Product Assessment

Report as at 07 Mar 2024

RECOMMENDED

KKR Global Credit Opportunities Fund

Rating issued on 07 Mar 2024 | APIR: CHN2049AU

Investment objective

To outperform a hybrid benchmark, comprising 50% S&P/LSTA Leveraged Loan 100 Index and 50% ICE BofA US High Yield Index by 2% p.a. to 3% p.a. (gross) over a credit cycle.

Manager	KKR Australia Investment Management
Distributor	KKR Australia Investment Management
Sector	International Fixed Interest \ High Income
Investment Style	Active
RI Classification	Aware
Absolute Risk	High
Relative Risk	Opportunistic Credit
Investment Timeframe	5-6 Years
Benchmark	Bloomberg AusBond Bank Bill Index
Min Investment Amount	$300,000
Redemption Frequency	Monthly
Income Distribution	Monthly
Fund Size (31 Jan 2024)	$133.40M
Management Cost	0.82% p.a. Incl. GST
Performance Fee	N/A
Buy / Sell Spread	0.25% / 0.25%
Inception Date	01 Dec 2022

Fund facts

- Deep and highly-experienced investment team
- Focus on sub-investment grade securities
- Ability to opportunistically invest across a range of sub-sectors

Viewpoint

The Fund, managed by KKR, invests in a global portfolio of High Yield Bonds, Bank Loans, Structured Credit and Opportunistic Credit. Accessing the 'best ideas' from KKR's traded Credit platform, the portfolio management team seeks to generate Equity-like returns with a focus on managing the default risk of the underlying portfolio. In Zenith's opinion, KKR's proven expertise in the sub-investment grade sector and managing dislocated assets, positions the Fund as an attractive option, for those investors seeking more aggressive returns with attendant drawdown risk.

KKR's credit platform comprises 190 investment professionals and is led by San Francisco based Chris Sheldon, Co-Head of KKR Credit and Markets. In Zenith's opinion, Sheldon is a highly experienced investor and his contrarian mindset and ability to understand the intrinsic value of companies is a key contributor to the success of the underlying strategy.

The Global Credit Opportunities Fund (GCOF) is KKR's flagship credit strategy, representing the firm's highest conviction ideas, sourced from a broad investable universe that includes High Yield, Bank Loans, Structured Credit and Opportunistic Credit with the latter including Distressed Credit. Further, KKR can invest up to 20% of the portfolio in an 'Opportunistic Bucket' which includes the flexibility to purchase its Listed Investment Trust (LIT) (KKR Credit Income Trust (ASX code: KKC)) and other distressed opportunities including bilateral lending transactions.

Zenith highlights that the focus on sub-investment grade securities is a point of differentiation and adds a layer of specialisation to the investment process. In our opinion, the approach is more resource-intensive and requires a contrarian mindset given the focus is on understanding the default risk of a business.

In terms of composition, the portfolio comprises approximately 60 to 80 core holdings (including bonds and loans) with position sizes ranging between 1.5% and 4.0%. The final portfolio is managed with a credit spread duration range of between two and five years with a bias to senior secured securities which includes both loans and bonds. Consistent with the targeted opportunity set, KKR typically invests in lower quality credit securities with an indicative credit rating of B and CCC based on S&P's rating methodology.

Zenith notes that this cohort of securities is subject to a high level of mark-to-market volatility and potential default risk, particularly during stressed equity periods or cyclical downturns. Accordingly, investment outcomes will be closely tied to the quality and depth of KKR's bottom-up due diligence process. To this end, Zenith highlights that KKR has consistently outperformed the CCC component of the broader high yield indices, achieving higher returns and at the same time, demonstrating superior capital preservation qualities (i.e. lower default experience).

As detailed earlier, the team has the flexibility to purchase units in KKC, which potentially serves the dual purpose of enhancing the liquidity profile of the the portfolio and also generating performance through acquiring units at a discount to the underlying net tangible assets (NTA) (assuming that the price converges to the NTA over time).

Zenith is supportive of the approach if used on a selective basis and in the 'best interests' of unitholders. We are cognisant that the allocation could be used as a tool to control the NTA discount and potentially result in 'listed equity beta' being imparted in the Fund's return outcomes. Zenith will continue to monitor this, highlighting KKR's strong governance framework and the role of the external Responsible Entity in overseeing the process.

Fund analysis

Fund characteristics

Constraint	Value
Cash (%)	0% to 100%
Sub-Investment Grade (%)	Up to 100%
Currency Constraints	GCOF (AUD) will be hedged back to Australian dollars. GCOF (AUD) does not take active currency risk or bets within the market other than to hedge out currency risk.

Investment objective and philosophy

The Fund's investment objective is to outperform a hybrid benchmark, comprising 50% S&P/LSTA Leveraged Loan 100 Index and 50% ICE BofA US High Yield Index by 2% p.a. to 3% p.a. (gross) over a credit cycle. In terms of absolute returns, and subject to the prevailing Cash rate, this is expected to result in a return range of between 8% p.a. and 10% p.a. (pre-fees) over the long-term.

