MaxCap
Investment Management

MAXCAP INVESTMENT TRUST HIGH YIELD

QUARTERLY INVESTOR UPDATE
DECEMBER 2023

MAXCAP INVESTMENT TRUST – HIGH YIELD

PORTFOLIO MANAGER REPORT – Q4 2023

Dear valued investors, we hope you had a restful holiday period and are looking forward to a prosperous 2024. As we reflect on the final quarter of the year, we are pleased to present the Quarterly Investor Report for the period 1 October 2023 to 31 December 2023 ('Quarter') for the MaxCap Investment Trust – High Yield ('Fund').

Whilst uncertain macroeconomic conditions continue to weigh on overall economic growth, the Fund continues to identify and pursue strong risk-adjusted opportunities in the market, with future deployment prospects buoyed by a substantial and high-quality pipeline.

In light of this, we are pleased to report that, despite an overall reduction in portfolio LVR to 60.8%, (prior quarter: 65.6%) and an overall improvement in underlying portfolio risk metrics, Fund performance continues to improve, with a since inception gross return of 13.76% as of December 2023 (target: 13.27%).

Fund Investments

Our commitment to optimising portfolio composition, risk and return remains unwavering, and we continue to strategically deploy capital into investments that capitalise on both current and emerging macroeconomic tailwinds.

During the quarter we were deployed into, or were mandated on, 12 new investment opportunities:

- Industrial: Mentone (VIC)
- Residential: Sunbury Hills (VIC), Oakleigh (VIC), Oak Grove (VIC), Richmond (VIC), Mosman (NSW), Lumina Stones Corner (QLD), Bellfields (NZ), Rochedale (QLD)
- Office: Brunswick (QLD)
- Hotel: Rydges (NSW)
- Retail: Warrawong (QLD)

With an average LVR of 62.1% and a gross IRR of 14.29%, these new investments continue to improve and enhance the overall metrics of the underlying portfolio. These positive trends are evidence of constrained capital availability, particularly for property development, which means that MaxCap can be highly selective with regard to new investments.

Investments during the quarter were heavily skewed towards Victoria and the residential sector, reflecting our overall portfolio construction strategy, with deployment focused on the deepest markets and the strongest-performing sectors. That being said, we continue to assess opportunities across all sectors and geographies based on their relevant idiosyncratic risks, as well as how they contribute to the overall diversification of the portfolio.

Market Overview

Credit conditions have remained broadly in line with those observed in recent quarters, with no material changes in market pricing. Despite this, the return for risk proposition for new opportunities continues to improve, with the Manager improving overall investor returns whilst also incorporating additional risk enhancements, including more conservative lending structures and lending metrics.

Whilst certain sections of the market remain under pressure, most notably the office sector, the residential and industrial sectors continue to perform well, attracting significant investment both domestically and offshore.

Residential house prices grew 11.1% and 3.5% YoY in Sydney and Melbourne respectively[1], supported by a continued lack of supply and strong immigration inflows. Pleasingly, settlement rates for newly completed Residential developments continue to hold up strongly, with no evidence of an increase in default rates.

The industrial sector continues to be underpinned by limited oncoming supply and record low vacancy levels, driving demand for space across the eastern seaboard. Industrial assets in New South Wales and Victoria continue to be the most sought-after, representing 82% of all industrial investment[2]. Cap rate expansion has so far resulted in moderating growth in valuations which, given the previous rapid increases, is viewed as a healthy development, removing some of the heat which previously built up in that sector.

The uncertain macroeconomic environment continues to dampen overall transaction volumes, with commercial property volumes down 58% in Q3 2023 when compared to the prior year[3]. This is driven by significantly higher funding costs and a reduction in available leverage, with the large domestic banks continuing to reduce their exposure to commercial real estate lending. The reduction in bank

[1] CoreLogic December 2023
[2] Cushman and Wakefield, Marketbeat Australia Investment Q3 2023
[3] JLL 'Australian commercial sales bounce back slightly in Q3' 2023

activity is creating an enhanced opportunity set for non-bank lenders with specialist underwriting capability and sufficient scale to finance high-quality borrowers. Whilst transaction volumes remain low in a historical context, the September quarter represented an increase on the June quarter and may be indicative of investors re-entering the market. We continue to monitor this trend closely and ensure that the most up-to-date transaction data is incorporated as part of our overall risk underwriting process.

