January 2026 Review – Listed Hybrid Sector

Fund and market performance

The Elstree Enhanced Income Fund's investment return net of fees and including the value of franking credits for the month of January 2026 was 0.06% (over the 12months to 31 January it was 6.53%). This compares with the Elstree Hybrid Index return of 0.14%. In other markets the All-Ordinaries Accumulation Index returned 1.62% while the All Maturities Bond Index returned 0.21%.

"()" Denotes negative return outcome

While all are rowing the same way US "sell side" analysts are predicting the S&P500 will rise in CY2026. Should we be concerned about the unanimity? The contrarians would say yes.

Having concluded our December 2025 commentary and review with the statement "by all means spend your risk budget elsewhere" we thought it would be interesting to see what the collective thought of risk markets more broadly. The chart below sourced from the Financial Times is a summary of a survey conducted by Bloomberg on where "sell side" analysts (i.e stockbrokers) thought the US Benchmark S&P 500 Index would finish at the end of calendar year 2026. Of course, stockbrokers are renowned for their positivity and optimism – after all as firms they would be less likely to write much business if they weren't! What interests the author is the unanimity of the outcomes – all analysts surveyed are optimistic about the US Stock Market's trajectory in 2026. While some broking houses are more positive than others there is not one negative prediction among them. The foundation for the optimism has at its epicentre, additional US Federal Reserve interest rate cuts, closely followed by US Government tax cuts and of course the continued growth and impact on productively of artificial intelligence or AI. It's not hard to see where the optimism stems from. But is the unanimity something we should be concerned about? Certainly, the contrarian investor would argue there is. The contrarians would argue that because all the analysts are "rowing" in the same direction it only takes an earnings miss or a change in central bank sentiment to see things turn around quickly. And of course, the forecasts do not take into consideration the possibility of an event shock that might emanate from (say) unlisted private markets. The contrarian would also suggest that the market's expectations are priced in which makes absolute sense because equity markets are notoriously forward looking, typically 18months ahead of the real economy and data releases which of course are backward looking.

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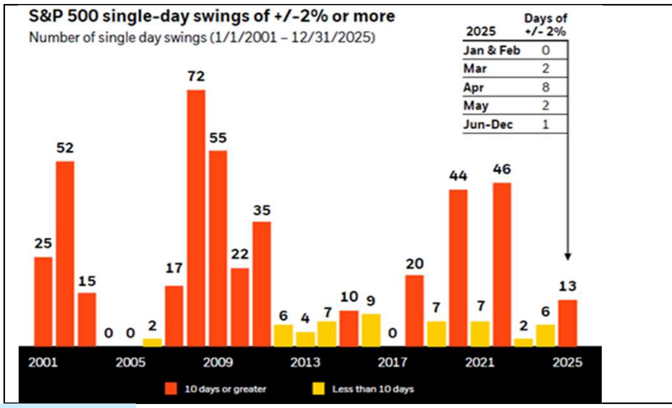
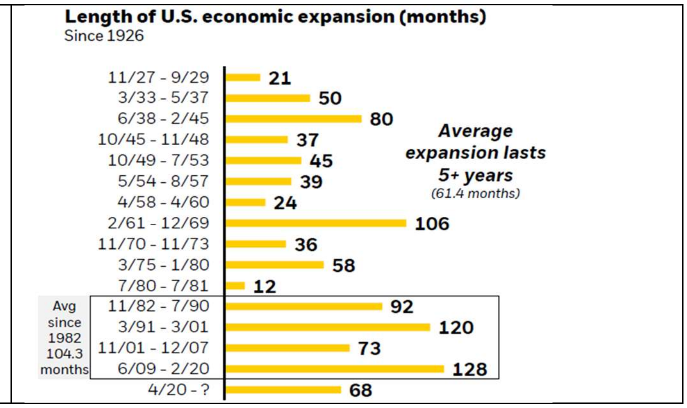
Bond and equity market volatility would suggest that for now investors are sanguine about risk

