversified from a maturity perspective. Around 6% of assets is directed to medium-term assets (1-2 years), which has resulted in solid performance during the challenging economic environment over longer-term time periods. There is still high capacity to invest in the short-medium term horizon (1-2 years), with approximately $92m at month-end.

Where liquidity permits (once immediate capital projects are finalised), we recommend new surplus funds be directed to 1-3 year horizon given this will help optimise returns over the long-run. We suggest this be allocated to any remaining attractive fixed term deposits.

In the interim, given the large ongoing capital expenditure flagged in the short-term, Council is likely to invest across shorter-tenors to match the capital program's cash flow requirements.

Compliant	Horizon	Invested ($)	Invested (%)	Min. Limit (%)	Max. Limit (%)	Available ($)
✓	0 - 90 days	$89,607,423	62.62%	10%	100%	$53,500,000
✓	91 - 365 days	$45,500,000	31.79%	20%	100%	$97,607,423
✓	1 - 2 years	$8,000,000	5.59%	0%	70%	$92,175,196
✓	2 - 5 years	$0	0.00%	0%	50%	$71,553,711
✓	5 - 10 years	$0	0.00%	0%	25%	$35,776,856
		$143,107,423	**100.00%**			

Counterparty

As at the end of May, all individual limits comply with the Policy. We remind Council exposures to individual ADIs are driven by the portfolio's movements throughout any month. Overall, the portfolio is lightly diversified across the investment grade spectrum, with no exposure to the unrated ADIs (high credit quality).

Compliant	Issuer	Rating	Invested ($)	Invested (%)	Max. Limit (%)	Available ($)
✓	ANZ (Suncorp)	AA-	$5,000,000	3.49%	30.00%	$37,932,227
✓	CBA	AA-	$31,607,423	22.09%	30.00%	$11,324,804
✓	NAB	AA-	$37,000,000	25.85%	30.00%	$5,932,227
✓	NTTC Treasury	AA-	$6,000,000	4.19%	30.00%	$36,932,227
✓	Westpac	AA-	$40,500,000	28.30%	30.00%	$2,432,227
✓	ICBC Sydney	A	$13,000,000	9.08%	15.00%	$8,466,113
✓	Bendigo	A-	$10,000,000	6.99%	15.00%	$11,466,113
			$143,107,423	**100.00%**		

On 31st July 2024, ANZ's takeover of Suncorp Bank was formalised, and ratings agency S&P upgraded Suncorp's long-term credit rating to that of its parent company immediately (now rated AA-). Any future investments with Suncorp will now be reflected under the parent company being ANZ.

Credit Quality

The portfolio remains lightly diversified and is of very high quality. As at the end of May 2025, all categories were within the Policy limits, with all now in the AA or A rated categories:

Compliant	Credit Rating	Invested ($)	Invested (%)	Max. Limit (%)	Available ($)
✓	AA Category	$120,107,423	83.93%	100%	$23,000,000
✓	A Category	$23,000,000	16.07%	60%	$62,864,454
✓	BBB Category	$0	0.00%	35%	$50,087,598
✓	Unrated ADIs	$0	0.00%	10%	$14,310,742
		$143,107,423	**100.00%**		

Arlo Advisory

Performance

Council's performance for the month ending May 2025 is summarised as follows:

Performance (Actual)	1 month	3 months	6 months	FYTD	1 year	2 years	3 years
Official Cash Rate	0.32%	1.00%	2.04%	3.88%	4.25%	4.25%	3.73%
AusBond Bank Bill Index	0.34%	1.05%	2.16%	4.06%	4.42%	4.37%	3.79%
Council's T/D Portfolio	0.34%	1.05%	2.11%	3.76%	4.07%	3.87%	3.35%
Council's FRN Portfolio	0.00%	0.00%	1.02%	3.39%	3.87%	4.68%	4.38%
Council's Bond Portfolio	0.11%	0.32%	0.64%	1.13%	1.22%	1.20%	1.19%
Council's Portfolio^	**0.33%**	**1.01%**	**2.03%**	**3.60%**	**3.89%**	**3.71%**	**3.23%**
Rel. Performance	**-0.01%**	**-0.03%**	**-0.13%**	**-0.46%**	**-0.53%**	**-0.66%**	**-0.56%**

^Total portfolio performance excludes Council's cash account holdings.

Performance (% p.a.)	1 month	3 months	6 months	FYTD	1 year	2 years	3 years
Official Cash Rate	3.85%	4.02%	4.14%	4.24%	4.25%	4.25%	3.73%
AusBond Bank Bill Index	4.12%	4.22%	4.38%	4.43%	4.42%	4.37%	3.79%
Council's T/D Portfolio	4.12%	4.24%	4.27%	4.10%	4.07%	3.87%	3.35%
Council's FRN Portfolio	0.00%	0.00%	2.07%	3.70%	3.87%	4.68%	4.38%
Council's Bond Portfolio	1.29%	1.29%	1.28%	1.23%	1.22%	1.20%	1.19%
Council's Portfolio^	**3.97%**	**4.08%**	**4.11%**	**3.93%**	**3.89%**	**3.71%**	**3.23%**
Rel. Performance	**-0.15%**	**-0.14%**	**-0.27%**	**-0.50%**	**-0.53%**	**-0.66%**	**-0.56%**

^Total portfolio performance excludes Council's cash account holdings.