Whilst supply chain issues are yet to be resolved entirely, pressure on the construction sector appears to be easing. CoreLogic data for Q4 recorded a quarterly construction cost growth rate of 0.8%, up 0.3% from Q3[4]. The small increase is considered a reversion to historical trends, rather than a new upward drift, with the quarterly growth rate below the pre-Covid decade average of 1.0%. The annual growth rate for the 2023 calendar year was 2.9%, down significantly from 11.9% in the prior year, and indicative that we have likely now passed the peak of cost escalations. As cost escalation returns to the long-term average, we expect construction activity to slowly improve, with the current market supportive of financially strong sponsors and well-located projects.

Interest Rate Overview

The Manager notes that despite an increase in the RBA cash rate to 4.35% in November, market consensus per Bloomberg[5] is that the tightening cycle has peaked, with 76% of economists surveyed forecasting no further cash rate increases. Whilst consumer price inflation dropped to a near two-year low of 4.3% in November[6], it remains stubbornly above the RBA target of 2% - 3%. The Manager is of the view that further policy tightening remains possible until inflation is managed within the target range. The portfolio's structural hedge against inflation continues to shield investors from this volatility, with the portfolio comprising 99% floating rate investments as of quarter end.

Outlook

As the non-bank CRED market continues to grow ahead of expectations[7], we believe the Fund represents a market-leading product through which investors can capitalise on expected future growth.

We look forward to the 2024 year with cautious optimism and remain committed to delivering strong risk-adjusted returns for our valued investors.

Baden Adams

Portfolio Manager

[4] Cordell Construction Cost Index Q4 2023
[5] Bloomberg data as of 22 January 2024
[6] ABS, Monthly Consumer Price Index Indicator, November 2023
[7] AFR, 'Non-bank lending worth $74b, could double in five years'

RETURNS AND PORTFOLIO METRICS

Gross Monthly Returns

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total Annual Return
2023	-	-	1.34%	0.91%	0.73%	0.87%	1.07%	1.14%	1.15%	1.22%	1.19%	1.14%	10.76%

Portfolio Metrics

Weighted average LVR	60.80%
Weighted average LVR target	75.00%
Weighted average term (months)	17
Weighted average time to maturity (months)	9
Borrowers	39
Largest Borrower exposure	14.8%
Fund leverage	17.4%
Percentage of floating rate investments	99%

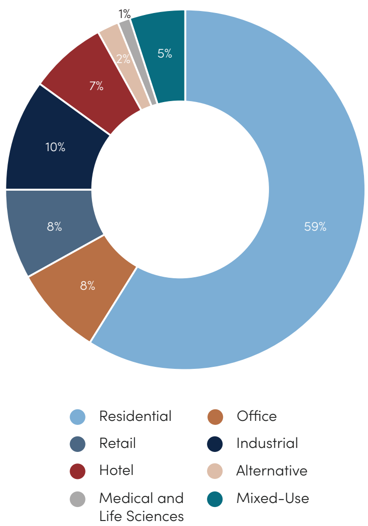
Returns

	1M	3M	6M	12M	Incep[1]
RBA Cash Yield	0.36%	1.05%	2.08%	-	4.03%
Gross Return					
Target	1.09%	3.24%	6.55%	-	13.27%
Q4 2023 actual	1.14%	3.50%	7.01%	-	13.76%
Net Return[2]					
Target	0.99%	2.95%	5.96%	-	12.03%
Q4 2023 actual	0.99%	3.04%	6.07%	-	11.87%

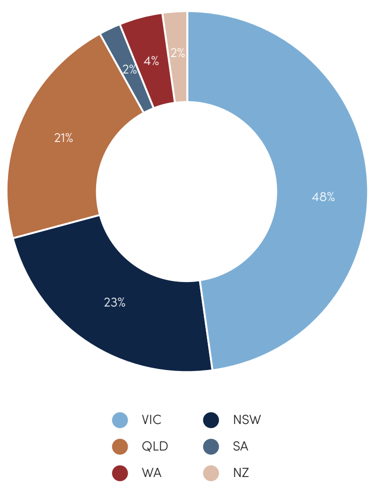
[1]Since inception return is annualised
[2]Net return (after management fees and performance fees) is calculated based on the blended management fee and performance fee rates.

EXPOSURES[1]

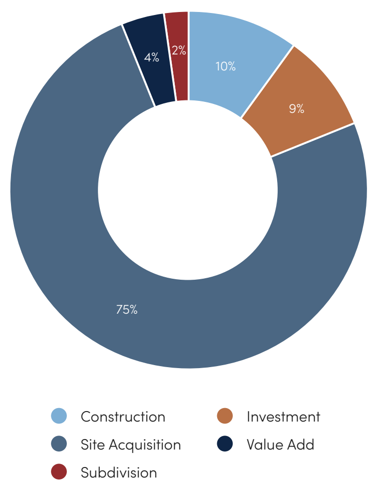
GRAPH 1: SECTOR



GRAPH 2: GEOGRAPHY



GRAPH 3: LOAN TYPE



[1]Based on current exposure

Portfolio Summary

For a detailed summary of each individual investment, please refer to Ansarada data room.