The author thought it sensible to seek out a tried tested independent source to determine if there is any validity in the markets' expectation for the S&P 500's trajectory in 2026. The author turned to Scott Grannis, the much-respected retired Chief Economist from Western Asset Management for "independent" input. The Bloomberg chart below which is sourced from Grannis' blog of 29 December details both the "Vix" and "Move" indices since just prior to the onset of covid in 2020. The "Vix" index being the volatility of equity market (S&P 500) options and the" Move" index being the volatility of treasury bond options. Paraphrasing Scott, *an increase in volatility drives the price of options higher, and vice versa. Because options reduce portfolio risk, they are keenly sort after during periods of heightened stress (and thus more expensive). The opposite is true during periods of less stress when they become cheap(er).* We can clearly see from the chart that both equity (white line) and bond (orange line) market option volatility are now very low which implies that the markets are sanguine about risk. So, on face value the markets are not expecting a disruptive event anytime soon, which, everything being equal should be interpreted as positive for risk markets.

….the data would seem to suggest that the S&P500 indeed has further to run

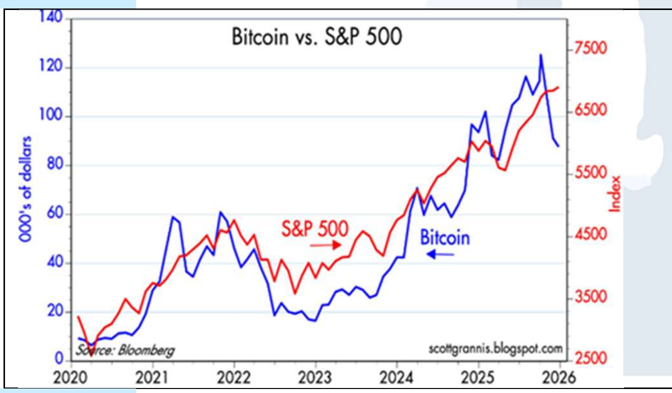
In support of low bond and equity market volatility the tables below and overleaf are sourced from a note compiled by Blackrock entitled "Inside the Market". The data (which is sourced by Blackrock from Morningstar) on the left-hand side is of the S&P500 and it details the number of volatile days as represented by +/- movements of 2% or more than 2% from 2001 to end 2025 while the right-hand chart details the length in months of US economic expansions since 1926. The key takeaways are that despite the volatility of Liberation Day in April, calendar year 2025 was not all that volatile, in fact if you were to strip out the month of April, where there were 8 +/- 2% events, 2025 would have been as un-volatile a year as the market had experienced this century. The data in the right-hand chart is interesting in that it demonstrates that the current economic expansion, which began in April 2020, is still relatively young at 68 months. While it is a fraction longer than the average, which is 61.4 months it still has some way to go to match the 10year expansion of 1991/2021 and the 11year expansion from 2009 to 2020! Both data sets are supportive of further S&P500 appreciation.

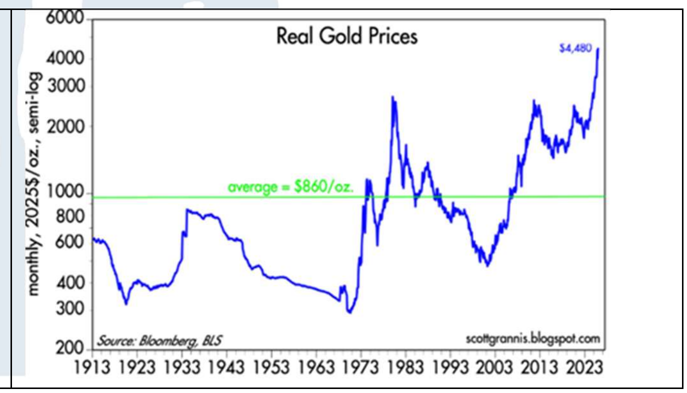




…as always there are some dark clouds on the horizon in the pricing behaviour of gold and bitcoin

In the interests of presenting a balanced view there are some potential dark clouds on the horizon with the charts below (once again) sourced from Scott Grannis. The left-hand chart details the relationship between Bitcoin and the S&P500 while the right-hand chart shows the real inflation adjusted price of gold. The left-hand chart suggests that the relationship between Bitcoin and the S&P500, which has been strong over the journey so far, looks like it might be about to break down. If the relationship is to hold true, either the S&P500 falls or Bitcoin goes back up. Just as Bitcoin has moved down the inflation adjusted price of gold has moved up! That, in and of itself is telling. While central banks have been accumulating gold since the covid period, was the most recent "over bought" spike due to the recycling of Bitcoin profits or was it due to speculation that President Trump's likely Federal Reserve Chair nomination would bring into question the Federal Reserve's independence, which of course had the potential to be disruptive to risk market pricing?





