PENDAL

Fund Manager Commentary

Month ended 28 February 2019

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Australian Shares

Pendal Australian Share Fund

Market Review

Australian equities extended gains through February, despite the latest reporting season seeing more earnings downgrades than the historical average – the market environment is tougher, however investors were braced for poor news. The S&P/ASX 300 Accumulation Index was up 6.0% for the month.

There was a marked rotation away from defensives over the month, towards cyclicals and the unloved as some of the macro fears receded. Financials outperformed, up +9.1% (S&P/ASX 300 Financials), with the banks outperforming despite lacklustre updates as the overhang from the Royal Commission disappeared. ANZ (ANZ) was the strongest of the Big 4, up +11.9% for the month. Resources (S&P/ASX 300 Resources) were up +6.9% as cyclicals shifted back in to favour. The S&P/ASX 300 AREIT sector underperformed, up +1.9% given the combination of its more defensive characteristics and the pressure on both the retail and residential housing sub-sectors. This was exemplified by the fall in Westfield Unibail Rodamco (URW, -7.1%) – with its exposure to European retail – and Stockland Group (SGP, -7.4%) which owns both residential and retail assets. Gold stocks such as Evolution Mining (EVN, -9.1%) and Newcrest (NCM, -0.1%) lagged as investor confidence improved.

At a stock level, Cochlear (COH, -11.9%) was among the notable underperformers, as a highly-rated growth stock not delivering on expectations. This was the largest drag on Healthcare (-11.8%). Dominos Pizza (DMP, -8.0%) and Treasury Wine Estates (TWE, -3.0%) are two other market favourites which are finding it hard to meet expectations. The Australian domestic demand for DMP seems to be slipping, perhaps in response to the greater choice offered by online food delivery companies. TWE hit its numbers, which had been preannounced, but the low conversion of reported earnings into cash disappointed the market.

The regional banks Bank of Queensland (BOQ, -11.4%) and Bendigo and Adelaide Bank (BEN, -8.5%) also lost ground on the view that they are doing it even tougher than their larger peers in an environment of muted revenue growth. Reporting season revealed that supermarkets, too, are in a challenging environment. Both Coles (COL, -9.4%) and Woolworths (WOW, -0.9%) are facing issues from higher costs coming through and the top line not moving as much as required to offset the margin pressure. The duo weighed on Consumer Staples (-1.4%), the only sector that finished the month in the red.

While the banks outperformed in February, some of the diversified financials (+11.5%) did even better. IOOF (IFL, +36.9%) was among the market's best, enjoying a relief rebound – and short squeeze – as some of the market's fears around the Royal Commission went unrealised. Fund managers Magellan (MFG, +25.0%) and Janus Henderson (JHG, +17.5%) bounced along with equity market sentiment. In Insurance (+9.1%), QBE's strong final week saw it up 15.1% for the month.

Elsewhere, the implications of Vale's tailings dam tragedy dominated the macro for the miners. Reduced production has seen tighter iron ore markets and a sharp reduction in the discount for lower grade 58-fines ore – such as that mainly produced by Fortescue Mining (FMG, +12.6%) – below 62-fines. The issue continues to escalate, with the Vale board bowing to government pressure and standing down its executive and installing temporary management. Ultimately, as much as 70m tonnes could be withdrawn from the seaborne market in the near term, from a total Brazilian production of around 440m tonnes. Iron ore futures are currently trading at US$85 a tonne, but there is an expectation that this tightness could shift this into the US$90 range. Most consensus mid-to-long term forecasts have iron ore at US$60-$65, implying material upgrades for

the miners. Over the month, this helped both BHP (+6.9%) and Rio Tinto (RIO, +10.5%) to outperform. The Materials sector finished February 6.4% higher as a result.

Portfolio performance

The Pendal Australian Share Fund returned 6.66% (post-fee, pre-tax) in February, outperforming its benchmark by 0.65%.

Contributors

Overweight Viva Energy

Viva Energy (VEA, +31.0%), which distributes Shell fuel in Australia, soared on the back of a deal which saw it purchase the right to set the retail fuel margin at the Coles-operated petrol stations, which had been previously set by Coles management. This will result in a meaningful earnings uplift for VEA, as well as allowing it to drop the fuel price – currently at a material premium to the market – in order to win back some market share. VEA has recently battled with the headwind of low refining margins, which should see some seasonal improvement as northern hemisphere refiners shut down for maintenance as they move into Spring.

Underweight Woolworths

Results from reporting season for Woolworths (WOW, -0.9%) painted a picture of tough conditions for supermarkets. It is proving difficult for companies to pass on higher input costs as competition remains tight. WOW is set to face the higher labour costs as a result of new employee benefit agreements (EBAs) over the next year. This is a broader theme within the market, with some companies looking to undertake new EBAs ahead of a possible change in Federal Government this year. The supermarkets are also finding it tough to grow: most of their sales growth is coming in online channels, which means higher costs and almost no margin. These issues underpin our preference for Metcash (MTS) in this space. As a wholesaler, MTS is not under the same pressure from renegotiated EBAs. At the same time, a lot of the cost pressures in supermarkets is coming in the fresh food, which is less of an issue for MTS. WOW retains its defensive valuation premium, trading at 22.2x next-12-month consensus PE despite a 5% FY19 downgrade at its result. COL is at 17.3x, while MTS is 12.2x.

Not holding Coles

Coles (COL, -9.4%) delivered its maiden result after spinning out from Wesfarmers. Its report, like that of competitor Woolworths painted a picture of tough conditions for supermarkets. It is proving difficult for companies to pass on higher input costs as competition remains tight. COL has had to wear higher labour costs as a result of new employee benefit agreements (EBAs) and WOW is set to face the same challenge over the next year. This is a broader theme within the market, with some companies looking to undertake new EBAs ahead a possible change in Federal Government this year. The supermarkets are also finding it tough to grow: most of their sales growth is coming in online channels, which means higher costs and almost no margin. These issues underpin our preference for Metcash (MTS) in this space. As a wholesaler, MTS is not under the same pressure from renegotiated EBAs. At the same time, a lot of the cost pressures in supermarkets is coming in the fresh food, which is less of an issue for MTS. WOW retains its defensive valuation premium, trading at 22.2x next-12-month consensus PE despite a 5% FY19 downgrade at its result. COL is at 17.3x, while MTS is 12.2x.

Detractors

Overweight CSL

Our preferred growth stock, CSL (CSL, -0.5%) underperformed in February, despite delivering a decent result which is on track to hit the upper end of management guidance. The market focused on weakness in Albumin volumes, which management has attributed to a one-off issue as it waits for a licence to supply Chinese demand from an additional plant.

Not holding QBE

Insurer QBE (+15.1%) saw its results from reporting season well received. It is enjoying the tailwind of mid-single digit price increases and has seen a material improvement in operating performance in recent halves. However, the company needs to deliver a strong ‘hockey stick’ second half to meet the full year guidance. We see further margin pressure coming through and, with consensus expectations currently at the top end of the guidance range, see some scope for disappointment here.

Not holding Woodside Petroleum

The Energy sector (+7.8%) outperformed in February, as the oil price continues to hover around the US$60/bbl mark. Alongside a declining Australian dollar, we saw oil price reach AU$80/bbl at month end which benefited Woodside Petroleum (WPL, +9.4%) amongst the others. WPL also reported a solid set of results where the underlying earnings rose by 38% year-on-year. Due to the strong Free Cash Flow and low gearing, Management paid out 100% of the second half earnings as dividend. We do not hold WPL, instead our preference is with Santos (STO, +8.3%). New supply remains constrained in the LNG market and we continue to like the quality of STO's portfolio of assets.

Strategy and outlook

February was eventful on several fronts. The market was braced for reporting season, conscious of the potential implications of softer consumer sentiment and declining house prices. As it transpired, there were more downgrades than usual as companies were generally cautious in their outlook and flagged a tougher environment. However, we are not seeing a collapse in earnings and the aggregate outcome of reporting season was not as bad as many had feared.

A reasonable reporting season therefore provided no impediment to the positive turn in sentiment on several macro issues which, in turn, saw a market re-rating and a 6.0% gain in the S&P/ASX 300. The US Federal Reserve’s decision to pause its hiking cycle has seen the fear of a policy mistake and over-tightening recede. At the same time, there are signs of Chinese stimulus measures starting to gain traction, cooling fears about the pace of economic deceleration and the effect upon global growth. The outcome of Sino-American negotiations remains unclear, but here too the consensus is more positive, with the expectation that some sort of deal will be forthcoming which will remove the uncertainty. Sentiment has swung quickly on these issues – and we are mindful that it could deteriorate just as quickly – but for the moment the more positive tone has allowed the market to bounce back and almost return to its level of October 2018.