TABLE 1: SUMMARY OF CURRENT INVESTMENTS IN THE PORTFOLIO

INVESTMENT	LOCATION	MATURITY DATE	RANKING	SECTOR	COMMITMENT[3]	CURRENT EXPOSURE[1, 3]	LVR
Brighton International	VIC	Q2 2024	Senior	Residential	$24.4m	$22.0m	65%
HQ78	NSW	Q3 2024	Senior	Industrial	$26.8m	$15.0m	64%
Gillieston Heights	NSW	Q1 2024	Senior	Residential	$23.4m	$18.8m	65%
Rolleston Fields[2]	NZ	Q1 2024	Senior	Retail	$22.2m	$19.1m	65%
Box Hill Shopping Centre	NSW	Q1 2024	Senior	Retail	$50.0m	$18.4m	58%
Brewery Yard	NSW	Q2 2024	Senior	Office	$79.6m	$72.8m	65%
Shell Cove	NSW	Q3 2025	Senior	Hotel	$46.2m	$4.3m	65%
88 Laurens	VIC	Q3 2024	Senior	Office	$30.0m	$20.4m	53%
Wellington	VIC	Q1 2025	Senior	Medical and Life Sciences	$49.9m	$18.5m	65%
Noosa Civic	QLD	Q4 2024	Senior	Medical and Life Sciences	$18.2m	$7.7m	65%
Bellfields[2]	NZ	Q4 2025	Senior	Residential	$39.3m	Not Yet Drawn	65%
Mentone (A-Note)	VIC	Q4 2024	Senior	Industrial	$12.2m	$3.7m	53%
388 Brunswick	QLD	Q4 2024	Senior	Office	$20.5m	Not Yet Drawn	65%
Richmond	VIC	Q3 2025	Senior	Residential	$19.4m	Not Yet Drawn	65%
Sunbury Hills - Construction	VIC	Q2 2025	Senior	Residential	$26.9m	Not Yet Drawn	65%
St Leonards	NSW	Q2 2024	Senior	Residential	$27.2m	$27.2m	65%
Beveridge	VIC	Q2 2024	Senior	Residential	$22.1m	$22.1m	51%
Main Beach (Retail)	QLD	Q3 2024	Senior	Retail	$15.0m	$15.0m	53%
Mackay	QLD	Q1 2024	Senior	Residential	$5.0m	$5.0m	65%
Cambridge	WA	Q3 2024	Senior	Office	$12.1m	$9.7m	60%
A'Beckett	VIC	Q3 2024	Senior	Alternative	$8.1m	$7.6m	65%
Pirie St	SA	Q2 2026	Senior	Office	$34.5m	$9.5m	55%
Brooklyn (Refinance)	VIC	Q2 2024	Senior	Industrial	$21.5m	$21.5m	43%

INVESTMENT	LOCATION	MATURITY DATE	RANKING	SECTOR	COMMITMENT[3]	CURRENT EXPOSURE[1, 3]	LVR
Woolloongabba (Refinance)	QLD	Q4 2024	Senior	Mixed-Use	$26.0m	$23.5m	65%
Ivanhoe	VIC	Q2 2024	Senior	Residential	$10.0m	$10.0m	60%
Frenchs Forest	NSW	Q3 2024	Senior	Industrial	$25.9m	$25.9m	55%
Burly	QLD	Q2 2024	Senior	Residential	$35.7m	$34.0m	70%
Esplanade	QLD	Q1 2024	Senior	Residential	$16.4m	$16.4m	75%
600 Lonsdale	VIC	Q1 2025	Senior	Mixed-Use	$24.0m	$24.0m	60%
Oakleigh	VIC	Q2 2025	Senior	Residential	$23.0m	$23.0m	50%
Rydges	NSW	Q1 2025	Senior	Hotel	$29.9m	$27.3m	61%
Oak Grove	VIC	Q4 2024	Senior	Residential	$74.4m	$74.4m	55%
Mosman	NSW	Q1 2025	Senior	Residential	$14.5m	Not Yet Drawn	65%
Sunbury Hills - Land	VIC	Q1 2025	Senior	Residential	$49.0m	$49.0m	65%
Perth	WA	Q2 2024	Junior	Hotel	$12.3m	$9.0m	66%
Main Beach (Resi)	QLD	Q3 2024	Subordinated	Residential	$13.4m	$12.8m	80%
Nelson Bay	NSW	Q2 2024	Subordinated	Residential	$2.7m	$2.5m	72%
Christchurch[2]	NZ	Q2 2024	Subordinated	Retail	$9.5m	$10.5m	65%
Robina	QLD	Q1 2024	Junior	Residential	$7.5m	$6.7m	77%
Cambewarra	NSW	Q1 2024	Junior	Residential	$11.0m	$10.9m	80%
Mentone (B-Note)	VIC	Q4 2024	Subordinated	Industrial	$2.8m	$2.5m	65%
Shenton Quarter	WA	Q1 2024	Subordinated	Residential	$4.3m	$4.0m	75%
Warrawong	NSW	Q3 2024	Junior	Retail	$11.4m	$11.4m	69%
Rochedale	QLD	Q2 2025	Subordinated	Residential	$11.7m	Not Yet Drawn	75%
388 Brunswick Street (B-Note)	QLD	Q4 2024	Subordinated	Office	$4.5m	Not Yet Drawn	75%
Lumina Stones Corner	QLD	Q4 2025	Junior	Residential	$12.5m	Not Yet Drawn	75%

