

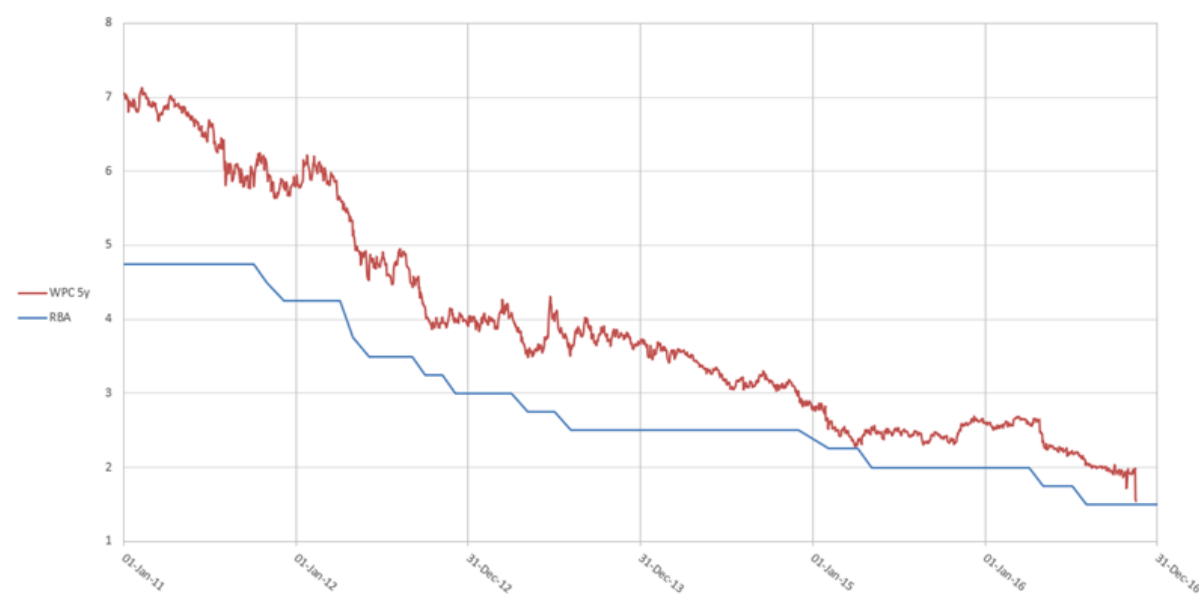
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## How to position your portfolio when rates fall

By Jacob Braddy

As the RBA considers when to finally cut interest rates, this presents an opportunity for investors to add longer dated, high coupon bonds and benefit from the potential capital upside, as it would appear these future rate cuts is a matter of when, not if. One way to highlight this opportunity is to look back to the RBA tightening cycle during the 2010's and see how certain bonds performed.

Over the span of six years, the RBA lowered interest rates from 4.75% in 2011, to 1.5% by 2017. As everyone is aware, this was primarily due to the fallout of the GFC on the global economy. Westpac had issued a 7.25% fixed rate bond in 2009 with a seven-year term. The chart below shows the Westpac bond yield versus the RBA cash rate movements, till the bond's maturity in 2016.



The chart clearly highlights as the RBA continued to cut rates, the yield on the Westpac bond significantly tightened as the price of the bond increased. The capital price eventually reached a high of \$112.84 from its issuance price of \$100 (see historical price chart below).



This is not a guarantee that similar bonds today will perform exactly as shown above – the RBA will eventually cut rates, but the pace at which they do so and the amount they reduce is yet to be determined. Nonetheless, the argument remains the same – long dated, high coupon bonds will outperform in a rate cutting environment. We have a high level of conviction in the list of investment grade bonds below, and believe it is worthy of strong consideration from investors.

Issuer	Payment Rank	Coupon Type	Coupon Formula	Rating (S&P, FITCH, MOODY)	Call Date	Maturity Date	Yield	Margin (TM/AS W)	Running Yield	Clean Price
NATIONAL AUSTRALIA BANK	Subordinated	FIXED	6.342%	A-,A-,A3	06-Jun-34	06-Jun-39	5.804%	1.748%	6.100%	103.973
WESTPAC BANKING CORP	Subordinated	FIXED	7.199%	A-,N/A,A3	15-Nov-33	15-Nov-38	5.774%	1.819%	6.539%	110.097
BANCO SANTANDER SA	Subordinated	FIXED	6.444%	BBB+,BBB,Baa2	17-Jul-29	17-Jul-34	5.643%	1.889%	6.232%	103.399
AUST & NZ BANKING GROUP	Subordinated	FIXED	6.124%	A-,A-,A3	25-Jul-34	25-Jul-39	5.894%	1.806%	6.021%	101.709
WESTPAC BANKING CORP	Subordinated	FIXED	6.934%	A-,N/A,A3	23-Jun-33	23-Jun-38	5.624%	1.672%	6.359%	109.037
COMMONWEALTH BANK AUST	Subordinated	FIXED	6.704%	A-,A-,A2	15-Mar-33	15-Mar-38	5.654%	1.697%	6.262%	107.064
AUST & NZ BANKING GROUP	Subordinated	FIXED	6.736%	A-,A-,A3	10-Feb-33	10-Feb-38	5.659%	1.703%	6.284%	107.185
HSBC HOLDINGS PLC	Subordinated	FIXED	6.211%	BBB,N/A,Baa1	21-Mar-29	21-Mar-34	5.477%	1.734%	6.033%	102.947

This is an opportunity for investors to add investment grade, high quality bonds while yields remain elevated, and position themselves to benefit once our cash rate does finally fall.

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