

Fund Manager Commentary

Month ended 31 May 2019

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Australian Shares

Pendal Australian Share Fund

Market Review

Sentiment around the domestic economy improved following the Coalition party's surprise win in the Federal election. This saw the Australian equity market, as measured by the S&P/ASX 300 Accumulation Index, extended its gains this year by another 1.7%. This is in contrast to the global equity market (-4.3%, the MSCI World Index in AUD) which was caught in the crosshairs of the ongoing US-China trade war tensions. Consequently, Crude oil was down by 16% over the month, whereas the US10-year bond yield fell by 36 basis points (bp) to 2.14% by the end of May, largely reflecting investor concerns over global economic growth in the near term.

Throughout May, Industrials (+1.9%) outperformed with the help of strong performance from Financials (+2.6%), and in particular the Banks (+5.3%). The broad outlook for the economy and earnings has changed favourably post the election. No change in government and therefore no significant policy shifts is expected to improve sentiment for older consumers and help business confidence. Subsequent indications from the Reserve Bank of Australia (RBA) of a June rate cut (which subsequently came to fruition), together with news APRA may reduce its mortgage serviceability assessment rate from 7.25% provided investors with some assurance policy makers are actively trying to avoid a housing confidence-led downturn. The net expectation is that the retention of negative gearing, lower rates and an easier serviceability hurdle will combine to stabilise the housing market and, in turn, reduce pressure on the banks. The 'big four' banks all recorded positive returns for the month, ranging from 3.4% (WBC) to 8.1% (NAB).

Resources (+1.3%) was the laggard, as Energy (-3.8%) pulled back amid a lower oil price. Metals & Mining (+3.3%) in general provided some offset, with the exception of Copper (-10.3%), which is another proxy for global growth prospects. At the sector level, Communication Services (+7.1%) recorded the best sector return whereas Consumer Staples (-4.2%) was both the worst performing sector in terms of absolute return and the largest performance detractor from the headline index return. China-related growth stocks, including Treasury Wine (TWE, -12.5%) and A2 Milk (A2M, -8.0%) weighed on the sector as Sino-US trade tensions intensified. With the exception of Consumer Staples, Information Technology (-3.1%) and Utilities (-0.6%) also finished the month lower.

Turning to the stock specifics, lower-grade iron ore producer Fortescue Metals Group (FMG, +20.6%) was the best performer amongst the iron ore miners. The cohort is enjoying a sweet spot considering the confluence of a number of macro and stock-specific factors. Reasonable Chinese demand and a reduction in Brazilian production is supporting prices at a far higher level than the market expected. FMG's return was boosted by the announcement of a 60c-a-share special dividend - the company's total yield, including special dividends and buy-backs, is now running at about 20%, providing plenty of stock support. Elsewhere, Xero (XRO, +9.8%) was the largest performance contributor to the IT sector. The accounting software company delivered a well-received result where subscriber growth was led by the UK division. Net profits and free cash flow from the second half also turned positive for the first time. The key attraction here is subscription growth as XRO rolls the model out into the UK and US following its success in Australia and New Zealand. They have achieved traction in the UK market in the most recent half, which is important given the one-off opportunity provided by the shift to an online tax system.

Within the same sector, Link Administration (LNK, -21.4%) was the largest performance detractor. The financial administration company tumbled on a profit warning, as management downgraded FY19 earnings (EBITDA) expectations to between \$350 and \$360m, versus consensus

expectations of \$390m. Management pointed to a drop in revenues in its UK business as Brexit has seen IPOs and secondary listings dry up.

Portfolio performance

The Pental Australian Share Fund (formerly the BT Wholesale Core Australian Share Fund) returned 2.05% (post-fee, pre-tax) in May, outperforming its benchmark by 0.30%.

Contributors

Overweight Nine Entertainment

Sentiment around the domestic economy improved following the Coalition party's surprise win in the Federal election. In turn, this bolstered investor confidence and share price performance of consumer stocks, including our preferred Nine Entertainment (NEC, +18.9%). During the month management indicated that while the overall trend in TV advertising remains weak, this is being offset through market share growth. Stan continues to see good growth, as does their digital channel. We believe that investors are under-estimating the value in these divisions.

QBE Insurance Group - not held

QBE Insurance Group (QBE, -9.7%) saw its share price retreat over the month, despite a lack of major news. The recent strong performance may be the reason for some profit taking in May. In addition, concerns arose in relation to US crop risks, whereby farmers could claim on their insurance instead of planting at the last minute for maximum coverage. This would lead to a worse-than-expected FY19 result for the insurer. We do not own QBE and this contributed to relative performance.

Overweight Telstra

The Australian Competition and Consumer Commission (ACCC) ruled against the tie-up between telecom operators TPG Telecom (TPM, -6.7%) and Vodafone. The ACCC's position is based on TPG following through on its initial plan to build a 5G mobile network and create a fourth mobile operator. However, TPG have announced they will no longer spend the billions required to build a credible network, citing the increased costs as a result of being prohibited from using Huawei technology. The outcome will be a legal tussle which is likely to be resolved towards the end of CY19 at best and this could drag on into mid next year. In the near term this is a positive for Telstra (TLS, +8.0%) as it further delays roll-out of a competitive 5G network.

Detractors

Overweight Santos

Our overweight in Santos (STO, -6.3%) detracted from portfolio performance in May. The oil price (-16%) declined in May as investors became more risk averse amid the intensified trade-war jitters. STO remains our preferred exposure to the oil/LNG thematic, with cyclical tailwinds augmented by significant self-help measures over the past couple of years. STO management have been successful in increasing drilling efficiencies and slashing per-unit costs, which has boosted their cash flow on the back of energy price tailwinds. Management have used this to pay down debt, bolstering balance sheet strength and further increasing their leverage to stronger oil prices.

Underweight NAB

The net expectation from the Coalition's surprise win in the Federal election is that the retention of negative gearing, lower rates and an easier serviceability hurdle will combine to stabilise the housing market and, in turn, reduce pressure on the banks. As such, our underweight in NAB weighed on performance in May. We remain underweight banks following RBA's recent rate cut in

June. While this is seen as limiting the downside risk from housing which is ultimately good for the banks, it also results in more pressure on margins and earnings for the core mortgage businesses. Consensus expectations are for the RBA to cut the cash rate again and if this occurs banks will be under pressure to pass the cut to customers which is likely to have a negative impact on earnings. The issue is compounded by the reluctance of most banks to cut deposit rates and risk losing flows, together with the fact that it becomes progressively harder to cut rates anyway, given they are already at very low levels.

The key takeaway is while sentiment on banks has no doubt improved, we are still cautious on their ability to sustain outperformance given the pressure on revenue, margins, costs and earnings. Valuations remain cheap by some measures, but look less compelling once earnings pressure is factored into the equation.

Overweight Oil Search

Our overweight in Oil Search (OSH, -6.3%) detracted from portfolio performance in May. The oil price (+16%) declined in May as investors became more risk averse amid the intensifying trade war jitters. In addition, there were mixed updates on the political front in Papua New Guinea (PNG) where the company operates a major project. PNG's Prime Minister Peter O'Neill resigned towards the end of the month as pressure mounted following the unveiling of the PM's prior involvement in a UBS loan incident and handling of the \$16b gas deal. There are some investor concerns that a change of government could lead to a re-negotiation of OSH's gas agreements.

Strategy and outlook

The portfolio outperformed the Index across an eventful month for Australian equities. The Coalition's unexpected victory in the Federal election buoyed the domestic equity market, allowing it to gain ground even as most other countries declined on increased trade tensions.

The election result also saw material rotation within the market. Consumer cyclicals tended to outperform as the removal of the political threat to negative gearing and franking credits saw an improvement in sentiment around domestic demand. This helped the portfolio's positions in companies such as Nine Entertainment (NEC) and JB Hi-Fi (JBH). Labor's loss also means less pressure on private health insurance premiums, which was beneficial for the stake in Ramsay Health Care (RHC).

The retention of negative gearing, in addition to signals from the RBA they would look to cut rates in June, has helped remove some of the downside risk of a housing-led economic downturn. Reports that APRA may reduce the mortgage service test have also helped bolster sentiment.

That said, we think this is more a case of removing some downside risk, rather than prompting a material recovery in housing prices any time soon. The economy is still working its way through a surplus of recent housing construction, while it remains to be seen if property investors return to the market. Greater focus on lending standards is still serving to keep credit growth tight.