[1]Inclusive of principal and capitalised interest and fees.
[2]NZ Facility Commitment and Current Exposure converted at the 31 December 2023 spot-rate.
[3]The Commitment and Current Exposure, which may involve multiple tranches and/or lenders/participants, in respect of which relevant sub-limits may apply.

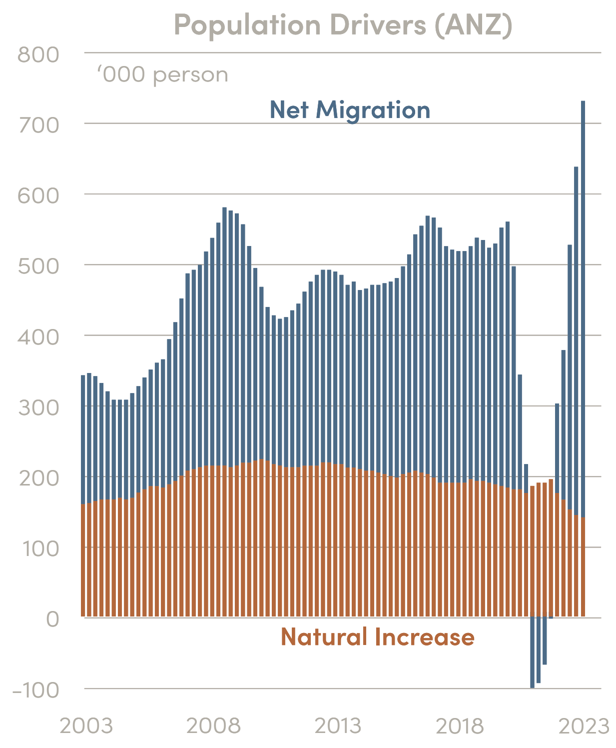
ECONOMIC AND MARKET UPDATE

Slowing economy, driving a likely turning point for interest rates

Economic conditions are generally moderating.

- The **global economy** is slowing clearly, driven mainly by the adverse impacts of higher interest rates, although there is an added layer of uncertainty arising from the conflicts in Ukraine, Gaza, and the broader Middle East. There is also a softening in the Chinese economy, which will have some adverse impacts through weaker commodity demand.
- In **Australia**, the economy continues a subdued expansion (Q3: +2.1% p.a.). Consumers are more visibly constrained by higher mortgage repayments and diminished savings. While housing construction continues to decline, there is remarkably sustained resilience so far in business investment and exports. A population boom (Q2: +2.4% p.a.) is adding considerably to potential economic demand.
- In **New Zealand**, the economy returned to a modest contraction (Q3: +1.3% p.a.), weighed down by broad-based downturns in mining, manufacturing, construction, trade and logistics. A similar surge in population is also occurring (Q3: +2.7% p.a.), which is not just raising demand, but also reducing the median age of the country.

Net migration is boosting population and demand.



Sources: ABS, NZ Stats, MaxCap Group (January 2024)