We have also seen material changes in the outlook for iron ore. The devastating tragedy in late January in Brazil - where the collapse of a tailings dam at the Corrego do Feijao mine in Minas Gerais state resulted in 186 deaths - has seen the government step in and look to shut down production at a number of mines where ‘downstream’-style tailings dams have been constructed in potentially vulnerable locations. While the outcome is uncertain, at this point there are indications that reduced production could see a shortfall against demand in FY20, resulting in much higher iron ore prices than consensus currently expects.

The banks enjoyed a relief bounce as the ultimate findings of the Royal Commission were seen as largely benign, although there is little doubt that it has wrought material changes upon both the structure of the financial sector and how the banks are likely to be managed in the near future. We see the banks as having valuation support at their current levels, however trading updates revealed that the environment remains challenged. The banks will do well to hold earnings flat in the next few halves and we may even see some declines. As such, it is hard to see the banks outperforming in the near term.

We believe we remain in an environment of subdued asset returns. There are pockets of strong organic growth – such as in mining services – however in aggregate economic growth remains muted. At the same time, we believe that liquidity will be tighter than has been the case in the previous five years. The implication is that we will see divergences within the market. Companies which are able to generate growth, exercise capital discipline, return cash to shareholders, and respond to disruptive threats should be well rewarded. Those that cannot are likely to be punished by the market, as we no longer have the rising tide of abundant liquidity lifting all boats. While this is an environment which does present challenges, it is one in which company level insight and the ability to identify companies with good strategies and adroit management, should be rewarded.

Pendal Smaller Companies Fund

Market review

Similar to its large cap counterpart, the S&P/ASX Small Ordinaries Index managed to extend its gains through February, finishing the month +6.8% higher, with the Small Industrials (+7.1%) marginally outperforming Small Resources (+5.8%). Despite the reporting season being less sanguine and company management teams being generally more conservative, investor sentiment was positive given the broad improvement in global macro influences. Although risks remain, the market appears to be strengthening the view that we are moving towards some form of resolution in the US/China trade dispute. The small companies index now trades on a one-year forward price/earnings multiple of 16.8x, representing an 11% premium to its five-year average.

Energy (+14.1%) was the best performing sector over the month, while index heavyweight Consumer Discretionary (+13%) contributed the most to the market's performance. The oil price continues to hover around the US$60 per barrel mark. Together with the impact of a declining Australian dollar, the oil price reach AU$80 per barrel at month end which benefited the Energy names in general. In addition, Viva Energy (VEA, +31.0%), which distributes Shell fuel in Australia, soared on the back of a deal which saw it purchase the right to set the retail fuel margin at the Coles-operated petrol stations, which had been previously set by Coles management. This will result in a meaningful earnings uplift for VEA, as well as allowing it to drop the fuel price—currently at a material premium to the market—in order to win back some market share. The stock was the largest contributor to Energy's outperformance.

A range of positive reporting season results helped to lift the Consumer Discretionary sector, including the likes of Webjet (WEB, +30.6%), IDP Education (IEL, +31.3%) and Consumer appliances maker, Breville Group (BRG, +45.2%). BRG delivered a good result, defying pressure on the retail sector. Its Global Products division grew sales by 9.2% in constant currency terms compared to the prior half. This was an even more encouraging result given the numbers were coming off a strong base effect of +20.5% growth in the prior corresponding period. Its 20% earnings-per-share growth was well ahead of consensus expectations and management gave optimistic guidance, expecting growth to accelerate in the second half.

Elsewhere, a number of the market darlings within Information Technology (+11.3%) continued to fetch higher prices. Altium (ALU, +32.3%), Appen (APX, +46.9%) and Afterpay Touch (APT, +15.9%) all reside in that group and recorded double-digit returns in February. Strong performance from all divisions helped ALU to deliver a solid print of revenue growth for the first half. In terms of users subscription, Management reaffirmed its target of 100,000 users by 2025 which helped to

support sentiment. APX also delivered a strong set of results, with second-half earnings (EBITDA) was 79% higher than the previous half. Improvement in efficiency and additional operating leverage continue to help APX and resulted in some broking analyst upgrades. Offsetting some of these gainers were Wisetech (WTC, -5.3%) and NEXTDC (NXT, -8.9%). Although both printed a good set of results, they failed to meet expectations implied in their valuation ratings.

On the other end of the spectrum, Consumer Staples (-2.8%) was the only sector that finished February weaker, despite some good returns from Metcash (MTS, +5.2%) and BWX (BWX, +53.9%). The share price of BWX soared after beating market expectations for earnings, despite the company providing full-year earnings (EBITDA) guidance that was at the lower end of its previous estimates. The broader sector was dragged down somewhat by a poor trading update from vitamins manufacturer Blackmores (BKL, -27.2%). BKL delivered +0.4% growth in net profit after tax (NPAT) for the first half. However, sales growth in China was up +8% for the half which, after +18% growth in the first quarter, implied a deceleration in Q2 FY19 and the aggregate result came in behind the market's expectations. Management also provided a cautious outlook for the second half.

Portfolio performance

The Pendal Smaller Companies Fund returned 6.02% (post-fee, pre-tax) in February, underperforming the S&P/ASX Small Ordinaries Accumulation Index by 0.76%.

Contributors

Overweight Seven Group (SVW)

Seven Group had dragged in late 2018 on broad concern over the outlook for the resource sector in the face of slowing Chinese growth. Sentiment here has rebounded as stimulus measures look to be gaining traction and there is renewed hope of a Sino-American trade deal. However, we think that ultimately Seven's positive medium-term outlook is underpinned by the requirement of miners to upgrade and maintain equipment, having delayed this spending for several years.

Overweight Breville Group (BRG)

Consumer appliances maker Breville Group delivered a good result, defying the pressure on the retail sector. Global Products grew sales at 9.2% in constant currency terms versus H1 2018 – an even more encouraging result given that it was cycling the strong base effect of +20.5% growth in the prior corresponding period. 20% earnings-per-share growth was well ahead of consensus expectations and management gave optimistic guidance, expecting growth to accelerate in the second half.

Detractors

Overweight Blackmore (BKL)

Blackmore's delivered +0.4% net profit after tax (NPAT) growth for the first half over H1 FY18. However sales growth in China was up +8% for the half which, after +18% growth in the first quarter, implied a deceleration in Q2 FY19 and the aggregate result came in behind the market's expectation. Management provided a cautious outlook for the second half.

Underweight Appen (APX)

Appen delivered strong results, with revenue growing 119% versus H1 FY18. We remain cautious on Appen – while the company has some attraction, the valuation is demanding and we have invested in other technology companies where we believe there is more valuation support. The underweight here dragged on performance.

Strategy and outlook

The portfolio rebounded in February as broad equity market sentiment improved, although it was a touch behind the index. The tech growth stocks led the market's rebound, demonstrating that these stocks remain popular despite heady valuations and the high expectations they imply. We remain judicious in our exposure to this part of the market, believing that it will become more difficult for some of these growth stocks to maintain their ratings as we move into an environment of lower liquidity. Our exposure to Altium was beneficial, although the underweight in stocks such as Appen and Afterpay Touch dragged on performance. The positions in Blackmores and Eclipx Group also detracted.

This was offset to some extent by strong performance from Seven Group, Nanosonics and Corporate Travel Management, among others. Seven, in particular, was one which had dragged in late 2018 as the market expressed concern over the outlook for commodity prices and the resource complex as Chinese growth slowed. We believe that mining services is one of the few areas in the domestic economy seeing decent organic growth. The miners have delayed new replacement mines and equipment maintenance for several years and are now at the point where this spending is critical, almost regardless of where commodity prices are.

February was eventful on several fronts. The market was braced for reporting season, conscious of the potential implications of softer consumer sentiment and declining house prices. As it transpired, the small cap sector saw more downgrades than usual, with downgrades outpacing upgrades by two to one. In aggregate, the Small Industrials earnings expectation for FY19 fell to 6% growth, from 11% growth before reporting season. Nevertheless, this was largely in line with the market's expectations, illustrated by the fact that only 41% of companies which downgraded saw their stock price subsequently fall.