Nevertheless, banks enjoyed a relief rally over the month. We are underweight the sector in aggregate and this detracted from performance. At this point we are not compelled to add to our position in banks. While the sector may enjoy some near-term momentum—which in part reflects the nadir to which sentiment had fallen—we are cautious on the sector's ability to sustain outperformance. Revenue growth remains muted, while high costs mean banks will find it hard to grow earnings over the coming halves. Rate cuts, while good for sentiment around housing, ultimately mean further pressure on earnings, which is only partially offset by more benign offshore funding conditions. Valuations are at historical lows by some measures, but look less compelling once earnings pressure is factored in.

Broadly speaking, we believe the election outcome has been positive for the broader outlook. The economy had been showing signs of deceleration in the past few months. We have been mindful of

some distortion with the timing of Easter and its proximity to Anzac Day, as well as the election itself.

Nevertheless, we are in a crucial period in terms of gauging the underlying strength of the economy. The moves by the RBA and APRA provide confidence that policy makers are actively seeking to avoid a housing confidence-led downturn. No change in government should also improve consumer sentiment and support business confidence.

From here, we expect to see mid-to-high single digit earnings growth over the next 12 months, although there is significant divergence between sectors. For example, Resources should have high growth while we expect to see muted growth from banks. Nevertheless, this level of earnings is broadly supportive for equity market returns.

Pendal Smaller Companies Fund

Market review

There was some performance divergence between the S&P/ASX Small Ordinaries Accumulation Index and its broad cap counterpart, the S&P/ASX 300 Accumulation Index. The former finished May (-1.3%) lower, underperforming the latter by 3.0%. This was partly due to the rally in banks following the Federal election and talk of rate cuts from the RBA. At the same time, weakness was noted among some of the larger stocks within the small cap universe.

Both Small Resources (-1.0%) and Small Industrials (-1.3%) ended the month lower. The headline index was trading at a one-year forward price/earnings multiple of 16.4x following May's losses, a 7% premium to its five-year average.

Communication Services (+4.5%) was one of the best performing GICS sectors over the month, mainly driven by Vocus Group (VOC, +17.4%) and Domain (DHG, +21.9%). The network fibre owner/operator received a non-binding, indicative proposal from EQT Infrastructure to acquire all shares in VOC at A\$5.25 per share, representing a 35% premium to its then closing price. The acquisition process was subject to the satisfactory completion of due diligence and regulatory approvals, but nevertheless bolstered investor interest. DHG rose amid a surprise win by the Coalition in the Federal election. The broad outlook for the economy and earnings has changed favourably post the election. No change in government and therefore no significant policy shifts is expected to improve sentiment for older consumers and help business confidence. Subsequent indications from the RBA of a June rate cut became a reality, while APRA's move to reduce its mortgage serviceability test from 7.25% provided investors with some assurance that policy makers are actively seeking to avoid a housing confidence-led downturn. This supported sentiment towards the property listing platform operator.

Index heavyweight Materials (+0.7%) also outperformed in May. Stock returns were somewhat divergent, with the likes of Lynas Corporation (LYC, +54.0%), Saracen Mineral (SAR, +14.7%) and CSR (+15.8%) delivering double-digit gains, while St. Barbara (SBM, -17.4%) and Nufarm (NUF, -22.1%) detracted. LYC, a rare earth miner was one of the few beneficiaries from intensifying Sino-US trade tensions, with speculation China could strangle global rare earth supplies in retaliation to the latest round of tariffs imposed by the Trump administration. Management also outlined a \$500m growth program that will be self-funded. In contrast, mid-tier gold miner SBM disappointed the market with another production downgrade for its Gwalia mine, due to temporary blockage in the mine's paste fill reticulation. Production volumes from the mine is now expected to be 220 thousand ounces (koz), compared to the 235-240koz guidance provided previously.

Consumer Staples (-8.1%) finished the month as the worst-performing sector. Metcash (MTS, +2.8%), Select Harvests (SHV, +10.3%) and Blackmores (BKL, +2.2%) outperformed, although the gains were more than offset by Costa Group (CGC, -30.3%), Graincorp (GNC, -14.2%) and Bellamy's (BAL, -20.6%). CGC delivered a guidance downgrade that disappointed the market. The company disappointed on a number of fronts, including a later-than-usual blueberries harvest from

its Moroccan acreage which brings the product into competition with Spanish suppliers, putting pressure on prices. At the same time, CGC has experienced issues with the quality of its raspberry crop and the discovery of a fruit fly at its NSW citrus farms which could see an increase in costs as fruit is shipped elsewhere for storage and packing. There was also some pressure on costs for its mushroom produce. Conversely, crop grower GNC released its first-half results, where earnings (EBITDA) for the period dropped by 78% year-on-year despite a 25% increase in sales. The persistent east coast drought conditions continue to weigh on the Grains division whereas margin compression was evident in both the malt and oils businesses. The market also remains sceptical about management's commentary around the proposed spin-off of the malts business towards the end of 2019.

Portfolio performance

The Pental Smaller Companies Fund returned -2.34% (post-fee, pre-tax) in May, underperforming the S&P/ASX Small Ordinaries Accumulation Index by 1.09%.

Contributors

Overweight Mainfreight

Mainfreight (MFT, +9.0%) is a New Zealand-listed logistics company. We view the company's business model as attractive, which is acting as a disruptor in the increasingly globalised world of packaging and the movement of goods. MFT delivered a strong set of full-year financial results towards the end of May. Net underlying profit was up 28% for the year and the company has flagged plans for additional domestic freight facilities in Sydney and on the Sunshine Coast to increase capacity.

Overweight AP Eagers

Car dealer AP Eagers (APE, +19.2%) began the month with a profit warning at its annual general meeting, citing weakness in national car sales this year. The stock's reaction was muted, as investors remained focused on the benefits of its proposed merger with Automotive Holdings Group (AHG). However, the Federal election result, in combination with signs the RBA would move to cut interest rates, saw the stock surge over the second half of May as investor sentiment improved around consumer cyclicals.

Detractors

Underweight Lynas Corporation

Rare earths producer Lynas Corporation (LYC, +54.0%) subsided from its initial share price spike following the takeover approach from Wesfarmers (WES) in March. However, the share price rose in May as China threatened to restrict the export of rare earths as part of the ongoing trade friction with the United States. Not owning LYC hurt relative performance but we remain cautious at this point. Not only does the outcome of trade negotiations remain opaque, LYC also faces the additional exogenous risk of political pressure in Malaysia around the waste from its beneficiation plant.

Overweight Technology One

Technology One (TNE, -18.4%) delivered a strong set of half-year results in May. However, management's full-year profit guidance came in at 45% growth, which was below consensus estimates. The stock sold off as a result, but is still up almost 60% for the previous 12 months. TNE is among our preferred exposures in the small cap technology sector. This is partly due to over two decades of profitable operations, whereas some of the other options in this space are yet to be proven over a cycle.

Outlook

The broader Australian market bucked the global trend of equity index declines, as the surprise victory by the LNP Coalition outweighed the uncertainties over global trade. However, a large portion of the S&P/ASX 300's 1.2% gain was driven by the index-heavyweight banks, which were up between 3% and 8%. This was in response to both the election result and moves by the RBA and APRA to help support the housing market.

Lacking this driver, the small cap sector declined -1.3%. Large parts of the market did well, but this was not enough to offset areas of weakness such as energy, where trade concerns weighed on the oil price. There was also some weakness in the small cap tech sector, where the largest index stock—Afterpay Touch (APT)—went backwards. Consumer staples declined due a combination of events including a downgrade by Costa Group (CGC) and the withdrawal of a private equity bid for Graincorp (GNC).

The Fund underperformed the Index. Not owning Lynas Corp (LYC) was a material detractor as interest in rare earths surged on threats from the Chinese Government to restrict their supply to the US. Not owning private health insurer NIB Holdings (NHF)—which surged on the election result, as well as Clinuvel Pharmaceuticals (CUV) and Vocus Communication (VOC) dragged on relative returns. The holding in Costa Group was also a detractor.

Consumer cyclicals tended to outperform as the removal of the political threat to negative gearing and franking credits, plus the expectation of an interest rate cut, saw an improvement in sentiment around domestic demand and the threat of a housing-led downturn. This helped the Fund's positions in companies such as Nine Entertainment (NEC), AP Eagers (APE) and Ooh Media (OML) outperform.