The investment philosophy is premised on the belief that intensive bottom-up credit analysis is a sustainable source of excess returns, particularly when applied with a capital preservation focus. KKR's approach is centred on its fundamental analysis of a company/issuer, including detailed historical and projected financial modelling. In our opinion, given KKR's presence across public and private markets, the firm is well positioned to assess the enterprise value of a company with both a private and public lens.

Zenith highlights that the focus on sub-investment grade securities is a point of differentiation and adds a layer of specialisation to the investment process. In our opinion, the approach is more resource-intensive and requires a contrarian mindset given the focus is on understanding the default risk of a business. This differs to traditional investment grade investing where the assessment is generally more relative-value based and understanding the relationship between spread and the potential for ratings changes.

The GCOF strategy represents the firm's 'best ideas' from across KKR's traded Credit platform including High Yield, Bank Loans, Structured Credit and Opportunistic Credit. KKR can invest up to 20% of the portfolio in an 'Opportunistic Bucket' which includes the ability to purchase its Listed Investment Trust (LIT) (KKR Credit Income Trust (ASX code: KKC)) and other distressed opportunities including bilateral lending transactions.

The portfolio managers employ a range of bottom-up strategies, which are classified based on the following:

- **Event Driven** - identifying securities with short-term catalysts for price appreciation which can include mergers and acquisition activity, restructuring and/or positive ratings movements
- **Dislocation/Relative Value** - high yielding securities from companies experiencing earnings/revenue challenges and/or its underlying sector is facing structural challenges
- **Proprietary Sourcing** - leveraging the firm's industry networks to access niche financing opportunities, which can include cornerstone or large block trades
- **Stressed Credits** - distressed companies that require refinancing or restructuring of debt arrangements. Typically these companies operate in structurally challenged industries or sectors going through transition
- **Structured Credit** - can include a range of Structured Credit opportunities, including investing in lower tranches of Collateral Loan Obligations (CLOs)
- **Illiquidity premium** - typically smaller businesses or industries, that are more illiquid and less frequently traded, thereby offering a market premium

The Event Driven and Dislocation/Relative Value allocations strategies are expected to account for the majority of portfolio risk, however the underlying portfolio weightings will change over time and reflect the prevailing opportunity set.

In sum, the GCOF strategy draws on the extensive network of the broader KKR business. In our opinion, the quality and depth of the bottom-up due diligence process, enables the portfolio management team to invest lower down the risk continuum to generate attractive risk-adjusted returns.

Portfolio applications

KKR manages a Credit-focused Fixed Income strategy, investing in high yield securities on an opportunistic basis. While the investable universe is relatively broad, KKR's focus is on sub-investment grade securities with a bias towards on US and European Credit markets.

The Fund provides exposure to an actively-managed Credit strategy that invests across a broad range of global spread sectors, including US and European High Yield, Bank Loans and Structured Credit.

Zenith believes the Fund may be suitable for investors seeking exposure to a higher yielding portfolio with 'Equity like' return expectations which may improve a portfolio's potential risk/return profile. However, given the Fund can invest in sub-investment grade and unrated assets, it may not be suitable for the more risk-averse investor.

From a portfolio perspective, the Fund may be suitable as a component in the income-producing portion of a well-diversified portfolio. The Fund is considered appropriate as a component of a defensive allocation; however, given the higher return and volatility profile of the strategy, Zenith believes that investors may partly fund the allocation from the growth portion of a portfolio. Due to the anticipated moderate to high levels of volatility, with the potential for capital losses, Zenith recommends taking a medium to long-term investment time frame.

The Fund should be treated as an illiquid investment with investors subject to a redemption cap of 20% of the Fund's net asset value (NAV) per month, processed on a 'pro rata basis'.

Fund responsible investment attributes

Key Information	Description
Zenith RI classification*	Aware
Has Responsible Investment Policy	Yes
PRI Status	

Key Information	Description
PRI Signatory	Yes

*Zenith RI Classification scale:

- Traditional
- Aware
- Integrated
- Thematic
- Impact

Absolute performance

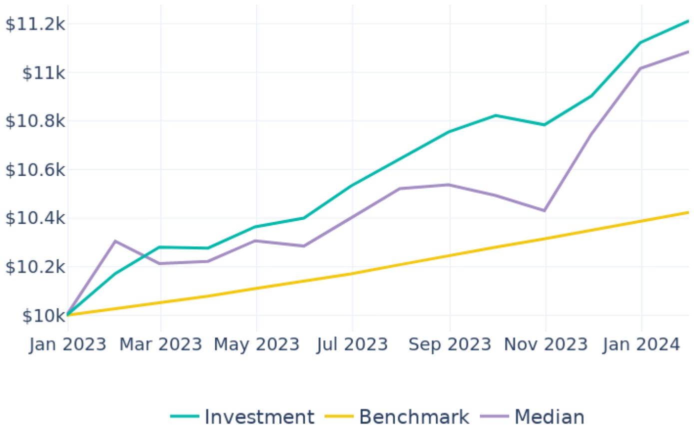
Performance as at 31 Jan 2024

Monthly performance history (%, net of fees)

