PENDAL

Fund Manager Commentary

Month ended 31 July 2019

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Market Review

Performance was strong for the Australian market in July, with the S&P/ASX 300 Accumulation index recording another 3%. While all sectors finished the month in the black, both index heavyweights Financials (-1.8%) and Materials (+1.2%) were laggards. The latter's muted performance was also in a stark contrast to the stronger iron ore price over the period (+10%).

Brazil's Vale has been successful in bringing around one-third of its shuttered production back on line, following the shut-downs that occurred after the tragic tailings dam disaster earlier in the year. It will take Vale's production between 60 and 90 days to find its way back into the market – and it is still a long way short of previous production. The iron ore price has subsided from its highs and an increase in trade friction may prompt further volatility. As such, the iron ore trio, BHP (-1.0%), Fortescue Metals (FMG, -7.6%) and Rio Tinto (RIO, -4.7%) all pulled back over the month.

Within Financials, bank performance remained muted: CBA (-0.6%) received several downgrades from brokers ahead of August reporting season, as it was trading at a valuation premium to its Big Four peers, which is getting harder to justify given the subdued operating environment domestically. CYB Group (CYB) also fell -9.4% for the month following its quarterly update, which disappointed on margins as competitive pressure remains strong. Management have pointed to the fact that front book pricing has started to improve (i.e. their most recent loans). That said, the back book remains a headwind for margins. NAB (+6.7%) was the standout from the cohort, as its appointment of the new CEO was well received by the market. Ross McEwan, who is currently the outgoing CEO of RBS in the UK and previously the head of CBA's Retail Banking Services division, has committed himself to protecting and accelerating NAB's transformation program. Outside the banks, AMP (AMP, -15.6%) came under pressure as management announced that the sale of its life insurance and mature business to Resolution Life is unlikely to proceed following intervention by the Reserve Bank of New Zealand (RBNZ). The RBNZ requires New Zealand-related assets to be ring-fenced, which would require a renegotiation of terms with Resolution Life. Management cancelled its interim dividend as a result.

Turning to the other side of the tally board, Consumer Staples (+9.6%) led the gainers, with Woolworths (WOW, +7.2%) being the largest contributor. The supermarket giant is combining its liquor business, Endeavour Drinks – the owner of Dan Murphy's and BWS – with its ALH Group, which is Australia's largest poker machine operator to create Endeavour Group. WOW is also planning to spin off this newly created entity in 2020, which will be a $7-8bn standalone business, with an implied EV/EBITDA multiple of 12x based on the market's current pricing. Also within the sector, China growth related market darlings, a2 Milk (A2M, +23.6%) and Treasury Wine (TWE, +18.6%) both rallied. The recent retail price increase for A2M's infant formula has given some investors more confidence that the company is likely to beat earnings expectation in August. TWE also rose in anticipation of a decent FY19 result, although there is a sense that they may be pulling forward some Chinese demand.

Lastly, CIMIC (CIM, -18.0%) saw a backlash to its quarterly update, with the market concerned over weaker cash flows. CIM has been under some pressure from an institutional short-seller, who noted the use of "reverse-factoring" arrangements as an accounting tool which can potentially help improve the optics on working capital. The practice, which involves using third-party institutions to honour accounts payable, then repaying the institution, may prove to be a niche issue in the upcoming reporting season if its use is wider spread.

Portfolio performance

The Pendal Australian Share Fund (formerly the BT Wholesale Core Australian Share Fund) returned 2.51% (post-fee, pre-tax) in July, underperforming its benchmark by 0.46%.

Contributors

Overweight Viva Energy

Viva Energy (VEA, +13.7%) rebounded strongly over the month, recouping the losses incurred in June. Both VEA and its peer Caltex (CTX, +8.9%) have been put under pressure over the past 18 months due to lower refining margins and refinery outage. In addition, there have been signs of economic deceleration in recent months which, in combination with higher oil prices in A$, has put some pressure on retail fuel volumes. VEA has a balanced portfolio of products which provides broader exposure, meaning it is not reliant just on retail fuel. Interest rate and tax cuts and the potential for further broader fiscal measures also provide a measure of underlying support for consumer demand. We retain our conviction in the company.