For the month of May, the total investment portfolio (excluding cash) provided a solid return of +0.33% (actual) or +3.97% p.a. (annualised), slightly underperforming the AusBond Bank Bill Index return of +0.34% (actual) or +4.12% p.a. (annualised). The relative 'underperformance' over the past few years was due to the unexpected aggressive rate hikes undertaken by the RBA following the aftermath of the pandemic and Russia's invasion of Ukraine, which resulted in spike in global inflation. Whilst this 'underperformance' may continue in the short-term, we do anticipate this to be fairly temporary given the RBA has now commenced its easing cycle.

Note the period of underperformance is also highly dependent on reinvesting maturing funds at prevailing market rates *beyond 6 month tenors*. With large capital outflows, maturing funds are largely being spent or kept in low yielding short-dated assets. Council should also remind itself it has consistently 'outperformed' over longer-term time periods (last +10yrs).

Recommendations for Council

Term Deposits

As at the end of May 2025, Council's deposit portfolio was yielding **3.93% p.a.** (down 14bp from the previous month), with a weighted average duration of around 122 days (~4 months). We recommend Council slightly increases this weighted average duration, should cash flows allow in future.

In the immediate future, given the significant outflows anticipated from capital projects, short-dated term deposits are suitable for North Sydney Council's purposes.

Please refer to the section below for further details on the Term Deposit market.

Securities

Primary (new) **FRNs** (with maturities between 3-5 years) are now 'fair value' again and remain appealing (particularly for those investors with portfolios skewed towards fixed assets) and should be considered on a case by case scenario. **Fixed Bonds** may also provide attractive opportunities from new (primary) issuances.

Please refer to the section below for further details on the FRN market.

Council's Senior Bonds

During October 2020, Council placed $3m in the Northern Territory Treasury Corporation (NTTC), locking in a yield of 1.00% p.a. for a 5 year term. In August 2021, it placed another $3m parcel with NTTC (AA-), locking in a yield of 1.50% p.a. for a 5 year term.

Council received the full rebated commission of 0.25% on the total face value of investments (i.e. $6m x 0.25% = $15,000) as it was introduced by Imperium Markets (sister company of Arlo Advisory). We believe these investments were prudent at the time of investment especially after the rate cut delivered in early November 2020 to 0.10% and the RBA's forward guidance on official interest rates (no rate rises "*until at least 2024*"). The NTTC bonds are a 'retail' offering and not 'wholesale' issuances. Given the lack of liquidity and high penalty costs if they were to be sold/redeemed prior to the maturity date, they are considered to be a hold-to-maturity investment and will be marked at par value ($100.00) throughout the term of investment.

Term Deposit Market Review

Current Term Deposits Rates

As at the end of May, we see value in the following:

ADI	LT Credit Rating	Term	Rate % p.a.
ING Bank	A	5 years	4.39%
NAB	AA-	5 years	4.30%
BoQ	A-	5 years	4.30%
Westpac	AA-	5 years	4.24%
ING Bank	A	4 years	4.24%
BoQ	A-	4 years	4.20%
Westpac	AA-	4 years	4.10%
Hume Bank	BBB+	4 years	4.10%
NAB	AA-	3 years	4.13%
ING Bank	A	3 years	4.10%
BankVIC	BBB+	3 years	4.10%
BoQ	A-	3 years	4.05%
State Bank of India	BBB-	2 years	4.25%
NAB	AA-	2 years	4.10%
BankVIC	BBB+	2 years	4.10%
ING Bank	A	2 years	4.06%

The above deposits are suitable for investors looking to maintain diversification and lock-in a slight premium compared to purely investing short-term.

For terms under 12 months, we believe the strongest value is currently being offered by the following ADIs (*we stress that rates are indicative, dependent on daily funding requirements and different for industry segments*):

ADI	LT Credit Rating	Term	Rate % p.a.
State Bank of India	BBB-	12 months	4.50%
ICBC	A	12 months	4.22%
Westpac	AA-	12 months	4.20%
Australian Unity	BBB+	12 months	4.20%
NAB	AA-	12 months	4.19%
State Bank of India	BBB-	9 months	4.50%
BankVIC	BBB+	9 months	4.25%
NAB	AA-	9 months	4.20%
Westpac	AA-	9 months	4.20%
State Bank of India	BBB-	6 months	4.60%
Bank of Sydney	Unrated ADI	6 months	4.40%
BankVIC	BBB+	6 months	4.35%
BoQ	A-	6 months	4.30%
NAB	AA-	6 months	4.25%
State Bank of India	BBB-	3 months	4.65%
Bank of Sydney	Unrated ADI	3 months	4.45%
NAB	AA-	3 months	4.25%

For those investors that do not require high levels of liquidity and can stagger their investments longer term, they will be rewarded over a longer-term cycle if they roll for an average min. term of 12 months, with a spread of investments out to 5 years (this is where we see current value). In a normal market environment (upward sloping yield curve), investors could earn over a cycle, on average, up to ¼-½% p.a. higher compared to those investors that entirely invest in short-dated deposits.