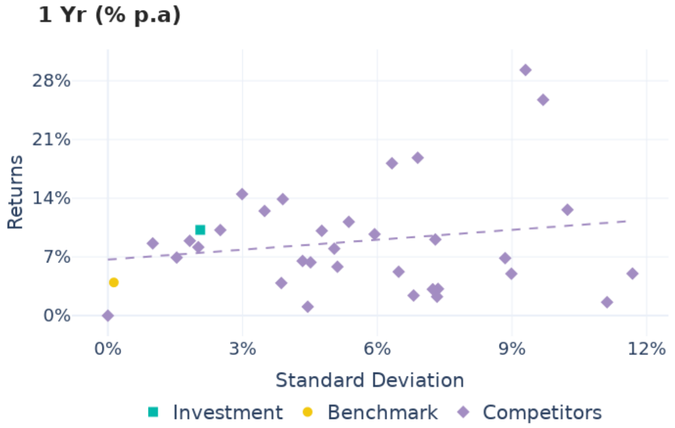
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD	BM YTD*
2024	0.81%												0.81%	0.37%
2023	1.72%	1.07%	-0.04%	0.85%	0.35%	1.27%	1.07%	1.03%	0.63%	-0.35%	1.10%	2.01%	11.22%	3.85%

Bloomberg AusBond Bank Bill Index

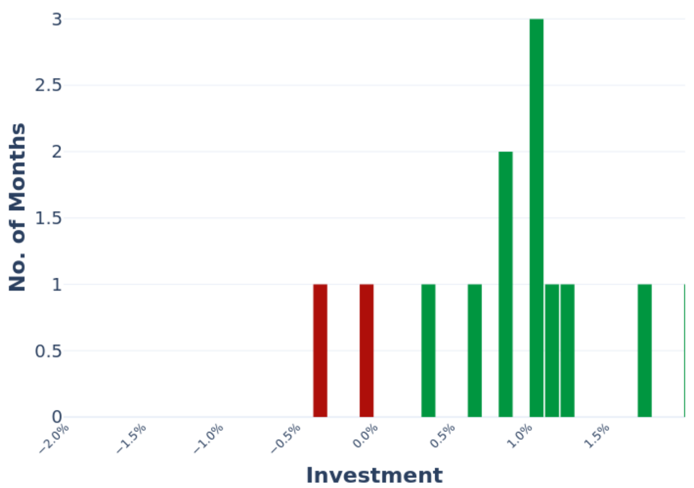
Growth of $10,000



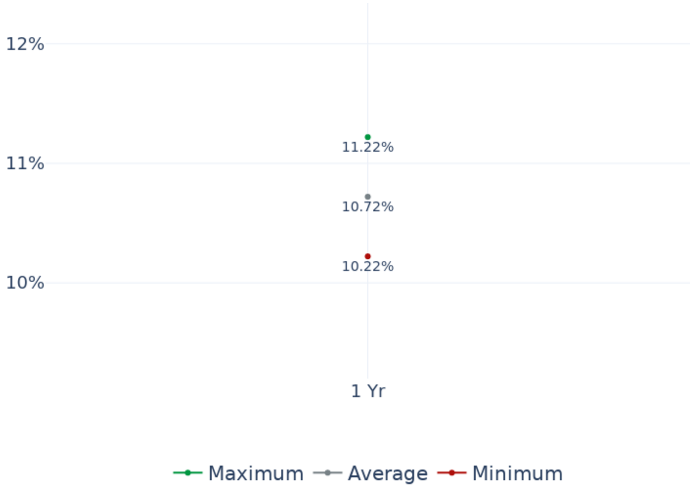
Risk / return



Monthly histogram



Minimum and maximum returns (% p.a.)



Absolute performance analysis

Instrument	1 Mth	3 Mths	6 Mths	1 Yr	Inception
Investment	**0.81%**	**3.97%**	**5.33%**	**10.22%**	**11.14%**
Income	-0.00%	1.55%	3.59%	7.09%	6.61%
Growth	0.81%	2.42%	1.74%	3.14%	4.52%
Benchmark	**0.37%**	**1.06%**	**2.11%**	**3.96%**	**3.90%**
Median	**0.63%**	**6.27%**	**5.36%**	**7.57%**	**9.98%**
Cash	**0.37%**	**1.06%**	**2.11%**	**3.96%**	**3.90%**

Ranking within sector (p.a.)