Broadly speaking, we believe the election outcome has been positive for the broader economic outlook. The economy had been showing signs of deceleration in the past few months. We have been mindful of some distortion from the timing of Easter and its proximity to Anzac Day - as well as the election itself.

Nevertheless, we are in a crucial period in terms of gauging the underlying strength of the economy. The moves by the RBA and APRA give confidence that policy makers are actively seeking to avoid a housing confidence-led downturn. No change in government should also improve consumer sentiment and support business confidence.

This all remains broadly supportive for the small cap market, although we are mindful that the developments of the last month are more likely to remove some of the downside risk, rather than ignite a material near-term improvement in economic activity.

International Shares

Pendal Concentrated Global Share Fund

Market review

Most major indices were down between 5-10% in May in response to an escalation of trade tensions between the US and China, emerging trade issues between the US and Mexico, continued Brexit uncertainty and weakness in global economic data.

The 10-year treasury yield fell to the lowest level since September 2017 closing at just over 2%. Bond markets are now pricing in three US rate cuts over the next 12 months.

The US market led the declines, with all but one of the 11 sector groups registering a negative return, real estate being the exception. Energy stocks were impacted by concerns over demand

growth for oil while the technology sector declined amid moves by the US Government against Huawei. Conclusion of the corporate earnings season was also a notable concern, with around 95% of US companies now having reported quarterly results. Earnings growth for five out of the 11 sectors was negative for the quarter and while a handful of companies acknowledged that a second-half earnings recovery is less likely, the majority are still projecting an earnings recovery. At the month's close, the S&P500 declined 6.6%, while the NASDAQ declined by 7.9%.

European markets also registered general weakness, despite the prevalence of localised issues. Elections were in focus for some markets, although results were mostly as expected. Economic indicators showed some degree of resilience, with the Flash Eurozone Composite PMI indicator for the region remaining broadly unchanged in expansionary territory. Conditions were particularly strong in Germany. In terms of market performance, the region's benchmark Euro Stoxx Index fell by 6.7%, although country level performance was considerably dispersed. Switzerland (-2.5%) and the UK (-3.5%) were at one extreme while Italy (-9.5%) and France (-6.8%) were in contrast.

Asian equity markets were not immune to the sell-off, considering the weight of sentiment towards US-China trade tensions. During the month the US announced it was raising tariffs on US\$200 billion of imports from China to 25% from 10%, and China responded by increasing tariffs on US\$60 billion of imports from the US. The weight on sentiment was most notable in China's markets, with Hong Kong (-9.2%) and to a lesser extent, China (-5.5%) bearing the brunt of the selloff. ASEAN markets were also generally weaker, evidenced by declines in Singapore (-8.3%), Indonesia (-3.8%) and Thailand (-3.2%), however Malaysia (+0.5%) and India (+1.5%) were clear exceptions. The latter performed well following a return to power of India's ruling BJP party in the world's largest general election to date.

The Australian dollar weakened against the majors, down 1.6% against the US dollar, 4.4% against the yen and around 1.2% weaker against the euro but 1.5% higher against the British pound. In commodity markets the oil price collapsed by 16.3% to close at US\$53.50 per barrel, while gold rose 1.7% to US\$1305 per ounce.

Portfolio performance

The Pandal Concentrated Global Share Fund returned -4.60% (post fee, pre-tax) in May, underperforming its benchmark by 0.17%.

Markets weigh on performance but portfolio shows resilience

The Fund declined in value through May, consistent with the broader negative sentiment. Among the detractors were our positions in Analog Devices, Lloyds Banking Group and Las Vegas Sands. Conversely, positions in Merck, Pfizer, Pernot Rickard, Deutsche Boerse and CME Group delivered gains. Our investments in stock exchanges tend to perform well in periods of heightened market sensitivity which often drives trading volumes. In addition, the Fund's 10.5% cash holding served to protect capital as markets declined.

Locking in gains at the top

The Fund exited its 2% position in Restaurant Brands International (QSR US) this month. The stock reached our target price at an all-time high in May, representing a 36% return (in Australian dollar terms) since the position was initiated. The cash weighting in the Fund—held at its current level of around 9% since December 2018—has reflected concerns the earnings growth and margins implied by consensus estimates looked optimistic. We remain of this view and look forward to opportunities to deploy the cash.

Pfizer beats expectations with a healthy outlook

Our holding in Pfizer outperformed this month, rising after the company reported its first-quarter results at the end of April. Revenues of US\$13.1b beat consensus estimates, as did earnings per

share (EPS, 85c). Management increased their EPS guidance and reaffirmed their revenue guidance for 2019. Outperformance on sales was driven by a number of different product lines, while the EPS result was driven by higher gross margins, lower operating costs and a more aggressive buyback of shares.

The share price received a further boost from the earlier than expected approval of Tafamadis, a drug that treats a rare and under-diagnosed heart condition caused by excessive protein deposits in the heart.

While the quarterly results and subsequent product approval was pleasing, our positive long term outlook for the company reflects our favourable view on the management team who are looking beyond their last major near term patent expiration and remain focused on an approval pipeline for new products in six key therapeutic areas.

We believe this strategy should allow for mid-single digit revenue growth and high single digit EPS growth beyond 2020.

Spirits remain high as management continue to invest

Our holding in Pernod Ricard also outperformed this month. Pernod is the world's second-largest spirits company, with a 20% share of the premium spirits market. After reporting quarterly numbers in April which provided evidence of strong underlying sales trends in most markets, the company also subsequently announced the acquisition of Italian premium gin brand, Malfy, which has a presence in the US, UK and Germany.

The market appears to have a growing confidence in the company's ability to meet medium term organic sales growth targets of 4-7% between 2019-2021, while at the same time improving margins by 50-60bp per annum.

We are encouraged by management's strategy of continuing to invest in brands with strong potential in growing categories, while at the same time being opportunistic about divesting businesses that are not going to contribute to the longer term goals of the group.

Considering the geographic diversity of this group, coupled with a number two global market share, we believe the company is in a strong position to navigate the current macroeconomic uncertainty.

Semiconductors sold on trade tensions

With the semi-conductor index (SOX US) declining by about 16% this month, our holdings in Texas Instruments and Analog Devices (ADI) also underperformed. The weakness in the sector relates to the breakdown of trade talks between China and the US along with actions of the US Department of Commerce which has essentially barred US firms from supplying components to Huawei.

The sanctions also prevent global firms with subsidiaries in the US or whose products are deemed to have more than 25% of US manufactured content from supplying Huawei. Huawei reportedly consumes anywhere between 5-10% of the world's semiconductors.

Texas Instruments have confirmed that Huawei accounts for under 5% of sales, while Analog Devices have confirmed Huawei accounts for mid-single digits of total sales. Both companies have halted shipments to Huawei in order to comply with the new US Export Administration Regulations.

Analog Devices (ADI) reported its second-quarter results in May. Revenue growth was ahead of prior guidance, although the company provided third-quarter guidance for revenue to decline by 8% over the year. This assumes zero contribution from Huawei.

Despite the negative guidance and continuing uncertainty regarding US/China trade, we believe the diversity of ADI's customer and product suite hold it in good stead. ADI has between 80,000 to 100,000 customers across a number of industry sectors and although it is not immune to the impacts of a trade war, such diversity does provide a degree of insulation relative to peers.

The company operates with gross margins in excess of 70%, operating margins that exceed 40%, and cash flow margins of around 35%.

With its breadth of product proliferation across a number of industries and with only a handful of competitors, we believe ADI will focus on what they can control and act opportunistically as market conditions permit.

Strategy and outlook

Although markets were lower this month, volatility remains depressed which is somewhat counter intuitive, given the level of uncertainty in markets.

While we would expect volatility to increase in this environment, we don't purport to predict macro-economic and geopolitical outcomes with any degree of certainty.

However, the current cash position reflects some concern that second-half earnings growth expectations appear optimistic for a number of companies.

Our focus remains on owning companies that are equipped with robust business models, have credible and nimble management teams and hold dominant market shares.

We buy these companies when valuations are compelling and when we have the confidence they are able to not only withstand, but prosper regardless of what the economic cycle may have to offer.

We believe the Fund is positioned to outperform over the long term and remain forthright in our belief of owning a concentrated portfolio of businesses to deliver attractive returns rather than a portfolio of indiscriminate broader market exposure which is more susceptible to market volatility and uncontrollable factors.

Pendal Core Global Share Fund

(managed by AQR Capital Management)

Market review

Most major indices were down between 5-10% in May in response to an escalation of trade tensions between the US and China, emerging trade issues between the US and Mexico, continued Brexit uncertainty and weakness in global economic data.