A reasonable reporting season therefore provided no impediment to the positive turn in sentiment on several macro issues which, in turn, saw a market re-rating and a 6.0% gain in the S&P/ASX 300. The US Federal Reserve's decision to pause its hiking cycle has seen the fear of a policy mistake and over-tightening recede. At the same time, there are signs of Chinese stimulus measures starting to gain traction, cooling fears about the pace of economic deceleration and the effect upon global growth. The outcome of Sino-American negotiations remains unclear, but here too the consensus is more positive, with the expectation that some sort of deal will be forthcoming which will remove the uncertainty. Sentiment has swung quickly on these issues – and we are mindful that it could deteriorate just as quickly – but for the moment the more positive tone has allowed the market to bounce back and almost return to its level of October 2018.

We have also seen material changes in the outlook for iron ore. The devastating tragedy in late January in Brazil - where the collapse of a tailings dam at the Corrego do Feijao mine in Minas Gerais state resulted in 186 deaths - has seen the government step in and look to shut down production at a number of mines where 'downstream'-style tailings dams have been constructed in potentially vulnerable locations. While the outcome is uncertain, at this point there are indications that reduced production could see a shortfall against demand in FY20, resulting in much higher iron ore prices than consensus currently expects.

We believe we remain in an environment of subdued asset returns. There are pockets of strong organic growth – such as in mining services – however in aggregate economic growth remains muted. At the same time, we believe that liquidity will be tighter than has been the case in the previous five years. The implication is that we will see divergences within the market. Companies which are able to generate growth, exercise capital discipline, return cash to shareholders, and respond to disruptive threats should be well rewarded. Those that cannot are likely to be punished by the market, as we no longer have the rising tide of abundant liquidity lifting all boats. While this is an environment which does present challenges, it is one in which company level insight and the ability to identify companies with good strategies and adroit management, should be rewarded.

International Shares

Pendal Concentrated Global Share Fund

Market review

Global share markets appeared to celebrate in February, pushing valuations higher largely in reaction to better prospects on the macro horizon. The US Federal Reserve (Fed) is now in a 'no rush' stance to raise interest rates, while sentiment was also supported by what appears to be a clearer path to resolving the US and China trade dispute. China's stock market certainly reflected this prospect and experienced one of the largest relief rallies, up 13.8%. Such prospects also supported most other markets to deliver strong gains and downplay other nascent risk factors. For February, the benchmark MSCI World ex Australia (A$) Index closed 5.6% higher.

Gains in the US share market were broadly based, although Information Technology registered the largest gains. Industrials and Materials stocks also moved higher as prospects for better trade relations with China supported investor sentiment. The US quarterly reporting season came to an end in February, with around 75% of companies reporting earnings growth on average of 12%, with the Industrials sector posting the best earning growth, averaging 17%. Guidance for the second quarter was generally muted; however, corporates–particularly in the technology sector–were optimistic for a strong rebound in second-half revenues. At the month's close, the S&P500 registered a 3.2% gain, while the NASDAQ had risen by 3.4%.

European share markets continued to build on January's gains to be led by cyclically oriented sectors, while the more defensive Real Estate and Utilities sectors lagged. Investors saw the decision by Trump to extend the March 1 tariff hike deadline as a sign that normalisation of trade may prevail, thereby having a positive flow-on effect for European companies. Hopes of the UK reaching a workable deal on Brexit prior to the 29 March deadline also supported sentiment. However, the uncertainty to date has likely taken a toll on economic growth for the UK, with the Bank of England cutting its GDP growth expectations to 1.2% from 1.7% for the year. UK inflation also fell below 2%, while the UK Purchasing Manager's Index fell to a 30-month low, signalling the extent of weakness in confidence for the economy. The UK's stock market etched out a 1.5% gain for February, lagging European markets like France (+5%), Germany (+3.1%) and Switzerland (+4.7%).

Most Asian equity markets also reflected optimism regarding the US-China trade issue, although performance was highly dispersed. China outpaced the region with a 13.8% gain following the Lunar New Year holiday period. Taiwan followed with a 4.6% return while South Korea bucked the trend, declining by 0.8% after talks between North Korea and the US were halted. Corporate earnings and inflation were both weaker for South Korea. Japan gained 2.9% while south-east Asian markets–Malaysia, Thailand and Singapore–registered smaller advances.

The Australian dollar lost ground against its major trading partners as sentiment shifted against the currency. The local unit fell by 2.5% against the US dollar, 1.8% against the euro and 3.6% on the British pound. In commodity markets the oil price's continued its rebound to close at US$57.25 per barrel.

Portfolio performance

The Pendal Concentrated Global Share Fund returned 5.60% (post fee, pre-tax) in February, outperforming its benchmark by 0.04%.

Heineken hops on board new markets

The price action for Heineken (+12%) was one of the highlights for the Fund in February. The company reported fourth-quarter and full-year results that were ahead of market expectations. For the full year organic sales growth of 6% was largely driven by better than expected volume growth, particularly in Europe, Africa, & the Middle East. The Heineken brand recorded its best performance in a decade, with volumes growing just under 8% which validated management's recent marketing and promotional spend.

Heineken is distributed now in 38 markets with plans to expand further in 2019. Guidance for 2019 was for "superior top-line growth driven by volume, price and premiumisation". While there is some cost pressure, the company still expects to deliver mid-single-digit earnings growth in 2019. Although top-line growth is clearly the priority of management in the shorter term, we believe market share growth will lead to operating leverage and margin expansion over time, a factor that is currently being underestimated by the market.

Analog Devices boosts dividend, holds place in portfolio

Our holding in semi-conductor manufacturer, Analog Devices (ADI) performed well this month after reporting quarterly earnings above expectations. The uncertainty resulting from ongoing US/China trade talks and the US allegations relating to intellectual property theft by China has impacted the sector. Sales for the sector are generally lower than for the same period last year. Regular readers would be aware that our investment case for ADI and Texas Instruments (the other semi-conductor company we own) is in part based on the diversity of each company's product suite and the end markets they sell into. While weaker demand from the automotive and industrial sectors has been felt across the whole industry, the strength of demand within ADI's communications business, driven by 4G network upgrades, resulted in overall sales being down only 2% for the year. Management have also signalled a stabilisation of orders in January. Although we think consensus expectations for industry sales growth in the second half of 2019 may prove to be optimistic, we remain confident in the diversity of the business model and quality of management which will support growth for the company over the longer term. Management clearly share this confidence, announcing an upward revision to their annual dividend growth target from 5-10% to 7-15%.

Another 'paid to wait' position

Caixa Bank (-4%) was a detractor from Fund performance this month. The share price fell following the release of the Spanish bank's fourth-quarter results. The bank missed consensus expectations due to a number of one-off hits. While this was disappointing, the operating results were in line with expectations and credit quality improved. However, the share price reacted negatively to cost growth guidance for 2019 of 5% (ahead of revenue growth). Caixa Bank had previously announced a restructuring program aimed at boosting efficiency. The planned restructure involved a reduction in head count and the closure of small branches in cities to focus on larger offices that offer more services.

Management had previously guided to a 3% compound average annual growth rate in costs between 2019 and 2021; this guidance has not changed, however the costs have been front loaded to the first year of the restructure, implying cost growth in 2020 will be 2%. We continue to believe Caixa Bank offers compelling value over the longer term, with asset quality trends continuing to improve and the bank remaining well capitalised with a positive outlook for revenue. The bank is trading on a 6% dividend yield and we are prepared to wait for the benefits of restructuring efforts to flow through to earnings.

Strategy and outlook

The month of February saw markets perform well, sentiment improve and volatility subside from the elevated levels in December. However, economic data is mixed and there remains a number of geopolitical uncertainties that continue to cloud the outlook for corporates. As long term investors

we remain focused on owning companies that are equipped with robust business models, have nimble management teams and dominant market shares.

We buy these companies when valuations are compelling and we hold confidence in their ability to not only withstand but prosper, regardless of what the economic cycle may have to offer. In this environment, we believe owning a concentrated portfolio of businesses exhibiting these characteristics will generate better investment performance than having indiscriminate broad market exposure.