Ranking within Sector	1 Yr	Inception
Fund Ranking	8 / 33	12 / 34
Quartile	1st	2nd

Absolute risk

Instrument	1 Yr	Inception
Standard Deviation (% p.a.)		
Investment	2.06%	2.15%
Benchmark	0.13%	0.14%
Median	3.99%	4.44%
Downside Deviation (% p.a.)		
Investment	0.35%	0.34%
Benchmark	0.00%	0.00%
Median	1.17%	1.12%

Absolute risk/return ratios

Instrument	1 Yr	Inception
Sharpe Ratio (p.a.)		
Investment	3.04	3.37
Benchmark	0.00	0.00
Median	0.91	1.37
Sortino Ratio (p.a.)		
Investment	17.71	21.29
Benchmark	NaN	NaN
Median	3.10	5.43

Zenith benchmarks funds within the 'International Fixed Interest - High Income' peer-group against the Bloomberg AusBond Bank Bill Index. While this benchmark may not be consistent with the one adhered to by all sector participants, it has been adopted to provide investors with a common reference point against which the performance of similarly structured strategies may be assessed.

The following commentary is effective as at 31 January 2024.

The Fund's aim is to provide investors with a total return (before fees) of between 2% p.a. to 3% p.a. in excess of a composite benchmark (50% LSTA Loan Index / 50% BAML HY Index) over a credit cycle.

Given the recent inception date of the Fund, there is insufficient performance history to draw any meaningful conclusions. Notwithstanding this, KKR has managed the GCOF strategy since 2008. Over this period, the strategy has performed in line with Zenith's expectations.

Relative performance

Excess returns

Statistic	1 Mth	3 Mths	6 Mths	1 Yr	Inception
Excess Return	0.44%	2.91%	3.22%	6.26%	7.23%
Monthly Excess (All Mkts)	100.00%	100.00%	83.33%	83.33%	84.62%
Monthly Excess (Up Mkts)	100.00%	100.00%	83.33%	83.33%	84.62%
Monthly Excess (Down Mkts)	0.00%	0.00%	0.00%	0.00%	0.00%

Capture ratios (% p.a.)

Statistic	1 Mth	3 Mths	6 Mths	1 Yr	Inception
Downside Capture	0.00%	0.00%	0.00%	0.00%	0.00%
Upside Capture	218.39%	371.83%	249.53%	251.35%	276.58%

Tracking error (% p.a.)

Instrument	1 Yr	Inception
Investment	2.04%	2.15%
Median	3.94%	4.43%

Information ratio

Instrument	1 Yr	Inception
Investment	3.07	3.36
Median	0.92	1.37

Beta statistics

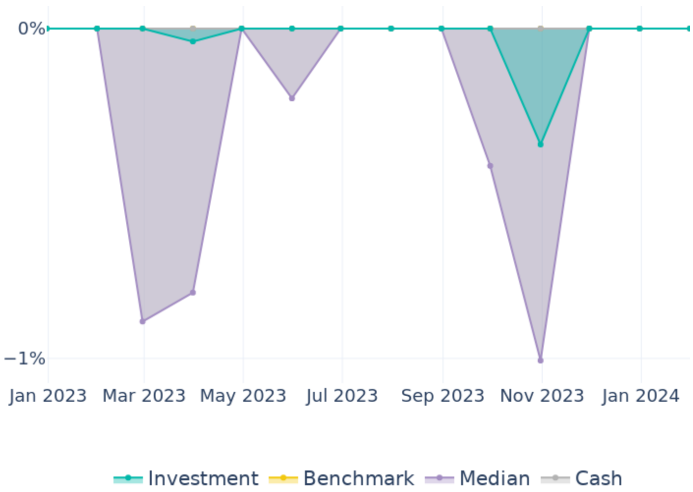
Statistic	1 Yr	Inception
Beta	2.22	-0.45
R-Squared	0.02	0.00
Correlation	0.14	-0.03

The following commentary is effective as at 31 January 2024.

Zenith typically seeks to identify funds which can outperform their index in greater than 50% of months as we believe this represents a persistence of manager skill. The Fund has an insufficient performance history to draw any meaningful conclusion as to its performance.

Drawdown analysis (since inception)

Drawdown analysis assesses the relative riskiness of a Fund versus the benchmark, in reference to capital preservation. The maximum Drawdown is recorded as the percentage decline in the value of a portfolio from peak to trough (before a new peak is achieved). All Drawdown analysis is calculated commencing from the inception date of the Fund in question, and Drawdown analysis for the Fund and benchmark(s) are calculated independently. That is, the largest drawdown for the Fund and benchmark(s) will not always refer to the same time period.



The following commentary is effective as at 31 January 2024.

Given the recent inception date of the Fund, there is insufficient performance history to draw any meaningful conclusions on the Fund's potential drawdown profile.