The 10-year treasury yield fell to the lowest level since September 2017 closing at just over 2%. Bond markets are now pricing in three US rate cuts over the next 12 months.

The US market led the declines, with all but one of the 11 sector groups registering a negative return, real estate being the exception. Energy stocks were impacted by concerns over demand growth for oil while the technology sector declined amid moves by the US Government against Huawei. Conclusion of the corporate earnings season was also a notable concern, with around 95% of US companies now having reported quarterly results. Earnings growth for five out of the 11 sectors was negative for the quarter and while a handful of companies acknowledged that a second-half earnings recovery is less likely, the majority are still projecting an earnings recovery. At the month's close, the S&P500 declined 6.6%, while the NASDAQ declined by 7.9%.

European markets also registered general weakness, despite the prevalence of localised issues. Elections were in focus for some markets, although results were mostly as expected. Economic indicators showed some degree of resilience, with the Flash Eurozone Composite PMI indicator for the region remaining broadly unchanged in expansionary territory. Conditions were particularly strong in Germany. In terms of market performance, the region's benchmark Euro Stoxx Index fell by 6.7%, although country level performance was considerably dispersed. Switzerland (-2.5%) and the UK (-3.5%) were at one extreme while Italy (-9.5%) and France (-6.8%) were in contrast.

Asian equity markets were not immune to the sell-off, considering the weight of sentiment towards US-China trade tensions. During the month the US announced it was raising tariffs on US\$200 billion of imports from China to 25% from 10%, and China responded by increasing tariffs on US\$60 billion of imports from the US. The weight on sentiment was most notable in China's markets, with Hong Kong (-9.2%) and to a lesser extent, China (-5.5%) bearing the brunt of the selloff. ASEAN markets were also generally weaker, evidenced by declines in Singapore (-8.3%), Indonesia (-3.8%) and Thailand (-3.2%), however Malaysia (+0.5%) and India (+1.5%) were clear exceptions. The latter performed well following a return to power of India's ruling BJP party in the world's largest general election to date.

The Australian dollar weakened against the majors, down 1.6% against the US dollar, 4.4% against the yen and around 1.2% weaker against the euro but 1.5% higher against the British pound. In commodity markets the oil price collapsed by 16.3% to close at US\$53.50 per barrel, while gold rose 1.7% to US\$1305 per ounce.

Portfolio performance

The Pandal Core Global Share Fund returned -5.18% (post-fee, pre-tax) in May, underperforming its benchmark by 0.75%.

Underperformance this month occurred in the North America and Europe portfolios, while developed Asia produced offsetting outperformance of its regional benchmark.

Thematically, Valuation was weak in all regions and responsible for overall underperformance over the month. In North America, Value, Quality and Sentiment factors drove underperformance, offset somewhat by positive returns to Momentum themes. In Europe, underperformance was due to weakness in Value and Momentum, offset somewhat by the positive performance of Quality and Sentiment. In Asia, the outperformance was due to the strength of Momentum signals, outweighing weakness in Value over the month.

From a stock and industry attribution perspective, industry tilts produced positive active returns, while intra-industry stock selection generated negative active returns over the month. At a sector level, the overweight tilts to Health Care and Utilities were the notable positive contributors, while an overweight tilt to Information Technology was the largest negative contributor. Stock selection within industries was weakest within Consumer Discretionary and Industrials, offset somewhat by positive active returns to stock selection within Financials.

At a stock level, the largest positive contributors to active returns came from underweight positions in Bank of America Merrill Lynch, a US multi-national investment bank; Exxon Mobil Corporation, a multi-national oil and gas corporation headquartered in Texas; J.P. Morgan Chase & Co., a multi-national investment bank and financial services company; Broadcom Inc., a US designer, developer, manufacturer and global supplier of a broad range of semiconductor and infrastructure software solutions; and Nvidia Corporation, a US technology company headquartered in California.

The largest detractors from active returns over the month came from overweight positions in Capri Holdings., a multi-national fashion holding company headquartered in New York; Skyworks Solutions, a US semiconductor company; Covestro, a manufacturer of high-tech polymer materials; Ralph Lauren, a US corporation producing mid-range to luxury fashion products; and Deutsche Lufthansa AG (Lufthansa), a major European airline headquartered in Germany.

Strategy and outlook

Entering June, the largest sector tilts are overweights in Industrials and Health Care and underweight positions in Financials and Energy.

Australian Fixed Income

Pendal Fixed Interest Fund

Market review

Australian bond yields fell substantially during May with larger declines at the long-end leading to a further flattening of the curve. The slide was driven by growing expectations of a rate cut from the RBA, as well as offshore movements led by the US. By month-end the market was pricing over a 90% probability of a rate reduction by the Reserve Bank in June. This followed an address by Governor Lowe in which he signalled an intention to act in the wake of a weaker employment picture and ongoing subdued inflation. At the time of writing, expectations had become reality with a 25bp cut delivered on June 4th. Domestic data through the month supported such a decision. The unemployment rate unexpectedly rose to 5.2% in spite of a larger number of job additions than anticipated. First quarter wage numbers missed expectations with 0.5% growth over the period, which kept the year-on-year rate at a sluggish 2.3%. Turning to market movements, the Australian 3 and 10 year yields fell by a sizeable 19bp and 33bp to 1.10% and 1.47% respectively. 90 day BBSW also experienced a large fall of 15bp to 1.42% alongside a lower repo rate, partly reflecting firmer expectations of a June RBA cut.

Portfolio performance

The Pendal Fixed Interest Fund returned 2.06% in May (post-fees, pre-tax), outperforming its benchmark by 0.36%.

The Fund outperformed its benchmark during May, which was driven by the alpha overlay. In the alpha overlay, the Duration strategy was the largest contributor from long duration exposures across a range of regions that benefited from the sizeable fall in global yields. The Yield Curve strategy was the second largest contributor of the month. Gains were predominantly from the US front end flattener as the market moved to price in more Fed cuts for the rest of this year. The FX strategy also added value from long USD positions against a range of EM currencies. Meanwhile, the Macro and Cross-Market strategies were roughly flat. Finally, the credit and government components of the fund both added value.

Strategy and outlook

The Reserve Bank eased monetary policy at its meeting in early June. It is highly likely that further easing occurs in the coming months. There had been ample opportunity for the Reserve Bank to ease at the May meeting - inflation data disappointed in late April and economic growth weakened over the second half of 2018. Why didn't the Board cut? The labour data had shown strong employment growth over the past 12 months and was at odds with the weak household consumption in the national accounts. Business liaison also indicated some labour tightness emerging in some areas. However, the increase in the unemployment rate from 5% to 5.2% revealed a weaker picture and in turn was the last domino to fall. The Reserve Bank had been looking for increasing labour market tightness feeding into underlying inflation. The increase in the unemployment rate put that to bed - there is more than ample slack in the labour market that will not result in the wage inflation outcomes they are looking for. For their forecasts to be achieved further policy easing will be required and soon, the question is not whether they ease again but how many times it occurs. The labour data will again be key in determining when the next rate cut occurs.

International Fixed Income

Pendal Global Fixed Interest Fund

Market review

Global bond yields fell substantially during May with larger declines at the long-end leading to a flattening of the curve. The market's attention was firmly centred on the latest bout in the ongoing trade war as a further escalation damaged investor sentiment. Concerns were renewed when President Trump raised tariffs from 10% to 25% on US\$200b of Chinese imports after claiming the Chinese broke a proposed deal. Policymakers in Beijing responded in kind with tariffs on US\$60b of imports from the US. Towards month-end tensions increased after Chinese telecom provider, Huawei, was blacklisted by US authorities. Separately, the Trump administration threatened tariffs on Mexico if illegal immigration from its southern neighbour was not curtailed. Beyond trade developments, US data weakened over the period. In combination with the trade war concerns this fanned expectations that the Federal Reserve would be required to cut rates over the next twelve months. Turning to market movements, US yields witnessed large declines with the 2 year and 10 year lower by 34bp and 38bp to 1.92% and 2.13% respectively.

Portfolio performance

The Pendal Global Fixed Interest Fund returned 2.18% in May (post-fees, pre-tax), outperforming its benchmark by 0.33%.

Over the month, the Duration strategy was the strongest performer. Yield Curve and FX strategies added to performance too, while Macro and Cross-Market strategies were roughly flat. Over the month, the portfolio risk level started at 6 risk units and rose to 11 units intra-month and closed the month at 6 risk units.