Pendal Core Global Share Fund

(managed by AQR Capital Management)

Market review

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European share markets continued to build on January's gains to be led by cyclically oriented sectors, while the more defensive Real Estate and Utilities sectors lagged. Investors saw the decision by Trump to extend the March 1 tariff hike deadline as a sign that normalisation of trade may prevail, thereby having a positive flow-on effect for European companies. Hopes of the UK reaching a workable deal on Brexit prior to the 29 March deadline also supported sentiment. However, the uncertainty to date has likely taken a toll on economic growth for the UK, with the Bank of England cutting its GDP growth expectations to 1.2% from 1.7% for the year. UK inflation also fell below 2%, while the UK Purchasing Manager's Index fell to a 30-month low, signalling the extent of weakness in confidence for the economy. The UK's stock market etched out a 1.5% gain for February, lagging European markets like France (+5%), Germany (+3.1%) and Switzerland (+4.7%).

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The Australian dollar lost ground against its major trading partners as sentiment shifted against the currency. The local unit fell by 2.5% against the US dollar, 1.8% against the euro and 3.6% on the British pound. In commodity markets the oil price's continued its rebound to close at US$57.25 per barrel.

Portfolio performance

The Pendal Core Global Share Fund returned 4.93% (post-fee, pre-tax) in February, underperforming its benchmark by 0.63%.

Thematically, the underperformance was driven by weakness in the manager's Value signals, particularly for stock selection within industries as this detracted from returns in all core regions. In North America, weakness in Value and Investor Sentiment themes were somewhat offset by the positive performance of Momentum and Quality themes. In Europe and Asia, both valuation and to a lesser extent, momentum, were weak over the month. This was partially offset by the positive performance of Quality themes.

From a stock and industry attribution perspective, intra-industry stock selection drove underperformance, while industry selection contributed positively to active returns over the month. Stock selection within industries was weakest within the Health Care, Energy and Information Technology sectors, with gains within Consumer Discretionary and Financials the notable offsets. At a sector level, an overweight tilt to Information Technology industries was the main positive contributor.

At a stock level, the largest contributors to active returns came from overweight positions in: Microsoft Corp., a US-headquartered multinational technology company; Merck & Co., Inc., a US multinational pharmaceutical company; Adobe Inc., a US multinational computer software company; Intel Corporation, a US multinational technology company; and Intuit Inc., a US headquartered business and financial software company. The largest detractors from active returns came from: an underweight in Visa Inc., a US multinational financial services corporation; an overweight in Humana Inc., a for-profit US health insurance company; an underweight in Exxon Mobil Corp., a US multinational oil and gas corporation; an overweight in Cigna Corp., a US personal insurance and health services organisation; and an underweight in Chevron Corp., a US multinational oil and gas corporation.

Strategy and outlook

Moving into March 2019, the largest sector tilts are overweights in Health Care and Information Technology and underweight positions in Financials and Consumer Staples.

Australian Fixed Income

Pendal Fixed Interest Fund

Market review

Australian bond yields fell during the month as the Reserve Bank of Australia (RBA) shifted its communication to suggest the outlook for rate changes was "more evenly balanced". The central bank also downgraded its projection for economic growth and lowered its inflation forecast in its quarterly Statement on Monetary Policy. In turn, markets are now pricing at least one cut from the Board over the next 12 months. Meanwhile, local economic data was mixed over the month. Labour data was stronger-than-expected with 39,000 jobs added, which was attributed to a strong increase in full-time positions. A small rebound in consumer confidence and business conditions was also encouraging. In contrast, retail sales slipped 0.4% and building approvals fell a sizeable 8.4% month-on-month. Wage data revealed a 0.5% increase over the quarter, which brought the year-on-year rate to 2.3%. Finally, the Australian 3- and 10-year yields fell 13bp and 15bp to 1.63%

and 2.10%, respectively. At the very front-end, the 3-month BBSW dropped a more sizeable -20bp to 1.87%.

Portfolio performance

The Pendal Fixed Interest Fund returned 0.84% in February (post-fees, pre-tax), underperforming its benchmark by 0.10%.

The Fund's underperformance in February was driven by the alpha overlay. The FX strategy was the largest drag due to long US dollar positions versus both emerging market (EM) currencies and the euro. The Duration strategy also detracted from EM positioning, including a long China duration trade that suffered as sentiment towards the trade war improved. Similarly, an improvement in risk appetite hurt the defensive positioning in the Macro strategy, including a European crossover versus main trade. The Relative Value strategy experienced a smaller loss over the month from the receive position in US real yields. The Cross-Market strategy also slightly underperformed from a long New Zealand versus short Australia position, while the Yield Curve strategy added to performance on a NZ curve steepener.

Strategy and outlook

The RBA left the cash rate unchanged at its meeting in early March and delivered a neutral statement. However, broader communication from the Board and softening economic data has stoked market expectations for a rate cut from the central bank over the next year. This was reinforced by fourth quarter GDP data released the day after the RBA's meeting. Of particular interest within the numbers was household consumption; this area has remained weak despite solid employment growth.

With the cash rate at 1.50% the hurdle for further policy easing is still high, with the catalyst most likely to come from inflation disappointing or the labour market deteriorating. The RBA is looking for labour market tightness to feed into wage inflation and in turn see underlying inflation increase. With the unemployment rate at 5% and according to the RBA's forecasts is expected to fall to only 4.75% by June 2021 it is difficult to envisage wage inflation pressure rapidly increasing. However, the labour force participation rate is around historically high levels that has kept the unemployment rate more elevated than would otherwise be the case.

Inflation has continued to disappoint, with the trimmed mean remaining below the RBA's 2-3% target band since March 2016. Its forecasts imply underlying inflation will only rise above 2% in the second half of 2020. Such a benign environment does not require the RBA to be pre-emptive. The economy continues to be supported by elevated commodity prices and a large pipeline of infrastructure investment.

International Fixed Income

Pendal Global Fixed Interest Fund

Market review

The US Federal Reserve's tilt to a more neutral stance in January continued to buoy risk appetite and lift global equities during the month. This was alongside optimism towards a positive outcome to US-China trade negotiations that took place in Washington late in February. Although there was no formal agreement between both sides, some perceived progress and the indefinite delay of a proposed US tariff increase was well-received by markets. Economic data was less supportive for risk assets. US GDP figures revealed a softer 2.6% annualised growth rate for the fourth quarter

and Eurozone GDP growth printed at a preliminary 0.2% quarterly growth rate. German GDP figures revealed the region's largest member had narrowly avoided a technical recession, while its Italian counterpart was not as fortunate. In terms of market movements, the US 2- and 10-year yields increased by 6 basis points (bp) and 9bp to 2.52% and 2.72%, respectively.

Portfolio performance

The Pendal Global Fixed Interest Fund returned -0.31% in February (post-fees, pre-tax), underperforming its benchmark by 0.13%.

Over the month, the Duration and FX strategies were the main detractors from relative performance, while Macro, Relative Value and Cross-Market strategies slightly underperformed, and the Yield Curve strategy was largely flat. The portfolio risk level started at 4 risk units and increased to 9 risk units before finishing the month at 6 risk units.

The Duration strategy was the largest detractor over the month. The long duration position in China generated the largest loss due to growing positive sentiment on US-China trade negotiations. We added long duration positions in the front end of the New Zealand curve following the release of weak labour market data. In Europe losses were sourced from long duration positions in the front end of the euro and Swedish krona curves, although the losses were partially offset by a long position in German Bunds and a short position in Italian BTP's. Similarly, in the US we incurred losses in long positions in the front end of the curve, while the profit from a tactical short in 10-year Treasury notes helped to mitigate the losses. In Australia the performance of our long positions were largely flat. Later in the month we added a long duration position in the Korean long end, which had a fairly neutral impact on performance for the month.

The FX strategy detracted from performance over the month, due to our long USD bias which has been reflected in FX positions in both emerging and developed markets. In emerging markets we closed the short USD long CNH position early in the month and established a long position on USD against CNH in options. Later in the month we were stopped out of short positions in PHP and KRW. In the developed markets, losses mainly originated from short EUR positions. As of month end, we retained small positions in long USD against EUR, CNH and KRW which are all in options.

The Yield Curve strategy added to performance. Profits were mainly from a steepener in NZD. During the month we opened a US 5y-30y steepening position which was neutral to performance for the month.

The Macro strategy detracted from performance over the month. Losses were mainly from the iTraxx Europe Crossover to iTraxx Europe Index decompression position as the iTraxx Europe Crossover Index tightened more aggressively than the Main. In the middle of the month we reduced the CDX investment grade (IG) leg in the High Yield (HY)-IG decompression position, expecting the HY leg to widen out. Performance of this position was flat over the month. Facing the rosy sentiment ahead of the Trump-Kim meeting in Hanoi we closed the buy protection position in Korea CDS. Our curve flattening position in CDX HY kept a steady performance as expected.