Fund commentary

Fund risks

Zenith has identified the following key risks of the Fund. Although Zenith believes the risks noted are all significant, we have listed them in order of importance. In addition, we have not intended to highlight all possible risks.

Key person risk: Given the collegiate nature of the team, Zenith considers key person risk to be moderate. However, if Chris Sheldon or Jeremiah Lane, Head of US Leveraged Credit were to depart, this would warrant a reassessment of our rating.

Volatility risk: KKR retains the flexibility to invest up to 20% of the portfolio (soft limit) via its ASX-LIT, the KKR Credit Income Trust (ASX Code: KKC). Subject to market conditions, this has the potential to materially contribute to volatility and performance drawdowns, particularly during risk off environments.

Limited redemption risk: Investors are subject to a cap on net redemptions of 20% of the Fund's net asset value (NAV) per month, processed on a 'pro rata basis'.

Liquidity risk: As an over-the-counter 'private market', liquidity can vary significantly through different market conditions. Investors should be aware that while the Fund's PDS states that it has monthly liquidity, in certain market conditions KKR may be unable to meet redemption requests. Given the liquidity risks associated with the asset class, Zenith believes that the Fund should not be relied upon as a short-term liquidity vehicle.

Sub-investment grade credit risk: By its nature and as reflected by its rating, sub-investment grade debt has a higher potential of default. Although investors have historically been compensated, in the form of excess returns, there is the potential for the strategy to experience more defaults than the broader market. Additionally, defaults tend to cluster in certain years and therefore investors should expect periodic episodes of higher defaults. Nevertheless, given the Fund holds a significant proportion of sub-investment grade debt, investors should be aware of the increased risk involved in this allocation.

Relative performance risk: Investors should also acknowledge that the Fund may underperform traditional bond funds and those benchmarked against domestic or global bond indices in a falling interest rate environment, or in an environment where Credit performs poorly relative to Government Bonds.

Security/asset selection

The security selection process is based on traditional bottom-up credit analysis with the following section outlining the key steps of KKR's approach.

The first step involves sourcing potential investment opportunities which are identified across a range of channels and networks. KKR's global network of CEO's managing large companies, co-investors, advisory firms and other intermediaries all provide a source of investment ideas. As detailed earlier, investment opportunities can range from companies experiencing short-term liquidity needs, seeking M&A financing and/or industries facing transient challenges.

Each opportunity is supported by deep diligence analysis, with a clear investment thesis is identified and formalised in a proposal. While the approach varies based on the nature of the investment (i.e. loan or bond), it typically includes traditional financial statement and pro forma analysis and qualitative research with a focus on understanding a borrower's operating environment.

The analysis includes a comparison with the broader peer group, both in terms of pricing and risk. With respect to qualitative research, some of the key metrics assessed include industry structure, management strategy and governance, corporate structure, capital structure of the firm (i.e. level of subordination and equity support) and the level of operational risk. In terms of durability of earnings, each proposal includes earnings stress tests under a number of downside scenarios.

Prior to investment, all Investment Committee (IC) memos are reviewed and ratified by the U.S. Leveraged Credit Investment Committee, which is responsible for approving and maintaining eligible securities on an approved security list.

In our opinion, the quality and depth of KKR's bottom-up research process is a key competitive advantage, particularly when assessed relative to the nature of the underlying investments (i.e. sub-investment grade or potentially dislocated assets). Further, the role of the committee in reviewing and approving all submissions adds a layer of oversight.

Responsible investment approach

KKR has been a signatory to the United Nations Principles for Responsible Investment (PRI) since 2009.

KKR has an established Responsible Investment Policy (RIP) that was last updated in June 2023. The firm's senior leadership provides ultimate oversight of its responsible investment efforts, while an internal Global Public Affairs team, represents the core of the environmental, social and governance (ESG) related expertise. Where applicable, the IC oversees ESG issues that are material to an investment, both on a pre and post-investment basis.

ESG considerations are not formally assessed, however, where ESG risk has the potential to impact a company's earnings and profitability, this will be considered as part of the due diligence process. When material issues are identified, they will typically be explored and discussed at the IC, with the option of appointing specialist ESG advisors to undertake additional due diligence. In the instance where ESG-related risks have been identified, a detailed remediation plan will be outlined and agreed upon, and remain a standing item for the IC until resolution.

In Zenith's opinion, while ESG is considered as part of the due diligence process, the approach is less invasive relative to the broader peer group.

Portfolio construction

Responsibility for portfolio construction rests with Sheldon and Lane, who continuously review the composition of the portfolio and key risk drivers. This process is supported by a number of regular forums including daily monitoring meetings where analysts, portfolio managers and traders discuss market thematics and potential investment ideas.

The eligible universe include all those securities that are approved by the IC and have passed KKR's formal bottom-up due diligence process. In determining security weightings, Sheldon and Lane consider a range of factors including analyst conviction, dispersion of upside and downside scenarios, relative value, portfolio diversification and issuer concentration limits.