The Duration strategy was the largest contributor over the month. Throughout the month we kept long duration positions across markets globally. The majority of the gains were from long duration positions in the US front end. Long duration positions in New Zealand front end also performed strongly over the month. In emerging markets, we took profit on long duration positions in the long end of the Korean Won curve in the end of the month, while in China we added to long duration positions and held them through the intra-month volatility as the trade war between US and China escalated to a new level. As at month end, we continued to hold long duration positions in the front end of the US and New Zealand curves.

The FX strategy performed well over the month. Gains were mainly contributed by long USD positions against EM currencies, particularly in Asian markets. Profits were split between IDR, KRW and TWD, while the long THB experienced a minor loss. In G10 FX markets, gains were made from a long JPY short AUD position.

The Yield Curve strategy was the second largest contributor of the month. Gains were predominantly from the US front end flattener as the market moved to price in more Fed cuts for the rest of this year. Our steepening positions in the longer end in the US and Australian curves slightly detracted from performance.

The Macro strategy was roughly flat over the month. Gains were contributed by a buy protection position in CDX EM, offsetting the minor losses in CDX HY flattening position. As of the end of the month all positions in Macro strategy are closed.

There were no trades in the Relative Value strategy for this month.

In the Cross Market strategy, we opened a tactical long US short Australia position in the long end of the curves. This position was closed during the month with largely flat performance.

Strategy and outlook

Markets continue to contend with two dominant forces on the global stage; shifting perspectives on rapidly-evolving trade wars and the prospect of central bankers acting on a more dovish policy bias. While these continue to play out in headlines and contribute to the daily noise across wires, the economic engines of global growth are slowly stalling. After what was undeniably a period of exceptionalism, the US is exhausted and forward-looking indicators have turned. At the same time its trade adversary, China appears content with a lower growth profile and one that is more internally-focused - to the detriment of its neighbours. Predicting the outcome of trade wars brings inherent danger. However, the deteriorating outlook for the world's largest economies and the need for a refuel from central banks is becoming more apparent and continues to support our long duration bias over the medium term.

Credit

Pendal Enhanced Credit Fund

Market review

Australian credit generated another positive return in May, driven by a fall in yields and healthy accruals. The drop in yields was alongside firmer expectations of an RBA rate cut. At the same time renewed concerns over trade wars prompted a flight to safety that sent global yields lower.

Following a recent hiatus by the Big Four domestic banks, Westpac and NAB returned to debt capital markets and raised \$3.5b and A\$1b respectively. Offshore banks also conducted deals of a reasonable size, including Citibank with an A\$1.25b issue, Sumitomo Mitsui with \$500m and Credit Agricole with \$600m. Issuance from supras was also strong through the month. In aggregate it was the largest monthly volume since January in spite of the weaker backdrop for risk assets.

The Australian iTraxx index (Series 31 contract) traded in a 12.5bp range finishing the month 12bp wider to +78bp. Physical credit spreads on the other hand narrowed 1bp over the month, with the best performing sectors being utilities and real estate tightening 4 and 2bp respectively. The worst performing sector was domestic banks which finished 1bp wider. Semi-government bonds were basically unchanged to government bonds.

Portfolio performance

The Pendal Enhanced Credit Fund returned 1.12% in May (post-fees, pre-tax), matching the benchmark return.

A fall in underlying rates and accruals made a positive contribution. Positions in infrastructure and utilities, where the Fund is overweight, outperformed the credit index. Portfolio purchases over the period included issuance from Westpac and NAB.

Strategy and outlook

Our overall credit view remains cautiously constructive. We are positive on corporate fundamentals, but are wary that appetite for credit has demonstrated varying sensitivity to geopolitical developments and the ongoing trade war.

From a bottom-up perspective, corporates in the US have demonstrated resilience with upside surprises to earnings growth in the Q1 reporting season. Similarly, domestic fundamentals remain relatively healthy as issuers have not increased balance sheet leverage materially over the past several years. The major Australian banks also have stronger capital ratios than previous years, which should support domestic financial stability. Moreover the weight of the Royal Commission has finally been lifted from their shoulders. That said, recent results from the majors have revealed challenges as a result of the Commission as well as slowing mortgage growth.

From a macro standpoint, the volatility has itself been volatile over the past six months. Elevated levels during 2018 (particularly December), subsided in January this and resurfaced again this month. This has been alongside shifting perspectives towards the trade war central bank policy stance. While the more dovish tilt from central bankers is a significant positive, we are wary that attitudes towards these developments can shift quickly as the story evolves, particularly with geopolitical flare-ups.

Of further consideration is the softening of domestic economic growth, where there is likely further risk to the downside as weak wage growth and the house price correction threaten to dampen consumption. As such we continue to recommend a defensive approach with any overweights in 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 substantially during May with larger declines at the long-end leading to a further flattening of the curve. The slide was driven by growing expectations of a rate cut from the RBA, as well as offshore movements led by the US. By month-end the market was pricing over a 90% probability of a rate reduction by the Reserve Bank in June. This followed an address by Governor Lowe in which he signalled an intention to act in the wake of a weaker employment picture and ongoing subdued inflation. At the time of writing, expectations had become reality with a 25bp cut delivered on June 4th.

Domestic data through the month supported such a decision. The unemployment rate unexpectedly rose to 5.2% in spite of a larger number of job additions than anticipated. First quarter wage numbers missed expectations with 0.5% growth over the period, which kept the year-on-year rate at a sluggish 2.3%. Leading indicators also softened including the NAB Business Survey; conditions fell from +7 to +3 and the employment subcomponent dropped from +6.2 to -1.2. Housing credit growth also slowed further from 4.2% year-on-year to 4.0% and retail sales grew by only 0.3% versus 0.8% in the prior month. There was likely a negative impact on some data points, particularly confidence data, due to uncertainty around the pending Federal Election.

Meanwhile offshore, attention was firmly centred on the latest bout in the ongoing trade war as a further escalation damaged investor sentiment. Concerns were renewed when President Trump raised tariffs from 10% to 25% on US\$200b of Chinese imports after claiming the Chinese broke a proposed deal. Policymakers in Beijing responded in kind with tariffs on US\$60b of imports from the US. Towards month-end tensions increased after Chinese telecom provider, Huawei, was blacklisted by US authorities. Separately, the Trump administration threatened tariffs on Mexico if illegal immigration from its southern neighbour was not curtailed.

Beyond trade developments, US data weakened over the period. In combination with the trade war concerns this fanned expectations that the Federal Reserve would be required to cut rates over the

next twelve months. Leading indicators such as the ISM manufacturing gauge for April fell to 52.8, the lowest since October 2016. Durable goods orders for the same period fell -2.1%, advanced retail sales slipped -0.2% and industrial production contracted by -0.5%. Lagging indicators reflected a more constructive picture; payrolls grew at a stronger-than-expected 263k, which caused the unemployment rate to fall to a new 49 year low of 3.6%. Revised first quarter GDP also surprised to the upside with a healthy 3.1% annualised rate.

Elsewhere, the ECB did not meet during the month and Eurozone data showed signs of stabilising. The preliminary Eurozone composite PMI ticked 0.1 of a point higher to 51.6 and retail sales data was flat versus expectations of a contraction. Data in China was less encouraging with falls in both the official and Caixin measures of manufacturing PMI. Total social financing was also weaker-than-expected and fixed asset investment slowed to 6.1% year-on-year.

Turning to market movements, the Australian 3 and 10 year yields fell by a sizeable 19bp and 33bp to 1.10% and 1.47% respectively. 90 day BBSW also experienced a large fall of 15bp to 1.42% alongside a lower repo rate, partly reflecting firmer expectations of a June RBA cut. US yields witnessed even greater declines with the 2 year and 10 year lower by 34bp and 38bp to 1.92% and 2.13% respectively. Despite a narrower AU-US yield differential, the Australian Dollar ended lower against its US counterpart on a combination of weaker domestic data, the outlook for a lower cash rate and the broader risk-off environment.

Turning to credit markets, synthetic credit spreads widened as the supportive backdrop for risk appetite deteriorated throughout the month. This was tied predominantly to renewed fears and uncertainty over the negative impact of the trade war escalation. This overshadowed the more dovish policy stance from the Fed that had been offered earlier in the year. That said, the domestic physical credit market outperformed its offshore counterparts with support likely stemming from a positive reaction to the Coalition's victory in the Federal Election.