The Relative Value strategy experienced a minor loss over the month from the received position in US real yields.

The Cross-Market strategy slightly underperformed over the month. Losses were from long New Zealand vs short Australia in the front end of the curves.

Strategy and outlook

Although the weakening growth backdrop was not the focus of attention in February, we believe it is still the core narrative that will continue to weigh on risk assets over the course of this year. For this reason, the Duration strategy will be playing an increasingly dominant role in our portfolio. While the combination of a more dovish Fed and receding tail risks is giving risk assets a boost for

now, if its pivot was because of growth concerns, then we should be wary of the bounce back in risk assets. Similarly, the dialing back of trade war escalation removes immediate threats, but the trade and electronics cycle still looks sick. Additionally, the impact of Chinese stimulus is far harder to predict (and control) than stimulating via infrastructure investment. As such, in spite of current optimism around trade deals and commodity prices, we expect ongoing growth challenges to resurface in China and Australia, and we may even see greater downside surprises later this year from the US.

Credit

Pendal Enhanced Credit Fund

Market review

Domestic credit generated another positive return for the month. This was driven by the combination of a fall in underlying yields, tightening of credit spreads and strong accruals. A strong recovery in risk appetite led the narrowing for spreads after the Fed signalled a more patient and flexible path for policy normalisation in January. Sentiment was also bolstered by perceived progress on a US-China trade agreement and the indefinite delay of a tariff increase.

Against a stronger risk backdrop, issuance also returned as a theme. NAB was the largest issuer with an A$3b deal split between A$400m fixed and the remainder in floating debt. This followed in the wake of issuance from the other three major Australian banks in January. General corporates returned to the market for the first time this year with noteworthy deals from General Motors (A$400m) and McDonald's (A$1.4b).

The Australian iTraxx index (Series 30 contract) traded in a 10bp range finishing the month 8bp tighter to +69bp. Physical credit spreads also closed the month narrower, with the best performing sectors being domestic banks, infrastructure and utilities which all tightened by 7bp. The worst performing sector was supranationals which only narrowed 1bp. Semi-government bonds performed well, tightening 2bp to government bonds.

Portfolio performance

The Pendal Enhanced Credit Fund returned 0.81% in February (post-fees, pre-tax), outperforming the benchmark return by 0.05%.

The Fund's outperformance this month was driven by a fall in underlying rates, together with a tightening of credit spreads and accruals. Positions in infrastructure and utilities, where the Fund is overweight, outperformed versus other sectors.

Portfolio purchases over the period included issuance from NAB and McDonald's, while holdings in Scentre Group were divested.

Strategy and outlook

Our overall credit view is cautiously constructive. We have been constructive on corporate fundamentals, but are also wary that appetite for credit has proven highly sensitive to geopolitical developments in recent months. This has been driven by macro concerns including trade wars as well as fears that troubles for specific US corporates, such as GE, could reflect broader systemic issues. However, on balance we believe corporate fundamentals are healthy for the bulk of investment grade issuers. Balance sheets are generally strong and earnings are improving as evidenced by solid corporate earnings seasons in the US and Europe.

Further, Australian domestic issuers have not increased balance sheet leverage over the many years. The major Australian banks have stronger capital ratios than in previous years, which should support domestic financial stability. Moreover, the weight of uncertainty in the lead up to the Royal Commission has finally been lifted from their shoulders.

From a macro standpoint, we acknowledge that risks have risen due to increasing volatility across markets. This has been driven in part by flare-ups of geopolitical risks, such as the ongoing trade war ructions, where troubles have been exacerbated by less forgiving markets. That said, the impact of developments such as trade wars and attitudes towards monetary policy normalisation have shown a tendency to shift quickly as the story evolves. For example, the headwind to risk assets from the Fed's hike in December was quickly replaced by a tailwind as greater policy flexibility which was subsequently emphasised in January.

On the domestic economy, growth has softened albeit more evenly balanced than previous years. There are further risks to the downside as weak wage growth and the housing market correction threaten to dampen consumption. As such, we continue to recommend a defensive approach, with any overweights placed towards operationally resilient sectors such as Utilities and Infrastructure that provide higher yield to index returns.

Cash

Pendal Managed Cash Fund and Pendal Enhanced Cash Fund

Market review

Australian bond yields fell during the month as the RBA shifted its communication to suggest the outlook for rate changes was "more evenly balanced". The central bank also downgraded its projection for economic growth and lowered its inflation forecast in its quarterly Statement on Monetary Policy. In turn, markets are now pricing at least one cut from the Board over the next 12 months. Also in money markets, a large fall in the 3-month BBSW rate caused the spread between this and the 3-month OIS rate to narrow to 39bp. This was driven in part by offshore movements as the comparable LIBOR-OIS spread tightened during February.

Meanwhile, local economic data was mixed over the month. Labour data was stronger-than-expected with 39,000 jobs added, which was attributed to a strong increase in full-time positions. A small rebound in consumer confidence and business conditions was also encouraging. In contrast, retail sales slipped 0.4% and building approvals fell a sizeable 8.4% month-on-month. Wage data revealed a 0.5% increase over the quarter, which brought the year-on-year rate to 2.3%.

Looking abroad, the Fed's tilt to a more neutral stance in January continued to buoy risk appetite and lift global equities. This was alongside optimism over a positive outcome to US-China trade negotiations that took place in Washington towards the end of February. Although there was no formal agreement between both sides, some perceived progress and the indefinite delay of a proposed US tariff increase was well received by markets.

Economic data from the world's largest economy was less supportive for risk assets. GDP figures revealed a softer 2.6% annualised growth rate for the fourth quarter. Readings from leading indicators varied with the ISM manufacturing gauge ticking higher, but its services cousin falling. At the same time, consumer confidence rebounded and the monthly payrolls report revealed a constructive 304,000 addition for the month.

In Europe, fourth quarter eurozone GDP growth printed at a preliminary 0.2% quarterly growth rate. German GDP figures revealed the region's largest member had narrowly avoided a technical recession, while its Italian counterpart was not as fortunate. Leading indicators were more mixed,

with a 0.4 point rebound in composite PMI and 0.5 point recovery in consumer confidence, but a -1.6% fall in retail sales and -0.9% drop for industrial production.

In terms of market movements, the Australian 3- and 10-year yields fell -13bp and -15bp to 1.63% and 2.10%, respectively. At the very front-end, the 3-month BBSW dropped a more sizeable -20bp to 1.87%. At the same time, US 2- and 10-year yields increased by 6bp and 9bp to 2.52% and 2.72%, respectively. This caused the AU-US 10-year yield spread to fall further into negative territory and end the month at -0.61%. Together with the growing expectations for an RBA cut, the Australian dollar finished -2.5% lower versus its US namesake.

Domestic credit generated another positive return for the month. This was driven by the combination of a fall in underlying yields, tightening of credit spreads and strong accruals. A strong recovery in risk appetite led the narrowing for spreads after the Fed signalled a more patient and flexible path for policy normalisation in January. Sentiment was also bolstered by perceived progress on a US-China trade agreement and the indefinite delay of a tariff increase.

Against a stronger risk backdrop, issuance also returned as a theme. NAB was the largest issuer with an A$3b deal split between A$400m fixed and the remainder in floating debt. This followed in the wake of issuance from the other three major Australian banks in January. General corporates returned to the market for the first time this year with noteworthy deals from General Motors (A$400m) and McDonald’s (A$1.4b).

The Australian iTraxx index (Series 30 contract) traded in a 10bp range finishing the month 8bp tighter to +69bp. Physical credit spreads also closed the month narrower, with the best performing sectors being domestic banks, infrastructure and utilities which all tightened by 7bp. The worst performing sector was supranationals which only narrowed 1bp. Semi-government bonds performed well, tightening 2bp to government bonds.

Portfolio performance

Managed Cash

The Pendal Managed Cash Fund returned 0.15% in February (post-fees, pre-tax), underperforming the benchmark by 0.02%.

The Fund is delivering a higher running yield than the index and remains well positioned to outperform. Themes and credit exposure remain consistent with prior months, with excess spread from A-1 rated issuers and yield curve positioning likely to be the main driver of outperformance. The Fund ended the month with a weighted average maturity of 65 days (maximum limit of 70 days). The RBA is unlikely to tighten monetary policy in the near term and yields further along the curve continue to offer better relative value. The weighted average maturity has consistently been longer than benchmark for this reason.