In terms of portfolio composition, the portfolio comprises 60 to 80 core holdings (including bonds and loans) with position sizes ranging between 1.5% and 4.0%. The final portfolio is managed with a credit spread duration range of between two and five years with a bias to senior secured securities. Consistent with the targeted opportunity set, KKR typically invests in lower quality credit securities with an indicative credit rating of B and CCC based on S&P's rating methodology.

Zenith notes that this cohort of securities is subject to a high level of mark-to-market volatility and potential default risk, particularly during stressed equity periods or cyclical downturns. Accordingly, investment outcomes will be closely tied to the quality and depth of KKR's bottom-up due diligence process. To this end, Zenith highlights that KKR has consistently outperformed the CCC component of the broader high yield indices, achieving higher returns and at the same time, demonstrating superior capital preservation qualities (i.e. lower default experience).

Based on the current Fund size of $A 133 million (as at 31 January 2024) the portfolio is yet to reach its optimal level of diversification, which KKR estimates will be achieved at a FUM level of approximately $US 100 million. Consequently, the portfolio is more concentrated with higher idiosyncratic risk expected to drive performance outcomes relative to KKR's flagship portfolios. Further, given KKR's contrarian approach and willingness to purchase distressed securities in dislocated markets, it is difficult to construct a portfolio that perfectly replicates its offshore flagship strategy.

In Zenith's opinion, the current portfolio is appropriately structured achieving diversification across issuers, sectors, country and ratings buckets. Over time, we expect the maturity of the portfolio will improve and more closely replicate KKR's offshore flagship strategies.

As detailed earlier, the team has the flexibility to invest up to 20% of the portfolio in an 'Opportunistic Bucket' which includes purchasing units in KKR's LIT (ASX: KKC) and other distressed opportunities including bilateral lending transactions. The allocation serves a dual purpose of enhancing the liquidity profile of the GCOF portfolio and also generating performance through acquiring units in the LIT at a discount to the underlying net tangible asset value (NTA), assuming that the price converges over time.

Zenith is supportive of the approach if used on a selective basis and in the 'best interests' of unitholders. We are cognisant that the allocation could be used as a tool to control the NTA discount and potentially result in the transmission of 'listed equity beta' in to the return outcomes of an unlisted fund. Zenith will continue to monitor this, highlighting KKR's strong governance framework and the role of the external Responsible Entity (Channel Investment Management Ltd) in overseeing the process.

The Fund's Currency exposure is expected to be hedged back to Australian dollars with the process supported by a proprietary Currency management tool. This system allows KKR to monitor foreign exchange exposures against derivatives and liability-based hedges at the Currency, portfolio and asset levels.

Overall, Zenith considers KKR's portfolio construction process to be well-structured and consistent with attaining the Fund's investment objective. Further, the portfolio management team has a proven track record in managing sub-investment grade portfolios and the attendant risk and liquidity challenges.

Risk management

The risk management process is largely an outworking of the firm's application of its investment selection process, which is complemented by issuer and diversification limits.

Zenith highlights that the GCOF portfolio is managed with no formal limits or restrictions, albeit in practical terms, the portfolio is highly diversified across issuers and sectors. In our opinion, this aspect of the process could be enhanced with the inclusion of a range of position, asset class, sector, industry and quality limits.

The Risk team comprises four Risk Managers with a reporting line to KKR’s Market Risk Committee. The team utilises a number of risk management tools and is integrated with the investment team to promote real-time discussions between portfolio managers, analysts and traders. The firm uses a range of external tools including FactSet, Black Mountain, Risk Metrics and Credit QB.

In terms of external oversight, the Fund is subject to the governance and compliance structures designed by the RE (Channel Investment Management Limited). The RE has formulated a monitoring and review process to ensure adherence to service agreements, including minimum standards. The Fund will be externally audited by PricewaterhouseCoopers, including an audit of KKR's adherence to its obligations under its AFS Licence.

Overall, Zenith believes KKR's risk management framework is sound and consistent with best practice.

Investment fees

	Fund	Sector Average
Total Fees and Costs (RG 97)	0.82% p.a.	0.89% p.a.
Management Fees and Costs	0.82% p.a.	0.82% p.a.
Transaction Costs	Not disclosed	0.10% p.a.
Performance fees	N/A	0.00%
Performance fees description	N/A	
Management Cost	0.82% p.a.	0.85% p.a.
Buy / Sell spread	0.25% / 0.25%	0.16% / 0.17%

All fees and costs are inclusive of GST unless indicated otherwise. The Performance Fee shown is the performance fee disclosed in the PDS. It is calculated by taking the average performance fees charged over the last five financial years (or less if the investment or performance fee mechanism has not been in place for five financial years).

The sector average is based on the average management fee of all funds within the International Fixed Interest - High Income sector as surveyed by Zenith.