The Australian iTraxx index (Series 31 contract) traded in a 12.5bp range finishing the month 12bp wider to +78bp. Physical credit spreads on the other hand narrowed 1bp over the month, with the best performing sectors being utilities and real estate tightening 4 and 2bp respectively. The worst performing sector was domestic banks which finished 1bp wider. Semi-government bonds were basically unchanged to government bonds.

Portfolio performance

Managed Cash

The Pental Managed Cash Fund returned 0.16% in May (post-fees, pre-tax), outperforming the benchmark by 0.01%.

With a higher running yield than the index remains well positioned to outperform. Themes and credit exposure remain consistent with prior months, with the excess spread from A-1 rated issuers and security selection likely to be the main driver of outperformance. The yield curve has flattened significantly and consequently yield curve strategies are less likely to add to performance in the near term. The Fund ended the month with a weighted average maturity of 60 days (maximum limit of 70 days). The weighted average maturity had consistently been longer than benchmark due to the higher yields available further out the curve with minimal risk of any monetary policy tightening from the Reserve Bank. With yields having rallied aggressively longer dated yields do not look as attractive unless monetary policy easing does occur - something we expect to happen. We remain wary of extending too far out the curve, particularly if the curve inverts.

The Fund is well positioned to outperform its benchmark.

Enhanced Cash

The Pental Enhanced Cash Fund returned 0.20% in May (post-fees, pre-tax) outperforming the benchmark by 0.05%.

Positive performance came primarily from financials and industrials sectors.

Activity during the month included investing in a primary market short dated major bank deal funded out of cash.

As at the end of the month, the portfolio had a credit spread of 61bp over bank bills, interest rate duration of 0.13 years and credit spread duration of 1.12 years.

Strategy and outlook

The Reserve Bank eased monetary policy at its meeting in early June. It is highly likely that further easing occurs in the coming months. There had been ample opportunity for the Reserve Bank to ease at the May meeting - inflation data disappointed in late April and economic growth weakened over the second half of 2018. Why didn't the Board cut? The labour data had shown strong employment growth over the past 12 months and was at odds with the weak household consumption in the national accounts. Business liaison also indicated some labour tightness emerging in some areas. However, the increase in the unemployment rate from 5% to 5.2% revealed a weaker picture and in turn was the last domino to fall. The Reserve Bank had been looking for increasing labour market tightness feeding into underlying inflation. The increase in the unemployment rate put that to bed - there is more than ample slack in the labour market that will not result in the wage inflation outcomes they are looking for. For their forecasts to be achieved further policy easing will be required and soon, the question is not whether they ease again but how many times it occurs. The labour data will again be key in determining when the next rate cut occurs.

Australian Property

Pendal Property Securities Fund

Market review

The ASX 300 AREIT index was up 2.5% in May, outperforming the broader market by 80bp, with the strongest performance coming from the residential REITs. REITs were driven by the 10 year bond yield falling 33bp (to finish at 1.45%) and the Coalition election victory also saw a relief rally for residential exposed stocks. On a rolling 12 months AREITS are +17.0%, outperforming the broader market by 5.9%. Globally REITs were down 0.2% for the month, with the Japanese AREIT sector the best performer at +4.2% and UK REITs the worse, down 6.3%. Year to date, the US REIT sector was the best performing market (+15.5%) with the worst performing market being the UK (+7.7%).

May saw two large scale capital raisings with DXS and MGR both tapping the equity market. DXS raised \$900m to acquire a 75% interest in 80 Collins St Melbourne (the other 25% acquired by its unlisted Diversified Fund), one existing office tower and another under construction, with completion in 2020. The project also includes a 255 room hotel and CBD retail. Mirvac raised \$750m to help fund its office, industrial and to a lesser extent residential development pipeline. Both equity issues were well received with the stocks trading up strongly post raisings. Scentre Group also divested 50% of its Burwood regional mall at a 4% premium to book value, on a 4.8% cap rate.

Increasing trade tension saw global markets retrace sharply, with developed markets down 5.6% and emerging markets down 6.6%. Worst sectors were IT (-8.4%) and Energy (-8.2%). Despite this the ASX200 saw a 1.7% increase, supported by a more market friendly election outcome (Coalition

win) and a significant fall in bond yields. Australian and US 10 year bond yields were flat over the month closing at 1.78% and 2.50% respectively.

Employment was solid +28.4k positions, however, a 20bp lift in the participation rate (to 65.8%) saw a 10bp increase in the unemployment rate to 5.2%. The RBA virtually guaranteed an interest rate cut for June stating rates needed to fall to help lift inflation towards its 2% target. Credit growth continues to be sluggish +0.2% month/month, and up 3.7% Y/Y, a 6 year low. Building approvals data was weaker than expected at -4.7% M/M and -24.2% Y/Y.

Portfolio performance

The Pandal Property Securities Fund returned 2.24% in May (post-fee, pre-tax), underperforming its benchmark by 0.06%.

Positive attribution from underweight positions in Unibail Rodamco Westfield and Scentre Group and overweight positions in Lifestyle Communities and Mirvac Group. An underweight position in Stockland Trust Group and overweight positions in GDI Property group, Japara Healthcare, Arena REIT and Charter Hall Retail REIT detracted from performance.

Over the month we increased our overweight positions in Goodman Group, Charter Hall Long WALE and reduced our underweight positions in Dexus Property Group and Stockland Trust Group. This was funded by reducing our overweight positions in GPT and National Storage REIT and increasing our underweight position in Unibail Rodamco Westfield.

Strategy and outlook

The AREIT sector is now priced on an FY19 dividend yield of 4.7%, a PE ratio of 19.3 times and a 44% 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 27%.

International Property

Pandal Global Property Securities Fund

(managed by AEW)

Market review (in US\$)

Performance of the global property securities market (on an ex-Australia basis) as measured by the FTSE EPRA Nareit Developed Index declined slightly in May, posting a total return of -0.3%.

Europe (down 0.7%) posted the largest decline followed by Asia Pacific (down 0.6%) and North America (down 0.1%). Within the Asia Pacific region, results were mixed. Hong Kong (down 5.7%) was the weakest performer, followed by Singapore (down 3.7%), while Japan (up 4.2%) was a positive performer; New Zealand was flat for the month. In Europe, results were similarly mixed across the region. The Netherlands (down 11.3%) posted the largest decline, followed by the United Kingdom (down 6.3%) and France (down 2.8%). Conversely, Austria (up 8.7%), Finland (up 7.2%), and Germany (up 6.1%) were notable positive performers. In North America, the US and Canada returned -0.1% and 0.7%, respectively.

Portfolio performance

The Pental Global Property Securities Fund returned -0.22% in May (post-fee, pre-tax), outperforming the benchmark by 0.20%.

North America

The North America portfolio returned 0.02% in May before fees and withholding taxes, slightly exceeding the FTSE EPRA Nareit North America Index by seven basis points. Modest outperformance relative to the benchmark was driven by positive stock selection results, which were partially offset by negative sector allocation results. In terms of stock selection, results were strongest in the health care, hotel, and storage sectors and were weakest in the shopping center, triple net lease, and diversified sectors. Regarding sector allocation, negative results were driven by the portfolio's underweight to the outperforming health care and storage sectors. Conversely, the portfolio's overweight to the outperforming other residential sector was a notable contributor to relative performance. Among the portfolio's holdings, top individual contributors to relative performance included overweight positions in outperforming HCP, Inc. (HCP) and CubeSmart (CUBE), and an underweight position in underperforming Prologis (PLD). Detractors most notably included overweight positions in underperforming Boston Properties (BXP) and Howard Hughes (HHC), and a lack of exposure to outperforming Ventas (VTR).

Europe

The European portfolio returned 0.41% in May before fees and withholding taxes, outperforming the regional EPRA benchmark by 115 basis points. Outperformance relative to the benchmark was driven by both positive stock selection and positive country allocation results. In terms of stock selection, results were strongest in the United Kingdom, Netherlands, and Sweden and were weakest in France, Spain, and Austria. Regarding country allocation, positive results were attributable to the portfolio's overweight to the outperforming Germany and Austria. Among the portfolio's holdings, top contributors to relative performance included overweight positions in outperforming Vonovia SE (Germany), Wihlborgs Fastigheter AB (Sweden), and Deutsche Wohnen SE (Germany). Detractors most notably included overweight positions in underperforming Workspace Group PLC (United Kingdom) and Gecina SA (France), and a lack of exposure to outperforming PSP Swiss Property AG (Switzerland).