Enhanced Cash

The Pendal Enhanced Cash Fund returned 0.26% in February (post-fees, pre-tax) outperforming the benchmark by 0.09%.

The Fund’s positive performance in February came from financials, industrials and infrastructure sectors.

Activity included investing in domestic banks and industrials sectors which was funded out of cash.

As at the end of the month, the portfolio had a credit spread of 60bp over bank bills, interest rate duration of 0.16 years and credit spread duration of 1.21 years.

Strategy and outlook

The RBA left the cash rate unchanged at its meeting in early March and delivered a neutral statement. However, broader communication from the Board and softening economic data has stoked market expectations for a rate cut from the central bank over the next year. This was reinforced by fourth quarter GDP data released the day after the RBA's meeting. Of particular interest within the numbers was household consumption; this area has remained weak despite solid employment growth.

With the cash rate at 1.50% the hurdle for further policy easing is still high, with the catalyst most likely to come from inflation disappointing or the labour market deteriorating. The RBA is looking for labour market tightness to feed into wage inflation and in turn see underlying inflation increase. With the unemployment rate at 5% and according to the RBA's forecasts is expected to fall to only 4.75% by June 2021 it is difficult to envisage wage inflation pressure rapidly increasing. However, the labour force participation rate is around historically high levels that has kept the unemployment rate more elevated than would otherwise be the case.

Inflation has continued to disappoint, with the trimmed mean remaining below the RBA's 2-3% target band since March 2016. Its forecasts imply underlying inflation will only rise above 2% in the second half of 2020. Such a benign environment does not require the RBA to be pre-emptive. The economy continues to be supported by elevated commodity prices and a large pipeline of infrastructure investment.

Australian Property

Pendal Property Securities Fund

Market review

The ASX 300 AREIT index was up 1.8% in February, underperforming the ASX 300 (+6.0%) by 420bp. On year rolling basis, AREITs are +18.9%, 11.8% ahead of the broader market. The two major driving forces of AREIT returns are the falling 10 year bond rate, down 10bp to finish at 2.10% as well as a solid reporting season, especially relative to industrial company results. Globally REITs were down 0.1% in February (USD terms). Year to date the UK was the best performing region +16.1% (USD terms) and Japan lagging, +4.7%.

Reporting season for AREITs showed quite a divergence in results and outlook for the industrial/office/fund managers relative to the retail/residential REITs. This was replicated in stock performance for the month with industrial/office REITs +9.3% & +4.5% vs retail REITs which were -2%. The office and industrial REITs showed comparable net property income up 4%, strong occupancy (97-98%) and continuing cap rate compression. With vacancy in Sydney/Melbourne office and industrial markets circa 3-4%, positive rental growth is expected to continue into 2020, sustaining positive leasing spreads and continuing asset value gains. Goodman Group guided to 9.5% EPS growth for FY19 and Charter Hall Group guided to 14-17% EPS growth for FY19. In contrast URW guided to EPS falling 8-9% on the back of challenging leasing conditions in the US/UK and dilutionary asset sales. Vicinity Centres guided to lower EPS growth (2-3%) as did Scentre Group with FFO growth +3%, well below consensus forecasts.

Following the postponement of US/China tariff increases and dovish comments from the Fed, global markets rallied over the month with the US +3.2% and Europe +4.4%. The US yield curve steepened slightly, +4bp to 2.71%. The Australian dollar fell 1.5c against the USD to $0.709. In Australia, data was mixed with house prices continuing to fall -0.7% in February (-6.3% Y/Y) and retail sales fell 0.4%. However, employment was strong +39k, with unemployment steady at 5%.

January private sector credit slowed more than expected to +0.2%, the weakest since 2012. Residential building approvals fell 8.4%, with the Y/Y -17%.

Portfolio performance

The Pendal Property Securities Fund returned 2.98% in February (post-fee, pre-tax), outperforming its benchmark by 1.18%.

The portfolio outperformed over the month with positive attribution from underweight positions in Vicinity Centres, Stockland Trust Group and Unibail-Rodamco Westfield and overweight positions in Mirvac Group and Charter Hall Group. Overweight positions in Arena REIT and National Storage REIT and underweight positions in Growthpoint Property, Cromwell Property Group and Charter Hall Education Trust detracted from performance.

Strategy and outlook

The AREIT sector is now priced on an FY19 dividend yield of 4.9%, a PE ratio of 18.7 times and a 38% premium to NTA, well above its long-term average of 16%. Cap rates are unlikely to compress any further from current levels and asset valuation improvements will be dependent on income growth and tenancy retention. Non-dominant discretionary malls with high specialty occupancy costs are actually expected to fall in value in the short to medium term. Balance sheets are stable with sector gearing at 28%.

International Property

Pendal Global Property Securities Fund

(managed by AEW)

Market review (in US$)

The global property securities market (on an ex-Australia basis) as measured by the FTSE EPRA Nareit Developed Index declined slightly in February, posting a total return of -0.1%. Europe (-1.9%) posted the largest decline followed by Asia Pacific (-0.4%), while North America (+0.6%) was a positive performer. Within the Asia Pacific region, results were mixed. New Zealand (-2.4%) was the weakest performer, followed by Japan (-1.9%), while Hong Kong (+1.4%) and Singapore (+0.6%) were positive performers. In Europe, results were similarly mixed across the region. The Netherlands (-9.8%) posted the largest decline, followed by Austria (-5.8%) and Germany (-4.8%). Conversely, Israel (+5.2%), the United Kingdom (+3.3%), and France (+0.5%) were positive performers during the month. In North America, the US and Canada returned 3.5% and 0.5%, respectively.

Portfolio performance

The Pendal Global Property Securities Fund returned 0.33% in February (post-fee, pre-tax), outperforming the benchmark by 0.08%.

North America

The North America portfolio returned 0.77% in February (before fees and withholding taxes), exceeding the FTSE EPRA Nareit North America Index by 16 basis points. Outperformance relative to the benchmark was driven to positive sector allocation results and, to a lesser extent,

positive stock selection results. Regarding sector allocation, positive results were driven by the portfolio's underweight to the underperforming health care and triple net lease sectors. In terms of stock selection, results were strongest in the Health Care, Hotel, and Regional Mall sectors and were weakest in the other Residential, Shopping center, and Office sectors. Among the portfolio's holdings, top individual contributors to relative performance included a lack of exposure to the underperforming Omega Healthcare Investors (OHI) and overweight positions in the outperforming Host Hotels & Resorts (HST) and Extended Stay America (STAY). Detractors most notably included overweight positions in the underperforming Pennsylvania REIT (PEI), American Campus Communities (ACC), and Americold Realty Trust (COLD).

Europe

The European portfolio returned -1.71% in February (before fees and withholding taxes), outperforming the regional EPRA benchmark by 24 basis points. Outperformance relative to the benchmark was driven by positive stock selection results, which were partially offset by negative country allocation results. In terms of stock selection, results were strongest in the Netherlands, the United Kingdom, and France and were weakest in Switzerland, Spain, and Austria. Regarding country allocation, negative results were attributable to the portfolio's overweight to the underperforming Germany and Austria. Among the portfolio's holdings, top contributors to relative performance included overweight positions in outperforming Segro PLC (United Kingdom) and Workspace Group PLC (United Kingdom), and an underweight position in the underperforming Unibail-Rodamco-Westfield (Netherlands). Detractors most notably included overweight positions in the underperforming Deutsche Wohnen SE (Germany) and Fabege AB (Sweden), and an underweight position in the outperforming Land Securities PLC (United Kingdom).

Asia

The Asia portfolio returned -0.76% in February (before fees and withholding taxes), lagging the regional EPRA benchmark by 35 basis points. Underperformance relative to the benchmark was driven by negative stock selection results in Japan and Hong Kong, while country allocation results were largely neutral. Among the portfolio's holdings, top contributors to relative performance included overweight positions in outperforming Champion REIT (Hong Kong), Keppel REIT (Singapore), and Link REIT (Hong Kong). Detractors most notably included a lack of exposure to the outperforming Hang Lung Properties (Hong Kong) and Sino Land Co. Ltd. (Hong Kong), and an overweight position in the underperforming Advance Residence Investment Corp. (Japan).