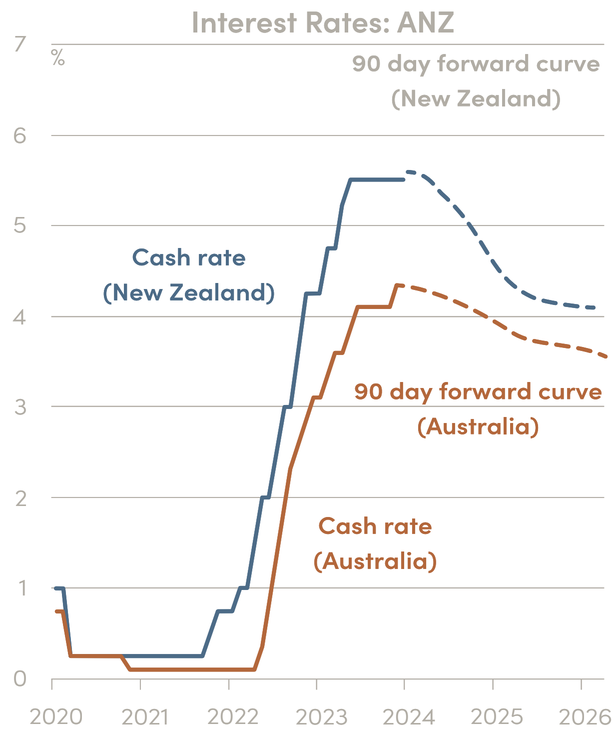
Inflation is easing more clearly and consistently.

- Consumer **price inflation** have moderated markedly from their peaks in both Australia (Nov: +4.3% p.a.) and New Zealand (Q3: +5.6% p.a.) but remain well above their respective central bank targets. The actual return to target inflation is likely still a year or more away.
- Meanwhile, **construction costs** have followed a similar path of sharp inflation, then gradual moderation. The pullbacks since 2022 in both Australia (from 17% to 4%) and New Zealand (from 13% to 5%) are providing a timely opportunity to restore builder profit margins in 2024.

Interest rates poised to ease by the end of the year.

- With more convincing signs of moderating inflation, **central banks** are now preparing for the next phase of cutting interest rates. While the US is likely to be more aggressive in reducing rates, the pace of adjustment is expected to be somewhat slower in Australia, reflecting relatively higher inflation and already lower rate settings locally.
- Indeed, US **money markets** are currently predicting 5-6 rate cuts over the course of 2024 (more than the 3 cuts predicted by policy officials). The equivalent forward curves are only pricing in 4 rate cuts in New Zealand and just 1-2 rate cut in Australia in calendar 2024.

Forward curves are starting to price in rate cuts.



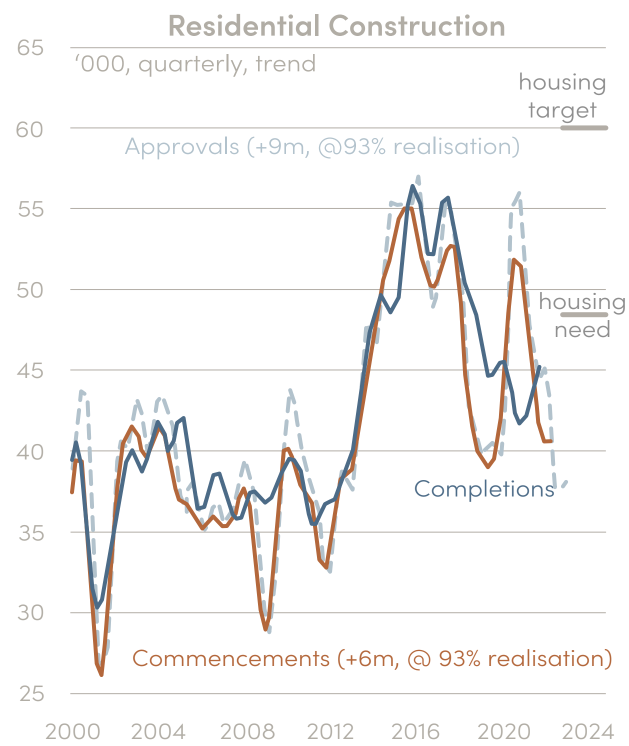
Sources: Bloomberg, MaxCap Group (January 2024)

Capital markets are adjusting to this new outlook.

- With the changing mood around monetary policy settings, there is **much more volatility** across many asset classes. Share markets are gyrating heavily off these evolving rate expectations, while bond markets make a partial comeback after a challenging period last year.
- **Listed real estate markets** started to recover lost ground in Q4 2023, given the quarterly rebounds in the US (+17%), Australia (+15%) and New Zealand (+6%). These more upbeat listed asset pricing – if sustained – should translate to firmer unlisted asset pricing over the course of 1H 2024.
- **Real estate credit** markets are still well on track to deliver sustained and resilient returns amid these bouts of capital market volatility. Indeed, the risk profile of the underlying collateral is expected to improve as these asset market pricing recoveries gather more momentum.

Residential market still marked by considerable undersupply

Housing supply fades amid surging demand.



