

RETURNS

The Elstree Hybrid Fund (“EHF1”) return for April was 1.11%, which was less than the market return of 1.24%. Another strong month was a result of continued confidence that economies would experience a soft landing and cash rates will stay high for a while: that’s a good combination for hybrids. The above income return occurred in a month where the equity market posted a c2% negative return. This level of outperformance is not common, and we expect it has a lot to do with the very healthy supply and demand characteristics. Most new issues allocate only 15% of bids, which indicates a degree of underlying demand.

PERFORMANCE FIGURES

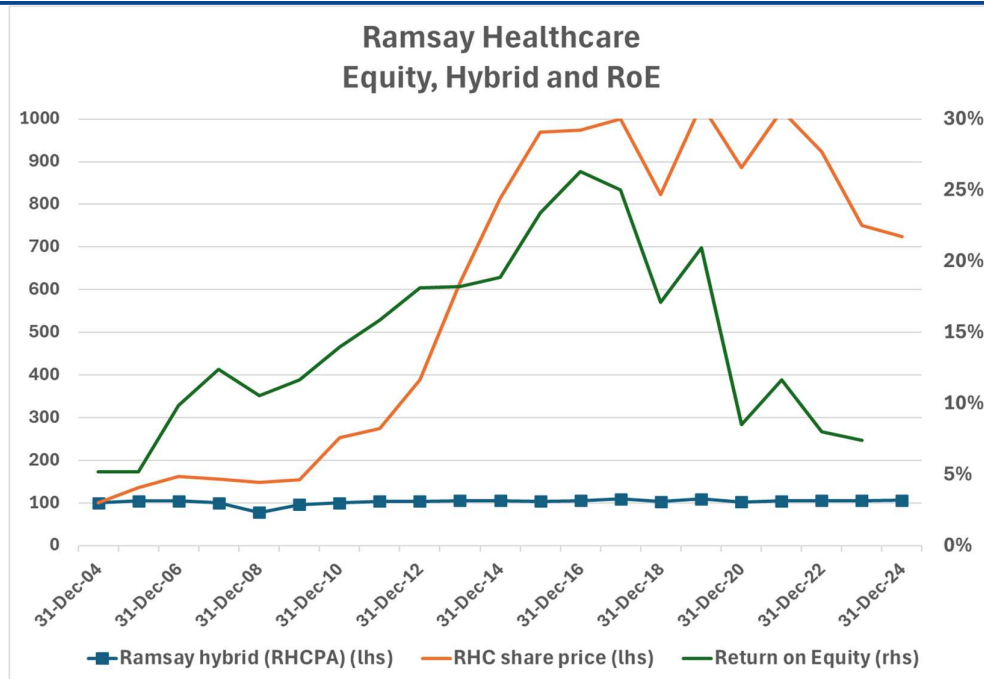
Performance as of 30 April 2024	1 month	3 months	1 year (p.a)	3 years (p.a.)
ELSTREE HYBRID FUND NAV + FRANKING (EHF1)	1.1%	3.4%	9.8%	6.2%
Distribution (cpu) (% franked)	1.8c (24%)	9.50c (59%)	31.7c (67%)	
Expected 3 month Income Distribution		5.80c (86%)		
ELSTREE HYBRID INDEX (P.A.) *	1.24%	3.40%	9.37%	5.7%
BANK BILLS	0.4%	1.1%	4.2%	2.2%

* Elstree Hybrid Index includes the value of franking credits.

ANATOMY OF A HYBRID ISSUER; RAMSAY HEALTHCARE

The Ramsay Healthcare CARES (RHCPA) is the oldest hybrid listed on the ASX with a May 2005 issue date. It is also the highest coupon security on issue. It now pays a margin of 4.85% over BBSW after the issuer didn’t call the security at its first call date in 2010. The RHCPA is an interesting illustration of what can happen to companies and what that means to their hybrids and what that means for hybrid values.

The RHCPA hybrid was issued to help fund Ramsay’s purchase of the Affinity Hospital Group. At that stage Ramsay was much smaller but it was the best hospital operator in Australia. At conferences, CEO’s of rival hospital groups would comment that their operational benchmark was Ramsay, and they never met the benchmark. Over the next few years, the share price went ballistic. The chart below shows the prices of Ramsay equity, the RHCPA (both lhs) and the Return on Equity (rhs) since 2005. The equity and hybrid are based to 100 (RHC share price in 2005 was c\$7: it reached \$70 and is now c\$50).



SO, WHAT HAPPENED THERE?

There is almost 1000 words in the chart above. The equity went bananas for a decade, was flat for another 5 years and then has lost 30% since then. It was one of the worst performing shares in 2023. The Return on Equity (RoE) line provides some clues. Ramsay became super profitable over the first decade of the hybrid and the share price followed. This was still the phase of Ramsay’s operational excellence, and hospitals were full all the time; there’s terrific occupancy leverage in hospitals and other accommodation industries; they all lose money at 70% occupancy and shoot the lights out at 90%. The hybrid performed like a debt instrument and even during the GFC, it was amongst the best performing hybrids, dropping to around \$80 but only for a short period.