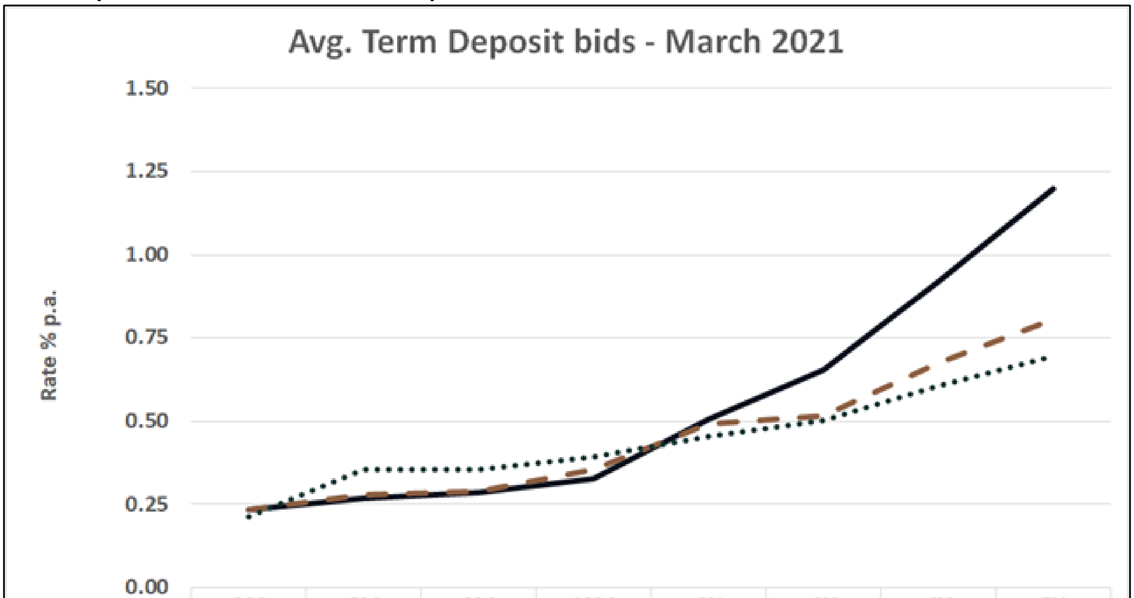
With additional rate cuts and a global economic downturn priced in over 2025, investors should consider allocating some longer-term surplus funds and undertake an insurance policy by investing across 1-5 year fixed deposits and locking in rates above 4% p.a. This will provide some income protection if the RBA decides to continue cutting rates over 2025 and into 2026.

Arlo Advisory

Term Deposits Analysis

Pre-pandemic (March 2020), a 'normal' marketplace meant the lower rated ADIs (i.e. BBB category) were offering higher rates on term deposits compared to the higher rated ADIs (i.e. A or AA rated). But due to the cheap funding available provided by the RBA via their Term Funding Facility (TFF) during mid-2020, allowing the ADIs to borrow as low as 0.10% p.a. fixed for 3 years, those lower rated ADIs (BBB rated) did not require deposit funding from the wholesale deposit. Given the higher rated banks had more capacity to lend (as they have a greater pool of mortgage borrowers), they subsequently were offering higher deposit rates. In fact, some of the lower rated banks were not even offering deposit rates at all. As a result, most investors placed a higher proportion of their deposit investments with the higher rated (A or AA) ADIs over the past three years.

Term Deposit Rates – 12 months after pandemic (March 2021)



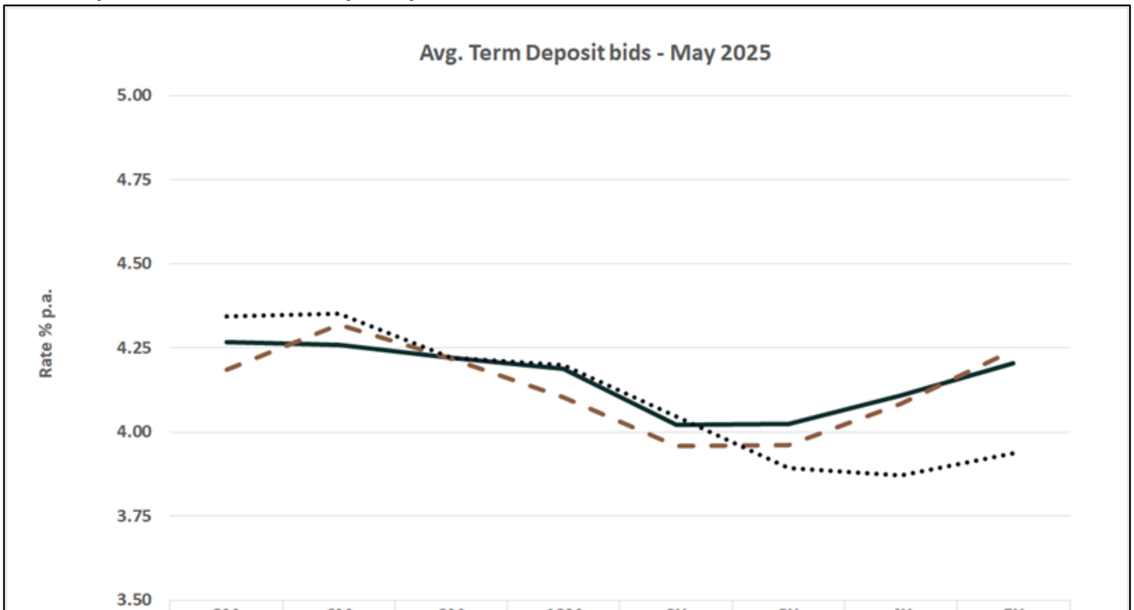
	3M	6M	9M	12M	2Y	3Y	4Y	5Y
Majors	0.23	0.27	0.29	0.33	0.51	0.65	0.92	1.20
A Rated	0.23	0.28	0.29	0.35	0.49	0.52	0.68	0.81
BBB Rated	0.21	0.36	0.35	0.39	0.45	0.50	0.61	0.70