Sources: ABS, MaxCap Group (January 2024)

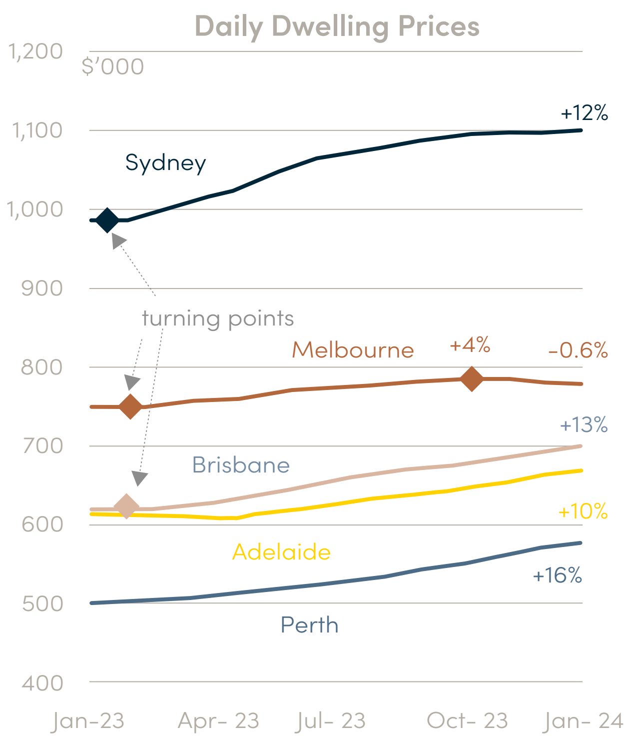
Housing market remains markedly undersupplied.

- **Housing demand** continues to strengthen on the back of robust population growth. Meanwhile, **housing supply** is weakening further in the face of rising construction costs, high interest rates and ongoing labour shortages in the construction industry.
- The clear outcome is a persistent state of **housing undersupply**, which – on Australian government estimates – totals to a shortfall of 125,000 dwellings over the next five years. This is evident from the exceptionally low level of residential vacancies in Australia (Dec: 1.3%) and the lengthening queues outside of weekly rental property inspections across the country.

More moderate gains in housing prices and rents.

- In the latter parts of the year, the housing market saw more **moderate gains** in both prices and rents, reflecting the very real constraints from rising mortgage rates on housing affordability for both buyers and renters alike.
- **Dwelling price** gains continue to be firm for Perth (+5% q/q), Adelaide (+3.7%) and Brisbane (+3.5%), while we see pauses in Sydney (+0.8%) and Melbourne (-0.2%) partially reflecting the seasonal lull around year end.
- Meanwhile, the persistent lack of rental stock continues to support **residential rents** at record levels, most prominently for Sydney units (+23% p.a.) and Melbourne units (+19% p.a.).

A rapid recovery in dwelling prices in 2023.



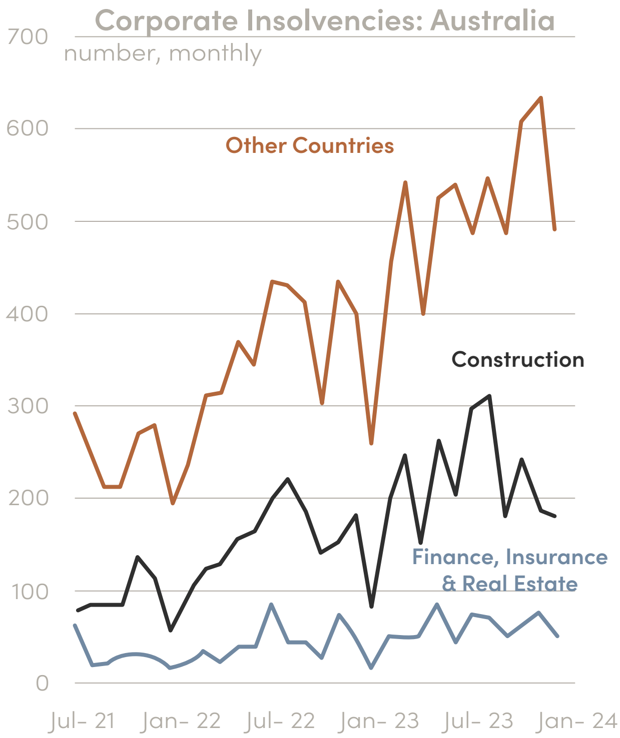
Sources: Corelogic, MaxCap Group (January 2024)

Builder insolvencies remain a key watch point.

- There are clearer signs of sustained moderation in **corporate insolvencies**, particularly in the building sector, towards the back half of 2023. The reasons are quite apparent, as rising selling prices and easing cost inflation combine to reduce the pressures on builder profit margins.