The markets are forgiving as new Fed chair nominee is announced. Meanwhile the RBA raises the cash rate

As if on cue, gold experienced its largest intraday fall since 1983, on news that President Trump had nominated Kevin Warsh to replace Jerome Powell as Federal Reserve Chair. The nomination of Warsh, an apparent "inflation hawk", allayed concerns that investors and speculators had about the nominee being sympathetic to Republican Party orthodoxy. While at home we note that the RBA raised the official cash rate (OCR) by 0.25% to 3.85% on Tuesday last setting the scene for another 0.25% rate rise timed for later this year. Of course, as an investor in instruments that pay a fixed coupon margin over a floating benchmark reference rate linked to the OCR this is excellent news. Average annual AT1 coupon rates, including franking credits, are now within spitting distance of 7%. While the average weighted yield to maturity (YTM) at current prices presents around 1% lower it is most attractive given the structural decline in risk typically associated with AT1 securities.

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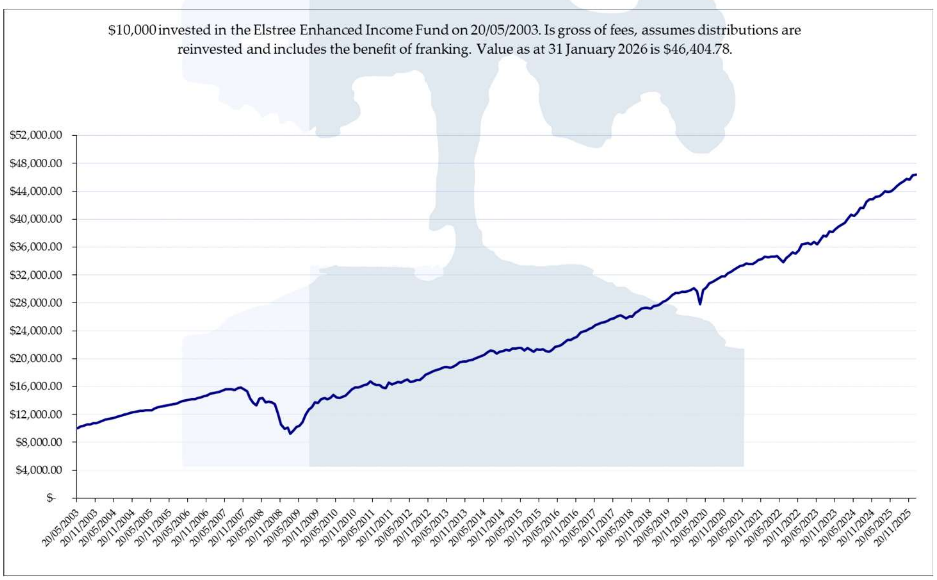
Elstree Enhanced Income Fund portfolio metrics as at (close of business) 31 January 2026

Performance Table	1 month	3 months	1 year	3years p.a.	5years p.a.
Elstree Enhanced Income Fund *	0.06%	1.22%	6.53%	7.66%	6.72%
Elstree Enhanced income Fund (Basis NAV)	0.06%	0.88%	4.94%	5.95%	5.33%
Betashares Hybrid Fund HBRD (Basis NAV)#	0.49%	1.12%	5.03%	5.45%	4.30%
UBS Australia Bank Bill Index	0.30%	0.91%	3.89%	4.12%	2.77%

Past performance is not necessarily a guide to future performance. *Is the "NAV" Plus franking.**"()"** denotes negative return outcome. # Source: Betashares. Betashares return is net of fees and does not include the value of franking credits.

Yield to Maturity (includes franking)	5.75%
Cash yield to maturity	4.90%
Credit term duration (average years)	3.65
Default cost (per annum)	0.07%
Investment grade issuer (% holding)	90.1%
Bank tier 1 exposure (% holding)	62.9%
Value at Risk (VaR)	3.09%

Value of $10,000 Invested on 20/05/2003



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