Active Balanced

Pendal Active Balanced Fund

Markets review

Australian equities extended gains through February, despite the latest reporting season seeing more earnings downgrades than the historical average – the market environment is tougher, however investors were braced for poor news. The S&P/ASX 300 Accumulation Index was up 6.0% for the month.

There was a marked rotation away from defensives over the month, towards cyclicals and the unloved as some of the macro fears receded. Financials outperformed, up +9.1% (S&P/ASX 300 Financials), with the banks outperforming despite lacklustre updates as the overhang from the Royal Commission disappeared. Resources (S&P/ASX 300 Resources) were up +6.9% as cyclicals shifted back in to favour. The S&P/ASX 300 AREIT sector underperformed, up +1.9% given the combination of its more defensive characteristics and the pressure on both the retail and residential housing sub-sectors.

Global share markets appeared to celebrate in February, pushing valuations higher largely in reaction to better prospects on the macro horizon. The US Federal Reserve (Fed) is now in a 'no rush' stance to raise interest rates, while sentiment was also supported by what appears to be a clearer path to resolving the US and China trade dispute. China's stock market certainly reflected this prospect and experienced one of the largest relief rallies, up 13.8%. Such prospects also supported most other markets to deliver strong gains and downplay other nascent risk factors. For February, the benchmark MSCI World ex Australia (A$) Index closed 5.6% higher.

Gains in the US share market were broadly based, although Information Technology registered the largest gains. Industrials and Materials stocks also moved higher as prospects for better trade relations with China supported investor sentiment. The US quarterly reporting season came to an end in February, with around 75% of companies reporting earnings growth on average of 12%, with the Industrials sector posting the best earning growth, averaging 17%. Guidance for the second quarter was generally muted; however, corporates—particularly in the technology sector—were optimistic for a strong rebound in second-half revenues. At the month's close, the S&P500 registered a 3.2% gain, while the NASDAQ had risen by 3.4%.

European share markets continued to build on January's gains to be led by cyclically oriented sectors, while the more defensive Real Estate and Utilities sectors lagged. Investors saw the decision by Trump to extend the March 1 tariff hike deadline as a sign that normalisation of trade may prevail, thereby having a positive flow-on effect for European companies. Hopes of the UK reaching a workable deal on Brexit prior to the 29 March deadline also supported sentiment. However, the uncertainty to date has likely taken a toll on economic growth for the UK, with the Bank of England cutting its GDP growth expectations to 1.2% from 1.7% for the year. UK inflation also fell below 2%, while the UK Purchasing Manager's Index fell to a 30-month low, signalling the extent of weakness in confidence for the economy. The UK's stock market etched out a 1.5% gain for February, lagging European markets like France (+5%), Germany (+3.1%) and Switzerland (+4.7%).

Most Asian equity markets also reflected optimism regarding the US-China trade issue, although performance was highly dispersed. China outpaced the region with a 13.8% gain following the Lunar New Year holiday period. Taiwan followed with a 4.6% return while South Korea bucked the trend, declining by 0.8% after talks between North Korea and the US were halted. Corporate earnings and inflation were both weaker for South Korea. Japan gained 2.9% while south-east Asian markets—Malaysia, Thailand and Singapore—registered smaller advances.

The Australian dollar lost ground against its major trading partners as sentiment shifted against the currency. The local unit fell by 2.5% against the US dollar, 1.8% against the euro and 3.6% on the British pound. In commodity markets the oil price continued its rebound to close at US$57.25 per barrel.

Australian bond yields fell during the month as the Reserve Bank of Australia (RBA) shifted its communication to suggest the outlook for rate changes was "more evenly balanced". The central bank also downgraded its projection for economic growth and lowered its inflation forecast in its quarterly Statement on Monetary Policy. In turn, markets are now pricing at least one cut from the Board over the next 12 months. Meanwhile, local economic data was mixed over the month. Labour data was stronger-than-expected with 39,000 jobs added, which was attributed to a strong increase in full-time positions. A small rebound in consumer confidence and business conditions was also encouraging. In contrast, retail sales slipped 0.4% and building approvals fell a sizeable 8.4% month-on-month. Wage data revealed a 0.5% increase over the quarter, which brought the year-on-year rate to 2.3%. Finally, the Australian 3- and 10-year yields fell 13bp and 15bp to 1.63% and 2.10%, respectively. At the very front-end, the 3-month BBSW dropped a more sizeable -20bp to 1.87%.

The US Federal Reserve's tilt to a more neutral stance in January continued to buoy risk appetite and lift global equities during the month. This was alongside optimism towards a positive outcome to US-China trade negotiations that took place in Washington late in February. Although there was no formal agreement between both sides, some perceived progress and the indefinite delay of a

proposed US tariff increase was well-received by markets. Economic data was less supportive for risk assets. US GDP figures revealed a softer 2.6% annualised growth rate for the fourth quarter and Eurozone GDP growth printed at a preliminary 0.2% quarterly growth rate. German GDP figures revealed the region's largest member had narrowly avoided a technical recession, while its Italian counterpart was not as fortunate. In terms of market movements, the US 2- and 10-year yields increased by 6 basis points (bp) and 9bp to 2.52% and 2.72%, respectively.

Portfolio performance

The Pendal Active Balanced Fund returned 3.60% (post-fee, pre-tax) for the month of February, outperforming its benchmark by 0.12%.

The Fund's return for February was largely driven by its exposure to Australian and offshore equity markets which experienced a strong rally. Overweight exposures to the best performing asset classes and investing in alternatives contributed to returns. The Australian fixed income segment also made a positive, albeit modest contribution, while international fixed interest made a small detraction from returns.

Outperformance of the benchmark was primarily driven by manager contribution within Australian equities. Our tactical asset allocation decisions saw the Fund's underweight exposure to global equities limit relative returns, as did the overweight position in international fixed interest.

The key factors influencing the alpha generated through active management were stock selection outcomes within Australian equities. Within the Australian equity strategy, overweight positions in Viva Energy, an underweight position in Woolworths and not holding Coles contributed to relative performance. Detractions from returns came from an overweight position in CSL and not holding QBE or Woodside Petroleum.

Within the global equities portfolio, the Concentrated strategy outperformed its benchmark (pre fees), but the positively trending developed markets impacted the Dynamic Market and Emerging Market equity strategies which underperformed their benchmarks, albeit generating positive returns.

The Alternatives strategy delivered a total return (before fees) of +1.32% versus a cash return of 0.17%. Our Alternatives core portfolio registered a negative return this month, whereby four of the eight sub-strategies delivered positive returns, while three had a negative impact. The Equity Market Neutral and Long-Short Equity strategies detracted from returns this month, in line with expectations for performance during a positively trending market. Meanwhile, the Global Macro, Event Driven and Convertible Arbitrage strategies added value.

In relation to our tactical positioning within the Alternatives component of the Fund, the overall positioning had a negative impact on performance. The Fund held a value adding position in Australian bonds but also held short positions in US equities, German equities and crude oil which detracted from performance in the rising market. The equities positions were neutralised by the end of the month and we will look to re-enter shorts on renewed weakness.

Strategy and outlook

Performance of the Fund in recent months has highlighted the importance of having a well-diversified and disciplined investment strategy that is founded on long-standing principles. Underlying asset markets have been particularly volatile and history tells us to expect periods of positive and negative performance through time. Despite the short term decline we saw 2018, markets have demonstrated a strong rebound this year, which highlights the importance of remaining invested through volatile periods.

We remain confident that our tried and tested investment philosophy and asset allocation processes employed by seasoned investment professionals will continue to deliver favourable

investment outcomes over the long term. We take an active approach to modelling scenarios and assessing market technical factors to identify opportunities and limit risks for our investors.

Several of our key strategies have begun to show signs of recovery in 2019 and we continue to have confidence in the team's ability to successfully navigate the market's ups and downs to deliver strong investment outcomes for our investors.

Regardless of short term market gyrations, we are always focused on continual improvement through a rigorous, research-based approach and are focused on ensuring the funds are well positioned to achieve their long term objectives.