Woodside Petroleum – no holding

Woodside Petroleum (WPL, -4.6%) delivered an underwhelming set of 2Q19 results in July. Production volume came in somewhat weak, as a maintenance led plant outage at Pluto caused lower volumes. In addition, realised prices over the quarter were also below that of 2Q18, resulting in a $165m hit to sales revenue over the quarter.

Overweight Metcash

Woolworth's proposed demerger of its hospitality group over the month provided a positive read-through for our preference in Metcash (MTS, +12.5%). Metcash runs three lines of businesses: Food, Liquor and Hardware and is currently trading at ~7x EV/EBITDA. While it is not a perfect like-for-like comparison, the implied multiple of Bunnings from Coles; and that of Endeavour Group from WOW help to provide some benchmark pricing for Metcash's Hardware and Liquor businesses. As such, it suggests that Metcash's Food business, which has been operating in a challenging environment is clearly undervalued at 5x EV/EBITDA. This helps to underpin our investment thesis in Metcash, and that any sight of sales growth improvement in the Food business, however slim, will likely see a re-rate for the company.

Detractors

Overweight Fortescue Metals

Fortescue Metals (FMG, -7.6%) pulled back in July alongside its iron ore miner peers. The company's most recent quarterly update was reasonably constructive. The discount for its lower-grade ore – which had blown out at points in the last couple of years – was slimmer than most had expected. The miners remain hugely cash generative and recent dividends and buybacks can be sustained in the near term. We have been reducing our overweight in iron ore in recent weeks, mainly via a reduction in Rio Tinto, but retain our exposure in FMG.

Overweight Amcor

Packaging company Amcor (AMC, -4.1%) sold off over July, despite the lack of any company specific news. Pepsi did report the 2Q19 results where its North America volume was down 2% over the reported periods. Some investors might take the weak trend as a negative read through for Amcor, as its North American rigid plastics accounts for ~20% of the company's revenues.

A2 Milk – no holding

It was a strong month for a2 Milk (A2M, +23.6%), and not owning it dragged on portfolio relative performance. The recent retail price increase for A2M's infant formula has given some investors more confidence that the company is likely to beat earnings expectation in August. The stock is currently trading on a FY1 P/E valuation of ~36x which we find hard to justify.

Strategy and outlook

The market is entering the FY19 reporting season at an interesting juncture, having enjoyed a very strong surge over the previous six months but with macro uncertainty (trade wars, Brexit) driving bouts of volatility. At the same time, there are clear signals that domestic demand has not recovered post-election.

We are taking a cautious approach to consumer cyclicals as a result - reducing those which have done well in recent months - or where we see risk of near term disappointment. We retain exposure, but only in those where we see an overly negative outlook already factored into valuations.

There are two broad views of the current environment. One states that data signals a continuing slowdown in the global economy, which will lead to recession. The other is that we are likely to see a policy response, which will help support both the economy and also the equity market. We subscribe to the latter.

Domestically we are seeing a version of this debate play out. The Coalition Federal government has set its stall out on maintaining a fiscal surplus - whereas arguably this is the one year where we need fiscal stimulus, given moribund growth and diminishing utility of monetary policy. The means are there, in the form of the windfall of iron ore royalties, as well as government borrowing costs at less than 1%. What's more, any more pressure on depositors – seeing term deposit rates likely going to 1.3% - is likely to prompt a political backlash. So the debate will be whether logic prevails over political heel-digging.

The outlook for the banking sector remains muted. Lower rates are good for sentiment and will help keep bad debts at low levels, but they will also ultimately crimp margins. Hedging programmes mean this effect will be delayed, but any further cuts are likely to mean further pressure on margins over the next three years. That said, dividends remain reasonable and supported for the time being - which should help support bank stocks in the current low yield environment.