Source: Imperium Markets

The abnormal marketplace experienced during the pandemic is starting to reverse as the competition for deposits slowly increases, partially driven by the RBA's term funding facility coming to an end. In recent months, we have started to periodically see some of the lower rated ADIs ("A" and "BBB" rated) offering slightly higher rates compared to the domestic major banks ("AA" rated) on different parts of the curve (i.e. pre-pandemic environment). Some of this has been attributed to lags in adjusting their deposit rates as some banks (mainly the lower rated ADIs) simply set their rates for the week.

Going forward, investors should have a larger opportunity to invest a higher proportion of its funds with the lower rated institutions (up to Policy limits), from which the majority are not lending to the Fossil Fuel industry or considered 'ethical'. We are slowly seeing this trend emerge, although the major banks always seem to react more quickly than the rest of the market during periods of volatility:

Term Deposit Rates – Currently (May 2025)



	3M	6M	9M	12M	2Y	3Y	4Y	5Y
Majors	4.27	4.26	4.22	4.19	4.02	4.02	4.11	4.20
A Rated	4.19	4.32	4.22	4.10	3.96	3.96	4.09	4.24
BBB Rated	4.34	4.35	4.22	4.20	4.05	3.89	3.87	3.94

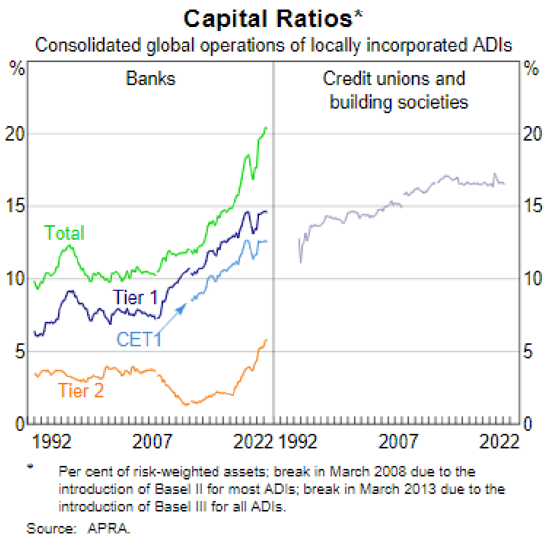
Source: Imperium Markets

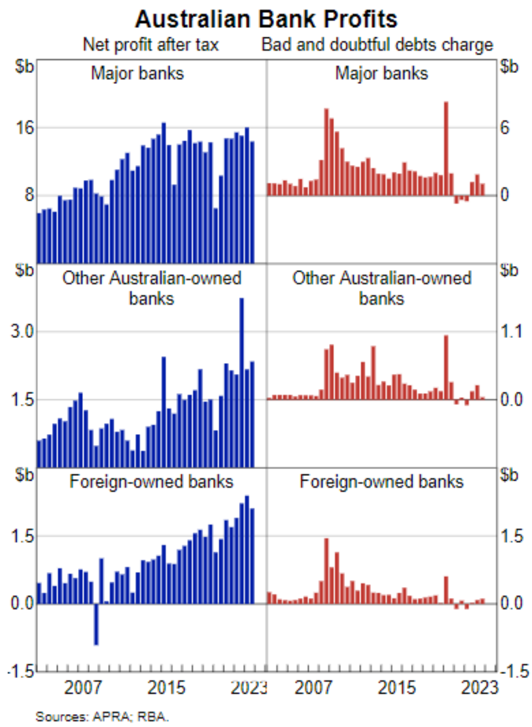
Financial Stability of the Banking (ADI) Sector

The RBA's latest Financial Stability report of 2024 reaffirms the strong balance sheet across the ADI sector. They noted that the risk of widespread financial stress remains limited due to the generally strong financial positions of most (individual) borrowers. Very few mortgage borrowers are in negative equity, limiting the impact on lenders (ADIs) in the event of default and supporting their ability to continue providing credit to the economy. Most businesses that have entered insolvency are small and have little debt, limiting the broader impact on the labour market and thus household incomes, and on the capital position of lenders (ADIs).

Australian banks (collectively the APRA regulated ADIs) have maintained prudent lending standards and are well positioned to continue supplying credit to the economy. A deterioration in economic conditions or temporary disruption to funding markets is unlikely to halt lending activity. Banks have anticipated an increase in loan arrears and have capital and liquidity buffers well above regulatory requirements (*see Capita Ratios chart below*). APRA's mandate is to "*protect depositors*" and provide "*financial stability*".