Performance as at 28 February 2019

(%)	1 Month	3 Months	6 Months	FYTD	1 year (pa)	2 Years (pa)	3 Years (pa)	5 Years (pa)	Since Incp. (pa)
Australian Shares - All Cap									
Pendal Australian Share Fund									APIR - RFA0818AU
Total Return (post-fee, pre-tax)	6.66	8.97	-2.25	0.26	3.30	9.15	11.94	7.50	9.83
Total Return (pre-fee, pre-tax)	6.72	9.18	-1.87	0.79	4.12	10.03	12.83	8.35	10.83
Benchmark	6.01	9.86	-0.35	2.37	6.80	8.55	12.86	7.28	9.86
Pendal Imputation Fund									APIR - RFA0103AU
Total Return (post-fee, pre-tax)	6.80	8.30	-1.17	1.46	6.06	8.65	11.85	6.65	9.40
Total Return (pre-fee, pre-tax)	6.87	8.54	-0.73	2.07	7.01	9.63	12.85	7.61	10.41
Benchmark	6.01	9.86	-0.35	2.37	6.80	8.55	12.86	7.28	8.64
Pendal Focus Australian Share Fund									APIR - RFA0059AU
Total Return (post-fee, pre-tax)	6.99	8.73	-2.19	-0.19	3.02	10.14	13.26	9.10	9.06
Total Return (pre-fee, pre-tax)	7.05	8.93	-1.83	0.32	3.59	11.50	14.39	10.21	10.17
Benchmark	6.01	9.86	-0.35	2.37	6.80	8.55	12.86	7.28	7.48
Pendal Ethical Share Fund									APIR - RFA0025AU
Total Return (post-fee, pre-tax)	7.03	9.13	-2.05	0.59	2.83	8.87	11.70	7.77	8.40
Total Return (pre-fee, pre-tax)	7.11	9.38	-1.59	1.23	3.81	9.91	12.76	8.80	9.46
Benchmark	6.01	9.86	-0.35	2.37	6.80	8.55	12.86	7.28	8.03
Australian Shares - Mid Cap									
Pendal MidCap Fund									APIR - BTA0313AU
Total Return (post-fee, pre-tax)	5.23	5.16	-6.78	-5.68	-2.31	11.09	13.37	11.55	9.84
Total Return (pre-fee, pre-tax)	5.30	5.39	-6.37	-5.11	-1.38	12.52	14.68	12.94	11.99
Benchmark	5.47	7.89	-4.44	-0.90	2.40	11.46	14.34	11.36	5.75
Australian Shares - Small Cap									
Pendal Smaller Companies Fund									APIR - RFA0819AU
Total Return (post-fee, pre-tax)	6.02	5.31	-7.27	-5.20	-0.14	10.52	11.24	8.58	12.85
Total Return (pre-fee, pre-tax)	6.12	5.63	-6.70	-4.42	1.11	11.90	12.63	9.93	14.14
Benchmark	6.78	8.01	-3.06	-1.65	3.48	11.81	13.44	7.74	7.71
Australian Shares - Micro Cap									
Pendal MicroCap Opportunities Fund									APIR - RFA0061AU
Total Return (post-fee, pre-tax)	7.21	8.48	-0.94	2.23	3.44	12.66	16.26	15.11	17.72
Total Return (pre-fee, pre-tax)	7.39	8.90	-0.31	3.09	4.73	14.24	18.26	18.30	22.68
Benchmark	6.78	8.01	-3.06	-1.65	3.48	11.81	13.44	7.74	3.28
International Shares									
Pendal Core Global Share Fund									APIR - RFA0821AU
Total Return (post-fee, pre-tax)	4.93	5.27	-5.80	0.14	2.82	9.75	9.93	9.79	5.77
Total Return (pre-fee, pre-tax)	5.01	5.53	-5.35	0.79	3.81	10.79	10.98	10.84	6.93
Benchmark	5.56	5.18	-1.78	4.86	10.06	12.99	12.78	11.66	7.41
Pendal Global Emerging Markets Opportunities Fund - WS									APIR - BTA0419AU
Total Return (post-fee, pre-tax)	2.61	5.65	-0.78	0.14	1.01	12.45	13.90	8.98	10.10
Total Return (pre-fee, pre-tax)	2.72	6.02	-0.08	1.09	2.42	14.03	15.49	10.56	12.26
Benchmark	2.72	8.92	1.99	3.60	-1.30	12.74	15.19	9.02	10.04
Pendal Concentrated Global Share Fund									APIR - BTA0503AU
Total Return (post-fee, pre-tax)	5.60	5.80	2.67	6.15	10.62	15.86	N/A	N/A	14.72
Total Return (pre-fee, pre-tax)	5.69	6.09	3.17	6.84	11.67	17.13	N/A	N/A	16.02
Benchmark	5.56	5.18	-1.78	4.86	10.06	12.99	N/A	N/A	12.69
Property									
Pendal Property Securities Fund									APIR - BTA0061AU
Total Return (post-fee, pre-tax)	2.98	11.93	5.54	10.37	20.79	9.93	9.64	13.37	7.83
Total Return (pre-fee, pre-tax)	3.04	12.11	5.88	10.86	21.57	10.65	10.36	14.11	8.64
Benchmark	1.80	9.73	4.38	8.13	18.88	9.32	8.94	13.20	7.63
Pendal Global Property Securities Fund									APIR - RFA0051AU
Total Return (post-fee, pre-tax)	0.33	3.30	2.03	4.40	14.83	6.13	8.17	8.29	9.14
Total Return (pre-fee, pre-tax)	0.41	3.55	2.50	5.05	15.88	7.11	9.16	9.30	10.13
Benchmark	0.25	3.38	1.90	4.00	14.25	5.45	8.19	8.49	8.83
Fixed Interest									
Pendal Fixed Interest Fund									APIR - RFA0813AU
Total Return (post-fee, pre-tax)	0.84	2.28	1.87	2.48	4.66	3.68	2.35	4.11	6.34
Total Return (pre-fee, pre-tax)	0.87	2.41	2.12	2.82	5.18	4.20	2.86	4.63	6.90
Benchmark	0.94	3.11	3.42	4.43	6.16	4.51	3.47	4.70	6.61
Pendal Global Fixed Interest Fund									APIR - RFA0032AU
Total Return (post-fee, pre-tax)	-0.31	1.77	1.05	0.53	2.29	1.60	1.05	3.68	5.77
Total Return (pre-fee, pre-tax)	-0.27	1.91	1.31	0.88	2.83	2.14	1.58	4.23	6.35
Benchmark	-0.18	2.39	2.48	2.36	3.83	2.74	2.32	4.57	6.72
Pendal Enhanced Credit Fund									APIR - RFA0100AU
Total Return (post-fee, pre-tax)	0.81	2.16	2.52	3.42	4.47	4.14	3.68	4.46	5.70
Total Return (pre-fee, pre-tax)	0.84	2.27	2.75	3.73	4.94	4.61	4.14	4.93	6.22
Benchmark	0.76	2.17	2.60	3.56	4.78	4.26	3.77	4.51	5.81
Cash & Income									
Pendal Enhanced Cash Fund									APIR - WFS0377AU
Total Return (post-fee, pre-tax)	0.26	0.61	1.10	1.52	2.17	2.64	2.70	2.73	4.85
Total Return (pre-fee, pre-tax)	0.28	0.67	1.22	1.69	2.42	2.89	2.96	2.99	5.19
Benchmark	0.17	0.51	0.99	1.35	1.99	1.87	1.91	2.14	4.78
Pendal Managed Cash Fund									APIR - WFS0245AU
Total Return (post-fee, pre-tax)	0.15	0.47	0.95	1.28	1.89	1.83	1.90	2.11	6.33
Total Return (pre-fee, pre-tax)	0.17	0.53	1.06	1.42	2.11	2.06	2.13	2.33	6.63
Benchmark	0.17	0.51	0.99	1.35	1.99	1.87	1.91	2.14	6.40
Pendal Monthly Income Plus Fund									APIR - BTA0318AU
Total Return (post-fee, pre-tax)	1.32	2.31	0.99	2.04	3.18	4.30	4.01	4.36	5.32
Total Return (pre-fee, pre-tax)	1.37	2.47	1.31	2.48	3.85	4.98	4.69	5.04	5.99
Benchmark	0.12	0.37	0.75	1.00	1.51	1.51	1.56	1.85	2.80
Diversified									
Pendal Active Balanced Fund									APIR - RFA0815AU
Total Return (post-fee, pre-tax)	3.60	4.86	-2.12	0.02	2.17	6.29	7.40	6.71	7.52
Total Return (pre-fee, pre-tax)	3.68	5.10	-1.66	0.66	3.14	7.30	8.42	7.73	8.60
Benchmark	3.48	5.66	0.53	3.27	6.55	7.57	9.17	7.35	7.48

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