- In terms of timing, we are most likely past the period of maximum strain on construction profit margins in 2022. And we are very likely past the peak of builder insolvency in 2023, which lags the profit squeeze by around a year.
- Undoubtedly, these indicators of financial distress warrant close watching in 2024, but there are more encouraging signs of improving profitability in 2023, which should translate – as we have seen in past cycles – into a lower trend for builder insolvency in 2024.
- Regardless, the trend for real estate developer insolvency remains low and steady, little affected by the recent and massive cycle in costs and profits.

Corporate insolvencies remain quite elevated.



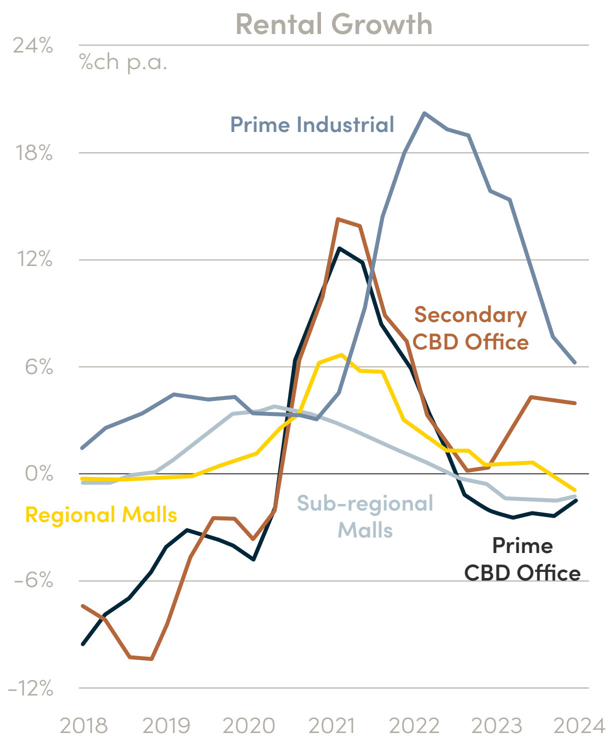
Sources: ASIC, MaxCap Group (January 2024)

Commercial markets face multiple adjustments ahead

Commercial market outlooks are diverging widely.

- **Office** markets are making the structural transition to lower and more selective demand, as white-collar workers cling dearly onto work-from-home arrangements. The longawaited pricing adjustment in office values is finally occurring with more urgency (5 capital cities: -14% from peak), as prices start to approach the thresholds where value investors would be drawn back into the market.
- **Retail** markets are facing big near-term challenges, as rising costs of living, higher mortgage repayments and downbeat consumer sentiment all weigh heavily on the spending outlook. That said, retail mall performances are proving to be quite resilient, with improving store occupancy rates and gradually stabilising rents.
- **Industrial** markets continue to see strong structural demand growth, spurred on by the sustained rise of online shopping and a keener preference for larger just-in-case inventory holdings to ward against supply chain disruptions. Rents are still rising – albeit at a more moderate pace – on the back of insufficient supply and low vacancy rates. That said, asset prices are pulling back a little given the surge in interest rates and funding costs.

Rental growth is differing a lot across sectors.



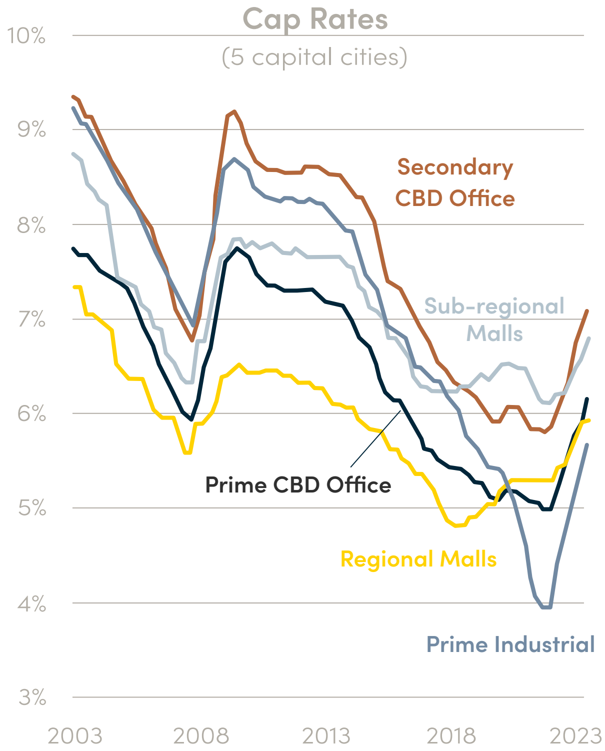
Sources: JLL REIS, MaxCap Group (January 2024)

Commercial capital markets are lagging for now.