Post 2015, the share price flattened and then fell materially, along with the RoE. The falls coincided with some ill-advised acquisitions in Europe and more recently, post Covid issues with hospital occupancy (and profitability): no one wants to stay overnight in hospitals anymore. The hybrid usually performed like a debt instrument, but the high coupon meant it performed well. The 5year annual return of 7.0% was well ahead of the Elstree Hybrid Index of 5.8% p.a. But it wasn’t a complete romp: because of the high coupon, there was always some incentive for the issuer to call the security at par and replace it. If it was trading at the post 2020 average price of \$104, that would have locked in a \$4 loss. In April 2022, KKR lobbed a bid in for RHC and the RHCPA fell 10% overnight. It wasn’t entirely clear how KKR and the existing RHC Board would treat the hybrid holders. The structural optionality of the hybrid meant that holders could potentially be put in a horrible position. Later in 2023 and 2024, Ramsay had debt and profitability and their investment grade credit rating was put on “watch”.

SO, WHAT DOES THIS ALL MEAN FOR UNITHOLDERS?

Our investment management process aims to identify cheap or fair value securities and hold an appropriate amount given the risk. At one stage, we loved the security. It wasn't well understood, it had just gained an investment grade credit rating which meant that the hybrid was not going to be called and it was cheap. We went from 1% weight to 5% and the price went up \$3 or \$4 as investors came to the same conclusion.

We got worried when KKR make a takeover offer. We don't trust Private Equity (PE) and the options in the RHCPA structure were all with the issuer. So, we sold down to 0.5% holding and we haven't bought back. We still get worried by PE or takeover by other parties given the woeful share price performance. We're not worried that it will be called given the material debt load RHC is carrying, so the c\$107 trading price is not too expensive. But it's not cheap enough yet, to justify increasing a position, given our assessment of the risks.

BBSW WATCH

March was boring, but it all livened up in early April after the US CPI release. That was higher than expected and US markets are placing a very low probability of more than 1 easing this year. US cash rates are 5.25%, which is the equal highest US cash rate this century. In 4 months, this period will take the crown as the longest period of high cash rates since 1997.

In Australia, markets pushed out the timing of the event a bit further. As the 4th column of the chart show, the expected average BBSW for 2 years is 4.1%, which implies only 1 cash rate cut in the next 2 years.

	ACTUAL 90DAY BBSW	HIGHEST EXPECTED 90DAY BBSW RATE	EXPECTED 2 YEAR AVERAGE BBSW	DATE OF HIGHEST 90DAY BBSW RATE
28 February 2022	0.1%	2.6%		June 2024
30 June 2022	1.8%	4.0%		June 2023
30 September 2022	3.1%	4.5%		December 2023
31 December 2022	3.3%	4.3%		December 2023
31 March 2023	3.6%	3.6%		December 2023
9 June 2023	4.2%	4.6%		December 2023
11 October 2023	4.1%	4.3%		June 2024
13 December 2023	4.3%	4.3%		June 2024
7 February 2024	4.3%	4.3%	4.0%	March 2024
6 March 2024	4.3%	4.3%	4.0%	March 2024
8 April 2024	4.3%	4.3%	4.1%	June 2024
6 May 2024	4.3%	4.3%	4.2%	September 2024

NEWS & MEDIA

Elstree Hybrid Fund (EHF1) has been mentioned in the following articles throughout the last six months, many of which are educational in nature.



- <https://www.livewiremarkets.com/wires/is-the-asx-home-to-the-longest-dividend-paying-company-in-the-world>
- [How Hybrids fit into 2021 Income Portfolios](#) – Campbell Dawson | Elstree Hybrid Fund
- [The Hitchhiker's Guide to Hybrids \(Part 1\)](#) – Bella Kidman | Livewire Markets
- [This is the secret to a diversified portfolio \(Part 2\)](#) – Bella Kidman | Livewire Markets
- [The forgotten asset class presenting exciting opportunities](#) – Bella Kidman | Livewire Markets



- [New Hybrid ETF on Chi-X](#) – Staff Reporter | Financial Standard



- [Hybrids remain attractive alternative for income generation](#) – Evergreen Ratings



- <https://www.firstlinks.com.au/hey-boomer-first-home-buyers-fuss>
- <https://www.firstlinks.com.au/bank-hybrids-equity-market-weakness>
- <https://www.firstlinks.com.au/ddo-change-hybrids-bank-treasurers-nightmare>
- [Fascinating Hybrid Journey Last Year](#) – Campbell Dawson | Elstree Hybrid Fund



- [Support for Elstree Hybrid Fund](#) – Staff Reporter | Money Management

More about Elstree Hybrid Fund (EHF1)

Elstree Hybrid Fund (CBOE Aust-X: EHF1) is an Exchange Traded Product or ETP. The fund is designed to allow retail investors to access the same successful and long-term investment strategy as our actively managed unlisted wholesale fund, the Elstree Enhanced Income Fund.

The Elstree Hybrid Fund is an ideal investment for investors seeking a cash or bank term deposit alternative investment that displays an acceptable and appropriate risk adjusted return outcome.

The Elstree Hybrid Fund has 'on market' liquidity provided by a market maker. The iNAV which is estimate of the live NAV, is updated every 20 seconds.

Additional details can be found on the [Elstree Hybrid Fund website](#) or email [Norman Derham](mailto:Norman.Derham) for further information.

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