Zenith believes the cost structure is in line with the peer group and reflective of the specialised nature of the asset class and investment approach.

In terms of applications and redemptions, a buy/sell spread of 0.25% is payable.

(The fees mentioned above are reflective of the flagship version only, fees may differ when the product is accessed through an alternate investment vehicle such as a platform.)

About the fund manager

Organisation

KKR was founded in 1976 by Jerome Kohlberg, Henry Kravis and George Roberts with its origins as a private equity firm. In 2010, the firm listed on the New York Stock Exchange (NYSE) and over time, has expanded its business activities and currently includes a Private, Public and Capital Markets divisions. While each business unit operates autonomously, a range of support functions are shared across the business including: KKR Capstone - a dedicated business unit that works closely with portfolio managers to extract operational efficiencies across portfolio companies; and a Stakeholder Management team, which is responsible for ensuring that all investment transactions are executed and managed in accordance with best practice.

As at 30 September 2023, KKR managed approximately $US 528 billion, which includes approximately $US 298 billion across its PE platform. The PE division comprises around 300 investment professionals based in 17 countries.

A key tenet of KKR's value proposition is the level of co-investment with investors, which has exceeded $US 28 billion (as at 30 September 2023), including both the firm's proprietary investments and capital invested by employees. Zenith is supportive of the level of commitment, which in our opinion, aligns the interests of investors to that of portfolio managers.

KKR currently manages $US 133 million in the Australian open-ended Fund (as at 31 January 2024).

Investment personnel

Name	Title	Industry Experience (yrs)	Tenure (yrs)	Location
Chris Sheldon	Co-Head of Credit and Markets	26	20	San Francisco, USA
Jeremiah Lane	Head of US Leveraged Credit	23	19	San Francisco, USA
Terry Ing	Co-Head of Research	24	4	San Francisco, USA
John Reed	Head of Trading for KKR Credit	27	15	San Francisco, USA

KKR's Credit platform comprises 190 investment professionals and is led by San Francisco based Chris Sheldon, Co-Head of KKR Credit and Markets. The team is primarily based in San Francisco and London and broadly divided into Portfolio Management, Sector Analysts, Trading and Portfolio Construction and Quantitative Insights.

Sheldon originally joined KKR in 2004 and maintains responsibility for the firm's Leveraged Credit, Private Credit and Strategic Investments Groups. In addition, he is a member of a number of key committees including the US Leveraged Credit and the Global Private Credit Committees. Prior to KKR, Sheldon worked at Wells Fargo as part of the High Yield Group.

In Zenith's opinion, Sheldon is a highly experienced and well-credentialed investor. In our opinion, his contrarian mindset and ability to understand the intrinsic value of a business is a key contributor to the success of the underlying strategy.

On a day-to-day basis, Jeremiah Lane, Portfolio Manager and Partner works closely with Sheldon to manage the portfolio's positioning and individual security selection. Lane joined KKR in 2004 and maintains responsibility for a number of the firm's Leveraged Credit strategies.

Zenith highlights Lane's contribution to the strategy's long-term track record and his ability to extract the 'best ideas' from across the KKR Credit platform. In our opinion, his ability to identify mispriced assets in dislocated environments and invest with an appropriate investment horizon, has been a key source of outperformance.

KKR's investment teams are supported by a well-defined governance structure, with a number of investment committees responsible for both approving investments and monitoring the composition and performance of underlying portfolios. At the highest level, a Credit Portfolio Management Committee is ultimately responsible for the performance of all KKR funds including adherence with investment guidelines and limits.

At the strategy level, a U.S. Leveraged Credit Investment Committee is responsible for approving and maintaining eligible securities for the GCOF portfolio. Zenith is supportive of KKR's investment structure, noting the additional layer of governance from the committee approach. While each committee is effectively a sub-set of senior investment professionals, the centralised decision-making structure ensures that all proposals are rigorously tested prior to investment.

An IC of four senior partners from KKR Credit has been established to oversee the implementation of the Fund's investment strategy and ensure the portfolio is managed in accordance with its stated investment objectives. The IC comprises Sheldon, Lane, Terry Ing, Co-Head of Research and John Reed, Head of Trading for KKR Credit.

KKR's remuneration structure is based on a global approach where firm-wide profitability is used as the basis for all incentive payments. Senior members of the investment team receive an industry-benchmarked salary and are also eligible for a Cash bonus and Equity. The Cash bonus/Equity component is discretionary and reflects a combination of firm and business unit performance, individual contribution and the performance of underlying funds managed.

To retain staff over the long-term, bonus payments are vested over multiple years and also include a portion that invests in underlying KKR funds under a system internally referred to as 'Dollars at Work'. In simple terms, the 'Dollars at Work' structure means that the economic return derived from the KKR investments changes over time, in line with each employees' overall contribution to performance. In our opinion, the approach embeds a strong co-alignment of interest, ensuring investment performance and remuneration are closely tied.