Asia

The Asia portfolio returned -0.53% in May before fees and withholding taxes, slightly beating the regional EPRA benchmark by six basis points. Outperformance relative to the benchmark was driven by positive stock selection results in Japan and Hong Kong, which were partially offset by negative results in Singapore. Country allocation results were largely neutral. Among the portfolio's holdings, top contributors to relative performance included a lack of exposure to underperforming Sino Land (Hong Kong) and Hang Lung Properties (Hong Kong), and an overweight position in outperforming Nippon Building Fund (Japan). Detractors most notably included overweight positions in underperforming New World Development (Hong Kong), CapitaLand (Singapore), and CK Asset Holdings (Hong Kong).

Active Balanced

Pendal Active Balanced Fund

Markets review

Sentiment around the domestic economy improved following the Coalition party's surprise win in the Federal election. This saw the Australian equity market, as measured by the S&P/ASX 300 Accumulation Index, extended its gains this year by another 1.7%. Throughout May, Industrials (+1.9%) outperformed with the help of strong performance from Financials (+2.6%), and in particular the Banks (+5.3%). The broad outlook for the economy and earnings has changed favourably post the election. Resources (+1.3%) was the laggard, as Energy (-3.8%) pulled back amid a lower oil price. Metals & Mining (+3.3%) in general provided some offset, with the exception of Copper (-10.3%), which is another proxy for global growth prospects. Communication Services (+7.1%) recorded the best sector return whereas Consumer Staples (-4.2%) was both the worst performing sector in terms of absolute return and the largest performance detractor from the headline index return.

Most major overseas equity indices were down between 5-10% in May in response to an escalation of trade tensions between the US and China, emerging trade issues between the US and Mexico, continued Brexit uncertainty and weakness in global economic data.

The 10-year treasury yield fell to the lowest level since September 2017 closing at just over 2%. Bond markets are now pricing in three US rate cuts over the next 12 months.

The US equity market led the declines, with all but one of the 11 sector groups registering a negative return, real estate being the exception. Energy stocks were impacted by concerns over demand growth for oil while the technology sector declined amid moves by the US Government against Huawei. Conclusion of the corporate earnings season was also a notable concern, with around 95% of US companies now having reported quarterly results. Earnings growth for five out of the 11 sectors was negative for the quarter and while a handful of companies acknowledged that a second-half earnings recovery is less likely, the majority are still projecting an earnings recovery. At the month's close, the S&P500 declined 6.6%, while the NASDAQ declined by 7.9%.

European markets also registered general weakness, despite the prevalence of localised issues. Elections were in focus for some markets, although results were mostly as expected. Economic indicators showed some degree of resilience, with the Flash Eurozone Composite PMI indicator for the region remaining broadly unchanged in expansionary territory. Conditions were particularly strong in Germany. In terms of market performance, the region's benchmark Euro Stoxx Index fell by 6.7%, although country level performance was considerably dispersed. Switzerland (-2.5%) and the UK (-3.5%) were at one extreme while Italy (-9.5%) and France (-6.8%) were in contrast.

The Australian dollar weakened against the majors, down 1.6% against the US dollar, 4.4% against the yen and around 1.2% weaker against the euro but 1.5% higher against the British pound. In commodity markets the oil price collapsed by 16.3% to close at US\$53.50 per barrel, while gold rose 1.7% to US\$1305 per ounce.

Australian bond yields fell substantially during May with larger declines at the long-end leading to a further flattening of the curve. The slide was driven by growing expectations of a rate cut from the RBA, as well as offshore movements led by the US. By month-end the market was pricing over a 90% probability of a rate reduction by the Reserve Bank in June. This followed an address by Governor Lowe in which he signalled an intention to act in the wake of a weaker employment picture and ongoing subdued inflation. At the time of writing, expectations had become reality with a 25bp cut delivered on June 4th. Domestic data through the month supported such a decision. The unemployment rate unexpectedly rose to 5.2% in spite of a larger number of job additions than

anticipated. First quarter wage numbers missed expectations with 0.5% growth over the period, which kept the year-on-year rate at a sluggish 2.3%. Turning to market movements, the Australian 3 and 10 year yields fell by a sizeable 19bp and 33bp to 1.10% and 1.47% respectively. 90 day BBSW also experienced a large fall of 15bp to 1.42% alongside a lower repo rate, partly reflecting firmer expectations of a June RBA cut.

Global bond yields fell substantially during May with larger declines at the long-end leading to a flattening of the curve. The market's attention was firmly centred on the latest bout in the ongoing trade war as a further escalation damaged investor sentiment. Concerns were renewed when President Trump raised tariffs from 10% to 25% on US\$200b of Chinese imports after claiming the Chinese broke a proposed deal. Policymakers in Beijing responded in kind with tariffs on US\$60b of imports from the US. Towards month-end tensions increased after Chinese telecom provider, Huawei, was blacklisted by US authorities. Separately, the Trump administration threatened tariffs on Mexico if illegal immigration from its southern neighbour was not curtailed. Beyond trade developments, US data weakened over the period. In combination with the trade war concerns this fanned expectations that the Federal Reserve would be required to cut rates over the next twelve months. Turning to market movements, US yields witnessed large declines with the 2 year and 10 year lower by 34bp and 38bp to 1.92% and 2.13% respectively.

Portfolio performance

The Pandal Active Balanced Fund returned -0.44% (post-fee, pre-tax) for the month of May, underperforming its benchmark by 0.16%.

The Fund's return for May was negatively impacted by exposure to offshore equity markets. Australian shares and listed property provided a partially offsetting effect, as did Australian and overseas fixed income, highlighting the importance of diversification in the Fund. Exposure to Alternatives detracted from returns this month.

Performance relative to the benchmark was impacted largely by the asset allocation position, while the underlying investment strategies provided a net positive contribution.

The key factors influencing the alpha generated through active management were stock selection outcomes within Australian and international equities. Within the Australian equity strategy, overweight positions in Nine Entertainment and Telstra contributed to performance, although this was partially offset by an overweight position in Santos and underweight position in NAB.

Within the global equities portfolio, the Core and European Value strategies underperformed their respective benchmarks (pre fees), largely due to stock-specific outcomes. However, the emerging markets strategy generated over 3% in excess returns. These active strategies are long term in nature and can be expected vary in performance during shorter term periods.

The Alternatives strategy delivered a total return (before fees) of -2.19% versus a cash return of 0.15%. Within our Alternatives core portfolio the Global Macro, Equity Market Neutral and Managed Futures strategies detracted from returns, while most of the offsetting gains came from the Dedicated Short Bias and Long/Short Equity strategies.

In relation to our tactical positioning within the Alternatives component of the Fund, the main detraction came from our long volatility position and exposure to crude oil, while long positions in Australian, German and US bond markets registered marginal gains. May's market environment was driven more by tweets than investment fundamentals. We remain concerned of an escalation in rhetoric and the potential impact on market prices and are defensively positioned within bond markets.

Strategy and outlook

Geopolitics are continuing to have a disproportionate impact on investment markets, causing many assets to deviate from their intrinsic value. May saw the return of a risk-off environment in many overseas markets as investors grew weary of the fallout from the trade war and the questions over economic leadership in Europe and the UK.

The trade issue between the US and China is likely to permeate markets for some time and flow on to other markets, given the inter-relationships in our globalised world. Our investment strategy takes into account short term considerations such as this, but is weighted more towards longer term, fundamentally driven return expectations.

Focusing on the domestic economy, the Reserve Bank's decision to ease monetary policy at its meeting in early June highlighted the conundrum facing policy makers. It is highly likely that further easing occurs in the coming months, largely dependent on what happens in the labour market. Business confidence is likely to improve following the election but sustaining a positive sentiment is heavily reliant on consumer behaviour, which is where much of the concern lies.

Beyond the headline impacts, there are opportunities in asset markets to tactically add value. We take these opportunities within a systematic approach while maintaining a focus on risks. This approach has served investors well over the long term and we see no reason for that to change.