The resource sector has seen a sudden drop in iron ore prices - although they remain above consensus expectations and the sector remains enormously cash generative. The iron ore miners have done well and we have been scaling back our position in recent months. Iron ore prices are retreating from their highs due to two reasons. First, Brazil's Vale is restarting some shuttered production. Second, there are increased concerns over global growth and Chinese demand. On the first issue, Vale has only managed to restart around one third of the production it took off line - and this will take between six and nine months to feed through to the system. On the second, we remain mindful that China can quickly pull the stimulus lever in response to subdued demand - as we saw in 2016. As a result, we do not believe it is time yet to go aggressively underweight the resource sector.

The overall market's valuation looks reasonable, at just under 16x next-12-month earnings, and should retain a degree of support from low yields in alternative asset classes.

Pendal Smaller Companies Fund

Market review

The S&P/ASX Small Ordinaries Accumulation index finished July +4.5% higher, with Utilities (-1.3%) and Communication Services (-3.0%) being the only GICS sectors that finished the month in the red. Nevertheless, the headline index outperformed its larger cap counterpart, the S&P/ASX 100 Accumulation index by +1.7%. It was largely attributed to the strong performance posted by Small Resources (+7.9%): gold miners helped lift the sector, as the ongoing decline in long-term bond yields, coupled with elevated geopolitical uncertainties has seen the gold price continue its recent strong run.

Within Communication Services, Speedcast International (SDA, -45.8%) was the largest performance detractor. The communication network service provider downgraded its FY19 EBITDA guidance from the previous US$160-171m to US$140m-150m; and it is skewed more towards the 2H given management expects US$60-64m to come from the first half. In particular, Globecomm underlying EBITDA is expected to be approximately US$21m in full year 2019, which is US$5 million lower than previously expected; whereas lower organic growth accounts for the rest of the lower guidance. Similarly, connectivity service provider Superloop (SLC, -36.4%) also fell on the back of downgraded guidance. FY19 EBITDA is now expected to come in the range of $7-8m, compared to the $13-18m previously communicated, as the company has not completed negotiations to secure a significant commercial agreement that was included in the previous guidance. Management did note that negotiations with parties will continue, and if successfully concluded will be reflected in future earnings.

Offsetting some of these losses within the sector, oOh media (OML) rose by +14.6% in July. While the company itself did not provide any update over the month, there was some positive read-through from the industry data: the Outdoor Media Association (OMA) announced that out-of-home advertising revenue in Australia was +5.2% higher for the June quarter, compared to same quarter last year. This was despite the strong comps from June last year (+14.2%); and the impact from both the NSW and the Federal elections recently. Elsewhere, WPP AUNZ (WPP, +35.4%) also outperformed strongly. WPP plc, WPP AUNZ's majority shareholder, has entered into an agreement to sell 60% of Kantar, its global data, research, consulting and analytics business, to Bain Capital. The company also confirmed it is in advanced discussions with WPP plc to sell 100% of its Kantar business in Australia and New Zealand. If a transaction is finalised WPP expects net proceeds after transaction costs and completion adjustments to be in the order of $150 million.

Turning to the sectors in the black, Materials (+7.5), Information Technology (+6.9%) and Consumer Staples (+5.5%) led the gainers in absolute return terms. As mentioned, gold miners including St Barbara (SBM, +25.9%), Saracen Mineral (SAR, +13.9%), Resolute Mining (RSG, +33.0%) and Independence Group (IGO, +14.0%) all recorded strong gains in July. In contrast, Adelaide Brighton (ABC, -12.4%) downgraded its full year guidance. In doing so it confirmed a trend first flagged by CIMIC that the pipeline of infrastructure work has proved slower than expected. Several of the domestic construction-related names have had bounces post-election. However there are signs now that the underlying environment has not improved.

Lastly in Consumer Staples, Metcash (MTS, +12.5%) rose on the back of improved sentiment, as the proposed demerger from Woolworths of its hospitality group provided a positive read-through for MTS. Metcash runs three lines of businesses: Food, Liquor and Hardware and is currently trading at ~7x EV/EBITDA. While it is not a perfect like-for-like comparison, the implied multiple of Bunnings from Coles; and that of Endeavour Group from WOW help to provide some benchmark pricing for Metcash's Hardware and Liquor businesses. As such, it suggests that Metcash's Food business, which has been operating in a challenging environment is clearly undervalued at 5x EV/EBITDA.