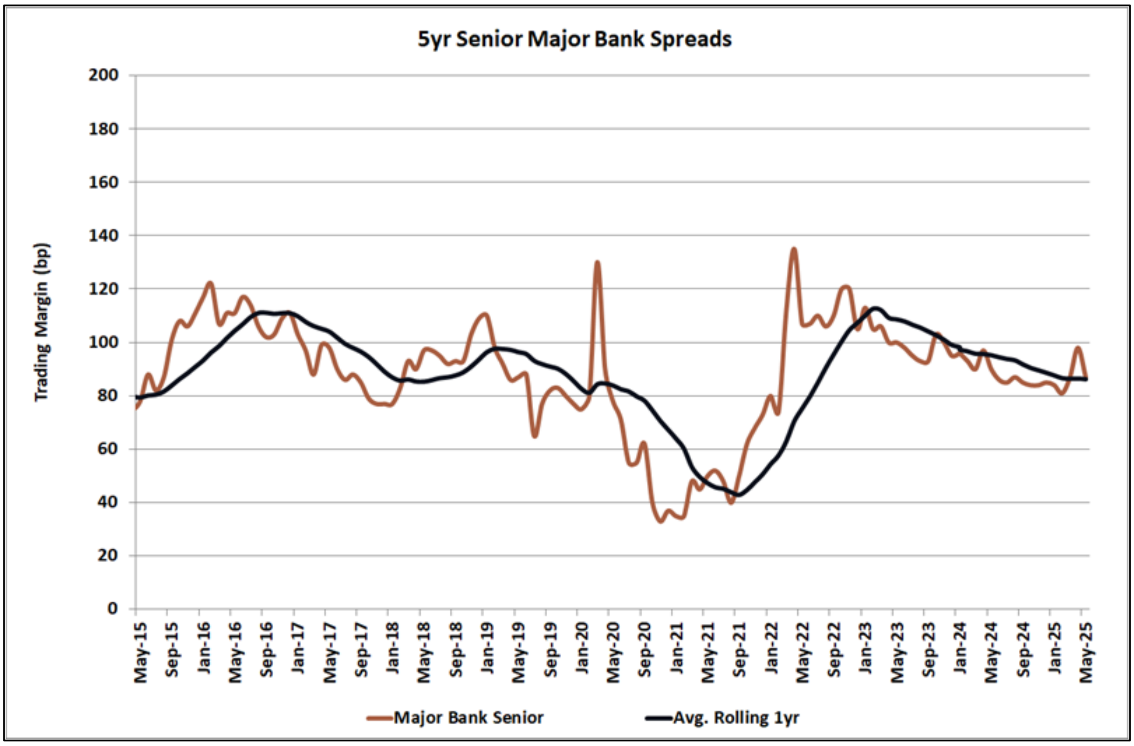
Over the past two decades, both domestic and international banks continue to operate and demonstrate high levels of profitability (*see Australian Bank Profits chart below*), which also includes two stress-test environments being the GFC (September 2008) and the COVID pandemic (March 2020):





Senior FRNs Market Review

Over May, amongst the senior major bank FRNs, physical credit securities tightened up to 11bp at the long-end of the curve. During the month, Suncorp (AA-) issued a new 5 year senior security at +93bp, whilst ANZ (AA-) issued a new 1 year FRN at +42bp. Long-term major bank senior securities are looking 'fair' value around the +85-90bp level for a 5 year tenor.



Source: IBS Capital

There was minimal primary issuances amongst the senior bank market this month, with the only notable lines being the small levels issued by:

- RACQ (BBB+) 3 year senior FRN at +135bp
- Bank of Us (BBB+) 1 year senior FRN at +95bp

Amongst the "A" rated sector, the securities widened up to 13bp at the longer-end of the curve, whilst the "BBB" rated sector remained relatively flat.

Overall, credit securities remain fair value on a historical basis. FRNs will continue to play a role in investors' portfolios mainly based on their liquidity and the ability to roll down the curve and gross up returns over ensuing years (in a relatively stable credit environment), whilst also providing some diversification to those investors skewed towards fixed assets.

Senior FRNs (ADIs)	31/05/2025	30/04/2025
"AA" rated – 5yrs	+87bp	+98bp
"AA" rated – 3yrs	+69bp	+77bp
"A" rated – 5yrs	+97bp	+110bp
"A" rated – 3yrs	+77bp	+88bp
"BBB" rated – 3yrs	+130bp	+130bp

Source: IBS Capital

We now generally recommend switches ('benchmark' issues only) into new primary issues, out of the following senior FRNs that are maturing:

- On or before mid-2027 for the "AA" rated ADIs (domestic major banks);
- On or before mid-2026 for the "A" rated ADIs; and
- Within 6-9 months for the "BBB" rated ADIs (consider case by case).

Investors holding onto the above senior FRNs ('benchmark' issues only) in their last few years are now generally holding sub optimal investments and are not maximising returns by foregoing realised capital gains. In the current challenging economic environment, any boost in overall returns should be locked in when it is advantageous to do so, particularly as switch opportunities become available.