Performance as at 31 May 2019

(%)	1 Month	3 Months	6 Months	FYTD	1 year	2 Years	3 Years	5 Years	Since
					(pa)	(pa)	(pa)	(pa)	Incp. (pa)
Australian Shares - All Cap									
Pendal Australian Share Fund APIR - RFA0818AU									
Total Return (post-fee, pre-tax)	2.05	4.59	13.97	4.86	7.04	10.62	10.29	7.83	9.92
Total Return (pre-fee, pre-tax)	2.12	4.81	14.44	5.64	7.91	11.51	11.17	8.68	10.92
Benchmark	1.75	5.01	15.37	7.50	10.93	10.46	10.57	7.79	9.96
Pendal Imputation Fund APIR - RFA0103AU									
Total Return (post-fee, pre-tax)	2.26	4.42	13.09	5.95	9.17	10.23	10.00	6.95	9.51
Total Return (pre-fee, pre-tax)	2.34	4.66	13.60	6.83	10.16	11.22	10.99	7.91	10.53
Benchmark	1.75	5.01	15.37	7.50	10.93	10.46	10.57	7.79	8.79
Pendal Focus Australian Share Fund APIR - RFA0059AU									
Total Return (post-fee, pre-tax)	3.14	6.26	15.54	6.06	8.24	12.13	12.04	9.55	9.36
Total Return (pre-fee, pre-tax)	3.20	6.46	15.97	6.79	8.90	13.41	13.26	10.66	10.47
Benchmark	1.75	5.01	15.37	7.50	10.93	10.46	10.57	7.79	7.71
Pendal Ethical Share Fund APIR - RFA0025AU									
Total Return (post-fee, pre-tax)	1.78	4.26	13.78	4.88	7.17	10.27	9.79	8.03	8.53
Total Return (pre-fee, pre-tax)	1.86	4.51	14.31	5.79	8.19	11.32	10.83	9.06	9.59
Benchmark	1.75	5.01	15.37	7.50	10.93	10.46	10.57	7.79	8.21
Australian Shares - Mid Cap									
Pendal MidCap Fund APIR - BTA0313AU									
Total Return (post-fee, pre-tax)	1.60	3.90	9.25	-2.01	-0.97	12.04	10.88	11.93	9.99
Total Return (pre-fee, pre-tax)	1.68	4.13	9.74	-1.19	-0.16	13.48	12.16	13.33	12.12
Benchmark	-1.36	1.79	9.83	0.88	2.67	10.04	10.23	11.30	5.79
Australian Shares - Small Cap									
Pendal Smaller Companies Fund APIR - RFA0819AU									
Total Return (post-fee, pre-tax)	-2.34	0.93	6.29	-4.32	-4.67	11.21	7.64	8.75	12.76
Total Return (pre-fee, pre-tax)	-2.24	1.25	6.95	-3.22	-3.48	12.60	8.98	10.11	14.05
Benchmark	-1.25	2.69	10.91	1.00	2.06	13.13	9.84	8.82	7.75
Australian Shares - Micro Cap									
Pendal Micro Cap Opportunities Fund APIR - RFA0061AU									
Total Return (post-fee, pre-tax)	0.80	5.25	14.18	7.60	8.73	14.71	14.72	13.37	17.81
Total Return (pre-fee, pre-tax)	1.47	6.09	15.53	9.36	10.62	16.41	17.28	19.65	22.76
Benchmark	-1.25	2.69	10.91	1.00	2.06	13.13	9.84	8.82	3.42
International Shares									
Pendal Core Global Share Fund APIR - RFA0821AU									
Total Return (post-fee, pre-tax)	-5.18	-1.73	3.45	-1.60	-0.73	4.44	7.22	9.80	5.65
Total Return (pre-fee, pre-tax)	-5.12	-1.51	3.93	-0.74	0.20	5.42	8.24	10.84	6.80
Benchmark	-4.43	1.42	6.67	6.34	8.82	9.31	10.63	12.19	7.39
Pendal Global Emerging Markets Opportunities Fund - WS APIR - BTA0419AU									
Total Return (post-fee, pre-tax)	-2.82	2.08	7.85	2.23	1.86	6.54	12.06	9.15	10.04
Total Return (pre-fee, pre-tax)	-2.71	2.43	8.60	3.55	3.29	8.03	13.62	10.73	12.17
Benchmark	-5.78	-1.95	6.80	1.59	-0.29	5.77	11.52	7.97	9.33
Pendal Concentrated Global Share Fund APIR - BTA0503AU									
Total Return (post-fee, pre-tax)	-4.60	-1.53	4.18	4.53	7.18	9.19	N/A	N/A	12.72
Total Return (pre-fee, pre-tax)	-4.51	-1.26	4.75	5.49	8.25	10.37	N/A	N/A	14.00
Benchmark	-4.43	1.42	6.67	6.34	8.82	9.31	N/A	N/A	12.06
Property									
Pendal Property Securities Fund APIR - BTA0061AU									
Total Return (post-fee, pre-tax)	2.24	6.12	18.78	17.13	19.69	12.03	8.97	13.86	8.03
Total Return (pre-fee, pre-tax)	2.30	6.29	19.16	17.83	20.47	12.76	9.69	14.60	8.85
Benchmark	2.30	6.00	16.31	14.61	17.22	11.30	8.22	13.63	7.82
Pendal Global Property Securities Fund APIR - RFA0051AU									
Total Return (post-fee, pre-tax)	-0.22	2.56	5.95	7.07	9.56	7.57	6.28	7.51	9.16
Total Return (pre-fee, pre-tax)	-0.14	2.80	6.45	7.99	10.56	8.56	7.26	8.50	10.16
Benchmark	-0.42	2.22	5.67	6.31	8.48	6.65	6.10	7.50	8.84
Fixed Interest									
Pendal Fixed Interest Fund APIR - RFA0813AU									
Total Return (post-fee, pre-tax)	2.06	3.81	6.18	6.38	7.21	4.34	3.45	4.40	6.43
Total Return (pre-fee, pre-tax)	2.11	3.94	6.44	6.87	7.75	4.86	3.97	4.92	6.98
Benchmark	1.70	3.85	7.08	8.44	8.96	5.25	4.33	5.01	6.70
Pendal Global Fixed Interest Fund APIR - RFA0032AU									
Total Return (post-fee, pre-tax)	2.18	3.68	5.52	4.22	4.97	2.80	2.11	4.04	5.91
Total Return (pre-fee, pre-tax)	2.23	3.82	5.79	4.73	5.53	3.34	2.65	4.59	6.49
Benchmark	1.85	3.56	6.03	6.00	6.33	3.88	3.09	4.84	6.84
Pendal Enhanced Credit Fund APIR - RFA0100AU									
Total Return (post-fee, pre-tax)	1.12	3.01	5.23	6.53	6.85	4.60	4.26	4.65	5.78
Total Return (pre-fee, pre-tax)	1.16	3.12	5.47	6.97	7.33	5.07	4.73	5.12	6.30
Benchmark	1.12	3.00	5.23	6.66	7.05	4.69	4.30	4.71	5.89
Cash & Income									
Pendal Enhanced Cash Fund APIR - WFS0377AU									
Total Return (post-fee, pre-tax)	0.20	0.71	1.33	2.24	2.42	2.62	2.74	2.69	4.83
Total Return (pre-fee, pre-tax)	0.22	0.78	1.45	2.48	2.68	2.88	3.00	2.95	5.17
Benchmark	0.15	0.48	0.99	1.84	1.99	1.88	1.87	2.10	4.76
Pendal Managed Cash Fund APIR - WFS0245AU									
Total Return (post-fee, pre-tax)	0.16	0.48	0.96	1.76	1.92	1.85	1.87	2.07	6.29
Total Return (pre-fee, pre-tax)	0.18	0.53	1.07	1.97	2.14	2.07	2.09	2.30	6.59
Benchmark	0.15	0.48	0.99	1.84	1.99	1.88	1.87	2.10	6.37
Pendal Monthly Income Plus Fund APIR - BTA0318AU									
Total Return (post-fee, pre-tax)	1.23	3.01	5.39	5.11	5.66	5.01	4.36	4.62	5.50
Total Return (pre-fee, pre-tax)	1.28	3.18	5.74	5.74	6.35	5.70	5.04	5.31	6.17
Benchmark	0.13	0.38	0.75	1.39	1.51	1.51	1.53	1.80	2.77
Diversified									
Pendal Active Balanced Fund APIR - RFA0815AU									
Total Return (post-fee, pre-tax)	-0.44	1.77	6.71	1.79	2.48	5.62	6.38	6.68	7.52
Total Return (pre-fee, pre-tax)	-0.36	2.01	7.22	2.69	3.46	6.63	7.39	7.70	8.59
Benchmark	-0.28	2.84	8.65	6.20	7.96	7.54	7.82	7.54	7.51

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