- The marked increase in interest rates has driven a clear repricing of asset values across all commercial sectors, more reflecting higher costs of capital rather than individual sector fundamentals. **Cap rates** have continued to soften across the board, lifting from cyclically low levels.
- **Equity investors** are still making active reallocations, downweighting retail initially and office more recently, by leaning heavily into the industrial / logistics space.

- **Bank lending** allocations are also moving visibly, albeit on a slower, more measured basis, reducing residential and land development over the longer term and cutting office and retail exposures over more recent years.

Cap rates are rising with higher interest rates.



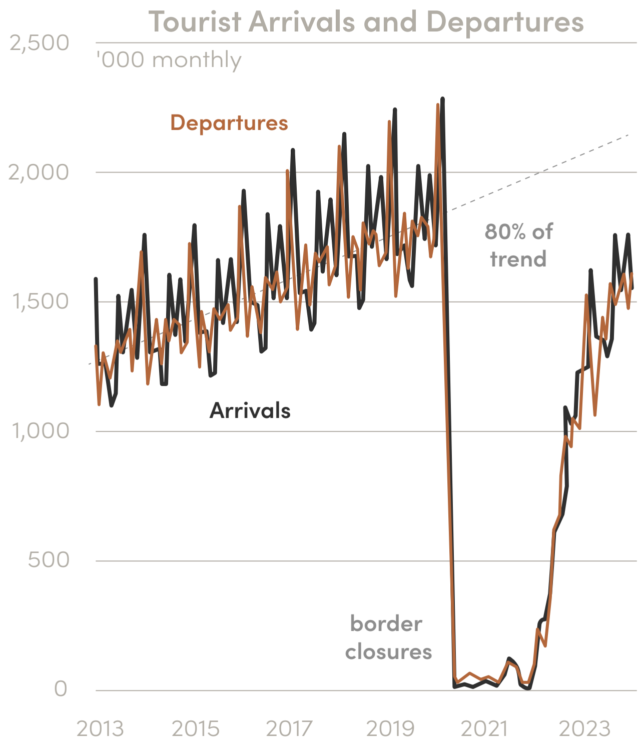
Sources: JLL REIS, MaxCap Group (January 2024)

SECTOR SPOTLIGHT

Local hotel markets see a roaring rebound.

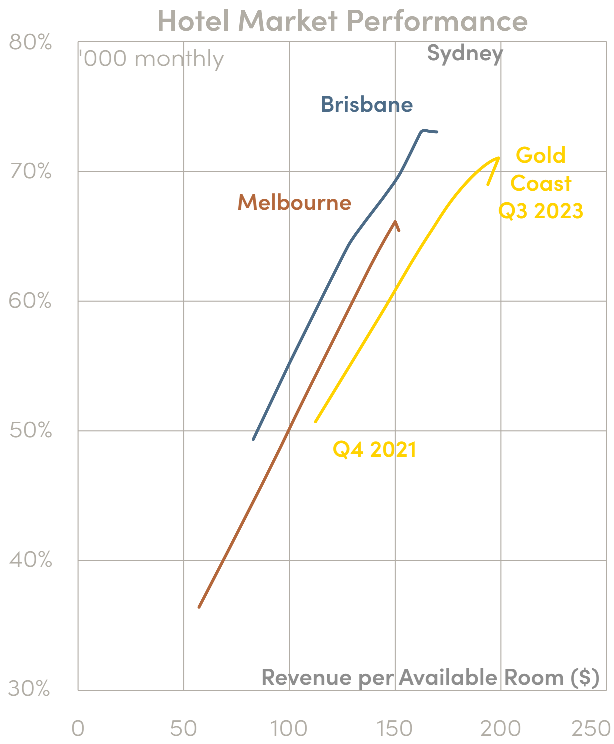
- After a difficult COVID lockdown period, the reopening of international borders has unleashed a sharp rebound in Australian **hotel markets**. The demand for travel and leisure remains strong, with appetite undiminished by higher mortgage rates and the associated drag on discretionary consumer spending.
- The resurgence in foreign and domestic visitor numbers has supported a massive recovery in **occupancy**. While rapid inflation supported the uplift in **room rates**. Certainly, local sporting and concert events have really helped the market rebound in 2023, including the FIFA Women's World Cup. Additionally, the move in Victoria to impose a 7.5% levy on short-term accommodation like Airbnb rentals are diverting some demand back towards traditional hotels.

Tourist flows see a dramatic rebound upon reopening.



Sources: ABS, MaxCap Group (January 2024)

Hotel performance has improved sharply.



Sources: Savills, STR, MaxCap Group (January 2024)

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