Senior Fixed Bonds – ADIs (Secondary Market)

With global inflation softening and official interest rates starting to drop progressively, investors may look at some opportunities in the secondary market. We currently see value in the following fixed bond lines (please note supply in the secondary market may be limited on any day):

ISIN	Issuer	Rating	Capital Structure	Maturity Date	~Remain. Term (yrs)	Fixed Coupon	Indicative Yield
AU3CB0314763	Bendigo	A-	Senior	24/10/2028	3.41	4.79%	4.38%
AU3CB0308955	BoQ	A-	Senior	30/04/2029	3.93	5.30%	4.53%
AU3CB0319879	Nova Sco.	A-	Senior	21/03/2030	4.82	5.23%	5.02%

Economic Commentary

International Market

Financial markets rallied in May in the 'risk-on' environment with tariff negotiations seemingly heading in the right direction. Shares provided strong returns, whilst bond yields rose (valuations fell), with the market softening their expectations of a severe (US and global) recession, whilst marginally parring back the timing and the number of additional rate cuts to be delivered by central banks.

Across equity markets, the US S&P 500 Index rose +6.15%, whilst the NASDAQ surged +9.56%. Europe's main indices also rose, with gains in Germany's DAX (+6.67%), UK's FTSE (+3.27%) and France's CAC (+2.08%).

US-China trade negotiations have improved market sentiment dramatically. The US reduced the tariffs on China imports to 30% from 145% for 90 days and China reduced its tariffs on US imports to 10% from 125%.

The US FOMC left the funds rate unchanged at 4.50-4.25%. The decision was unanimous. The post-meeting statement noted that "*uncertainty around the economic outlook has increased further*".

The US economy contracted an annualised -0.3% rate in the March 2025 quarter, the first GDP fall since 2022. The contraction is largely the result of a surge in imports before the implementation of tariffs.

US inflation for April came in better than expected at +0.22% for headline versus forecast of +0.30%, which saw the annual rate fall from +2.4% to +2.3%. Core inflation was +0.24% versus forecast of +0.30% with the annual rate holding steady at +2.8%.

Canada's headline inflation came down to +1.7% from +2.3% in March, its lowest since last September. Core measures in contrast accelerated, to an average of +3.2% up from +2.9%.

Eurozone headline CPI remained steady at a +2.2% annual rate in April which compared consensus expectations for a drop to +2.1%. Core inflation rose to +2.7%, from +2.4% in March which was also above expectations.

The Bank of England (BoE) cut interest rates by 25bp to 4.25%, but the vote split was hawkish with two (of nine) unexpectedly voting for unchanged and two wanting a 50bp cut. UK GDP figures surprised to the upside at +0.7% q/q, making it the fastest growing major economy in the quarter.

The MSCI World ex-Aus Index rose +6.00% for the month of May:

Index	1m	3m	1yr	3yr	5yr	10yr
S&P 500 Index	+6.15%	-0.72%	+5.52%	+12.68%	+14.19%	+10.87%
MSCI World ex-AUS	+6.00%	+2.20%	+14.30%	+13.90%	+14.80%	+10.60%
S&P ASX 200 Accum. Index	+4.20%	+4.31%	+8.79%	+9.62%	+12.11%	+8.12%

Source: S&P, MSCI

Domestic Market

The RBA cut the official cash rate by 25bp to 3.85% as widely expected, although the (slight) surprise was the admission that a 50bp cut was discussed. The Board assesses monetary policy after this cut to be "*…somewhat less restrictive*", which opens the door for further rate cuts.

The RBA's statement has evolved in a dovish direction since April, with the final sentence now acknowledging both sides of the RBA's dual mandate: "*the Board is focused on its mandate to deliver price stability and full employment and will do what it considers necessary to achieve that outcome*".

The monthly CPI indicator rose +2.4% y/y in April after +2.4% y/y in March. The annual trimmed mean was +2.8% y/y in April from +2.7% y/y in March.

The wage price index (WPI) rose +0.9% q/q (above consensus of +0.8% q/q) in Q1 2025 and +3.4% y/y.

The unemployment rate was 4.1% in April, unchanged from March. The +89k surge in employment growth was alongside a 0.3% lift in the participation rate to 67.1%.

The governing Labor party retained government with an increased majority. Projections put Labor on 94 seats, Liberal/National 43 seats, 11 Independent, and 9 seats are still in doubt.

The monthly trade surplus was much higher than expected with a surplus of $6.9bn for March vs. $3.2bn consensus. The better-than-expected outcome was mostly an exports story with exports lifting +7.6% m/m, while imports also fell -2.2% m/m.

Dwelling prices for April rose +0.3% m/m, further sustaining the turnaround seen since February.

The Australian dollar rose around +0.31%, finishing the month at US64.36 cents (from US64.16 cents the previous month).