In sum, Zenith is supportive of the resourcing structure, effectively combining specialist bottom-up investors with a strong governance framework and a range of ancillary support functions. Further, the portfolio management team's counter-cyclical approach to building the portfolios is a key competitive advantage and contributed to the underlying strategy's long-term track record.

About the sector

Sector characteristics

The Zenith 'International Fixed Interest – High Income' sub-sector consists of all funds that invest predominantly in the higher-yielding sectors of the Global Fixed Interest market. These sectors typically include High Yield, Securitised Loans and Emerging Market Debt. The category includes funds that invest in specific underlying markets or a combination of each. Given the idiosyncratic nature of the sectors, managers commonly add value through security selection and/or sector rotation.

Zenith benchmarks all funds in this space against the Bloomberg AusBond Bank Bill Index. However, Zenith only uses this benchmark as a common reference point and it may not be reflective of the underlying benchmark used by many managers in this category.

It should be noted that the Bloomberg AusBond Bank Bill Index is typically used as a benchmark to measure the investment performance of a passively managed Short-Term Cash portfolio. The Index has an average term to maturity of approximately 45 days. It comprises 13 domestic bank bills of equal face value, each with a maturity seven days apart.

Given the funds in the 'International Fixed Interest – High Income' sector invest in longer dated, higher default risk securities, they will potentially display higher downside volatility relative to the Zenith assigned Index (i.e. while the Index is used as a performance benchmark, it should not be used as an indication of the risk involved in investing in the sector).

Sector risks

Funds within the 'International Fixed Interest – High Income' sub-sector are exposed to the following broad risks:

Market risk: Changes in economic, technological, environmental or political conditions and market sentiment may lead to a decline in general security prices and overall market volatility. During a general downturn in the securities markets, multiple asset classes may decline in value simultaneously.

Interest rate risk: Fixed Interest securities are generally sensitive to changes in interest rates. An increase in interest rates may result in a fall in the value of these securities, while a decrease in interest rates can result in an increase in value.

Credit spread risk: In addition to being sensitive to general interest rate changes, non-government securities are also sensitive to changes in credit spreads (commonly the difference in yield between a Government Bond and a Corporate Bond). A widening of spreads results in a fall in the value of these securities.

Default risk: Given Fixed Interest securities represent loans to borrowers (including governments, banks and companies) there is a risk that these borrowers may default on interest or principal repayments. Default risk is often reflected in credit ratings assigned by various credit agencies, which are subject to change.

Currency risk: In addition to being exposed to general market risk, investments in international markets are exposed to changes in the value of the Australian Dollar relative to other foreign currencies. This may lead to increased volatility, independent of market moves. While Fixed Interest funds typically hedge their foreign investments back into Australian Dollars, there can be no guarantee that the funds will be hedged at all times or that a manager will be successful in employing the hedge.

Liquidity risk: Fixed Interest markets can experience periods of illiquidity, which can result in difficulties in buying or selling securities without adversely impacting the price.

Derivative risk: Derivatives are commonly employed by Fixed Interest managers to hedge Currency and other risks and/or as an alternative to direct purchases or sales of underlying assets. There are multiple risks associated with the use of derivatives; for example, the value of the derivative may not move in line with the underlying asset, counterparties to the derivative may not be able to meet payment obligations or a particular derivative may be difficult or costly to trade.

Leverage risk: Many derivatives have a leverage component. While leverage offers the opportunity to magnify gains, it may additionally magnify losses. An associated risk with leverage and magnification of gains/losses is that the portfolio's volatility may increase as a result. Investors need to be cognisant that the Fund may exhibit more volatility than one that is unlevered.

Administration and operations

Responsible Entity	Channel Investment Management Limited

Zenith rating

Report certification

Date of issue: 07 Mar 2024

Role	Analyst	Title
Analyst	Rodney Sebire	Head of Alternatives & Global Fixed Interest
Sector Lead	Rodney Sebire	Head of Alternatives & Global Fixed Interest

Role	Analyst	Title
Authoriser	Bronwen Moncrieff	Head of Research

Association & relationship

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Rating history

As At	Rating
07 Mar 2024	Recommended
09 Mar 2023	Recommended
07 Dec 2022	Not Rated - Screened Out

Last 5 years only displayed. Longer histories available on request.

In March 2021, Zenith implemented a new ratings methodology for products classified as Traditional Index. Any rating issued from this date forward for Traditional Index products only reflect this change in methodology, with the relevant Traditional Index ratings being Index Approved, Index Recommended and Index Highly Recommended. Ratings issued for Traditional Index products prior to March 2021 are retained for historical purposes in line with our regulatory requirements and were issued in line with Zenith's Fund Research Methodology. Further information in relation to Zenith's Traditional Index Research Methodology and Traditional Index Ratings can be found on the Zenith website.

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