Credit Market

The global credit indices tightened significantly in the risk-on environment. They remain at levels last seen around 12 months ago:

Index	May 2025	April 2025
CDX North American 5yr CDS	56bp	67bp
iTraxx Europe 5yr CDS	58bp	68bp
iTraxx Australia 5yr CDS	75bp	92bp

Source: Markit

Fixed Interest Review

Benchmark Index Returns

Index	May 2025	April 2025
Bloomberg AusBond Bank Bill Index (0+YR)	+0.32%	+0.35%
Bloomberg AusBond Composite Bond Index (0+YR)	-0.40%	+1.70%
Bloomberg AusBond Credit FRN Index (0+YR)	+0.64%	+0.22%
Bloomberg AusBond Credit Index (0+YR)	+0.21%	+1.09%
Bloomberg AusBond Treasury Index (0+YR)	+0.02%	+1.82%
Bloomberg AusBond Inflation Gov't Index (0+YR)	+0.41%	+1.22%

Source: Bloomberg

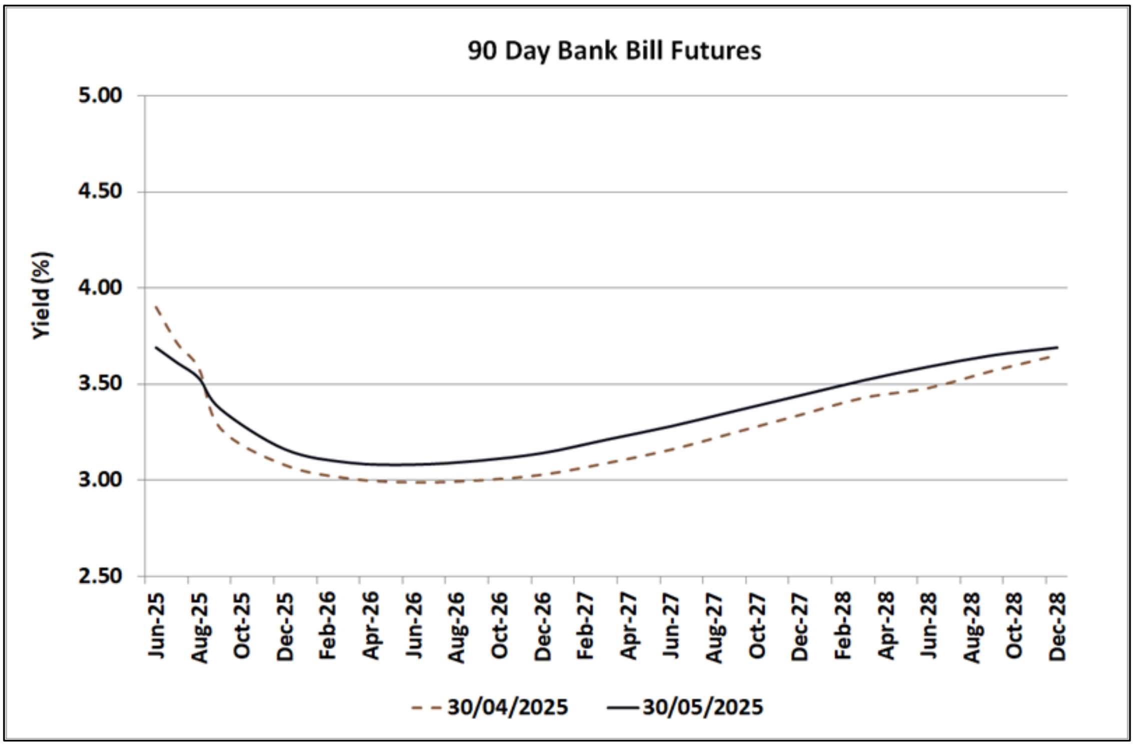
Other Key Rates

Index	May 2025	April 2025
RBA Official Cash Rate	3.85%	4.10%
90 Day (3 month) BBSW Rate	3.73%	3.87%
3yr Australian Government Bonds	3.31%	3.30%
10yr Australian Government Bonds	4.23%	4.14%
US Fed Funds Rate	4.25%-4.50%	4.25%-4.50%
2yr US Treasury Bonds	3.89%	3.60%
10yr US Treasury Bonds	4.41%	4.17%

Source: RBA, ASX, US Department of Treasury

90 Day Bill Futures

Bill futures rose across the curve this month, following the movement in global bond yields. The short-end reflects the market's expectations of further rate cuts to be delivered imminently:



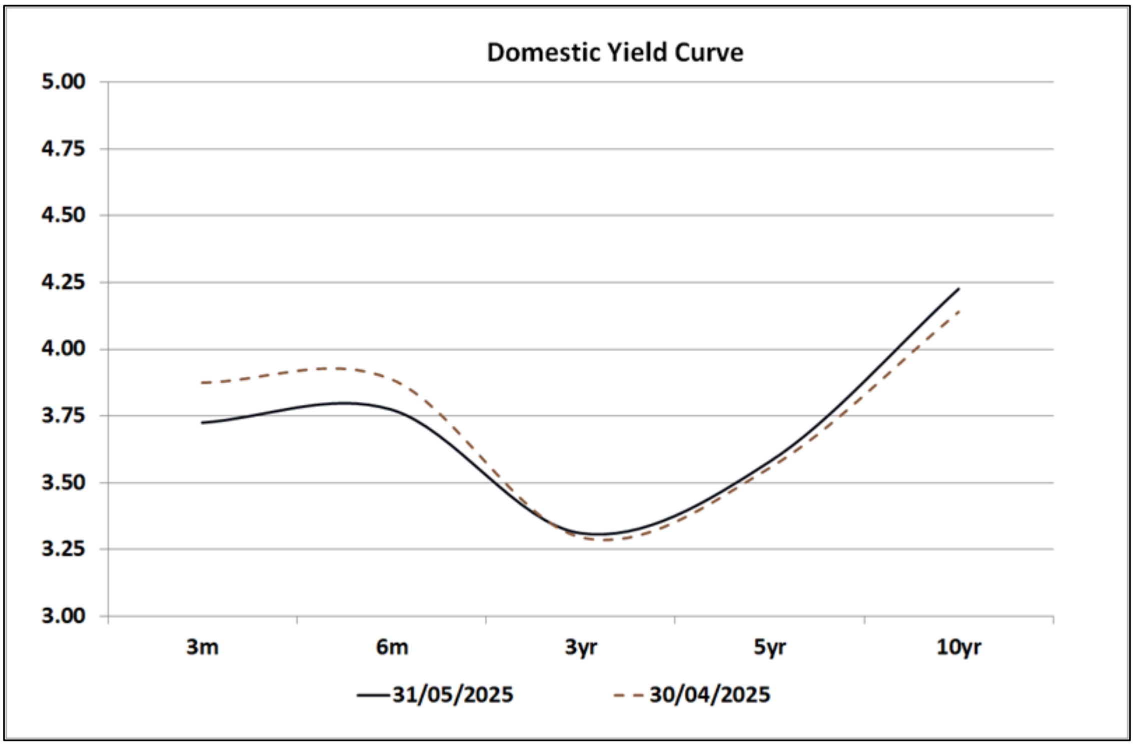
Source: ASX

Fixed Interest Outlook

After keeping interest rates unchanged (as expected) in its latest meeting, US Fed Chair Powell commented that "*the risks of higher unemployment and higher inflation have risen*". Overall Powell concluded that given the underlying solid nature of the economy, the "*the costs of waiting (delaying rate cuts) are fairly low*". The market continues to factor up to two rate cuts by the US Fed for the remainder of 2025, down from at least three the previous month.

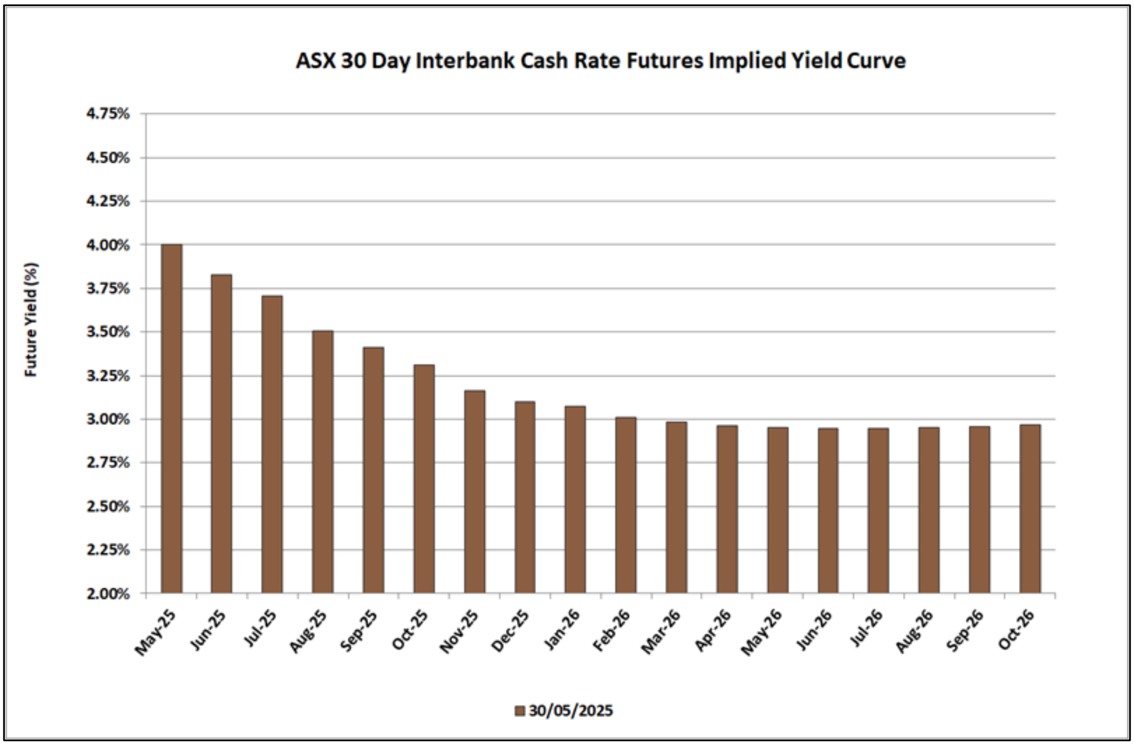
Domestically, after the RBA cut rates again in May, rhetoric on inflation now reflects greater comfort with the inflation forecast. Risks to inflation are described as "*more balanced*", a change from April, where it was noted that there were "*…risks on both sides and the Board is cautious about the outlook*." Core inflation was revised down slightly by the RBA, the unemployment rate was revised higher and the 2025 GDP forecast was revised down.

Yields rose up to 9bp at the longer-end of the curve:



Source: ASX, RBA

Financial markets are still pricing up to three (3) additional rate cuts by year-end, which would take the official cash rate down to 3.10%, although the RBA is still cautious on the potential upside risks to inflation due to international market developments, particularly surrounding the ongoing tariff wars:



Source: ASX

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