Portfolio performance

The Pendal Smaller Companies Fund returned 4.63% (post-fee, pre-tax) in July, outperforming the S&P/ASX Small Ordinaries Accumulation Index by 0.12%.

Contributors

Overweight Elders

Elders (ELD) provides financial and real estate services to the agricultural sector. It gained +20.2% for the month, surging on the news of a takeover offer for Australian Independent Rural Retailers (AIRR). The scrip and cash deal, which has approved by AIRR's board, provides exposure to the wholesale rural merchandise market. AIRR's wholesale network includes eight warehouses, 1500 customers and 240 independent member stores. It also has a network of stores focused on merchandise for pets. Management expect the deal – which is still subject to ACCC approval – to deliver material synergies over the next two years.

Overweight AUB Group.

Insurance brokers AUB (AUB) – previously known as Austbrokers – was up 14.0% for the month. The market responded well to a management update which announced that an investigation into the financial impact of misconduct at its Canberra subsidiary had been completed. The expected impact on FY19 NPAT, including remediation costs, was also revealed to be $4.6m. At the same time management reaffirmed their previous guidance for FY19 NPAT of $45.9m to $46.8m, which represents between 3% and 5% growth over 2018.

Detractors

Underweight Wisetech

Further signals from central banks that low rates are likely to persist saw the bond-sensitives continue to outperform, including the growth stocks such as small cap tech stock Wisetech (WTC). We do not own WTC, which dragged on performance. This is in part a preference for other small cap technology stocks – such as Technology One (TNE) – where we have more confidence that valuations more adequately reflect both the potential upside as well as the risks. In WTC's case, we do have some reservations that valuations do not reflect the risks in WTC's strategy of expanding beyond its successful core product into other adjacent offerings.

Underweight St Barbara

The expectation of a weaker US dollar – in the wake of looser US monetary policy – coupled with elevated geopolitical uncertainties has seen the gold price continue its recent strong run. The underweight in gold miner Santa Barbara (SBM) dragged, however this was offset to an extent by outperformance from our position in Independence Group, our preferred gold exposure.

Outlook

The portfolio delivered strong absolute gains in July, outperforming the S&P/ASX Small Ordinaries index. There was a diverse mix of contributors to performance. Agricultural services company, Elders (ELD), insurance brokers AUB Group (AUB), shipbuilder Austal (ASB), consumer appliances maker Breville Group (BRG) and New Zealand-listed Ryman Healthcare (RYM) were among the Fund's best performers for the month.

There are several key themes at play within the current environment for small caps. The first is clear signs of weakness in the domestic economy. Falling house prices and tighter credit have driven weaker consumer demand across a number of sectors, which is showing up in new car

sales, general retail and media. This is likely to be reflected in August's reporting season and potentially in cautious outlook statements from management.

There is scope for stimulus to offset this weakness, with the Federal government talking of fiscal measures to augment the effects of interest rate and tax cuts. However, this effect is not likely to come through until later in the year.

Where we have exposure to the domestic consumer, it tends to be in more defensive areas such as Bapcor (BAP), with a focus on supportive industry structures and strong free cash flow generation.

The second key trend is a weaker Australian dollar. This has crimped margins for some importers, however is providing a steady tailwind to offshore earners. This provides support to Australian businesses targeting particular global niches such as portfolio holdings Breville Group (BRG), IDP Education (IEL), Nanosonics (NAN) and Credit Corp (CCP). A weaker AUD also helps resource-related companies. Resource earnings; EV materials, mining services

The third trend is the expectation of low interest rates, which is fuelling a valuation re-rating in some long dated growth businesses. The ability to sift through the growth parts of the small cap market and identify companies with a reasonable valuation – and avoid those with more speculative ratings – is the key challenge for small cap investors in today's market. Several of the higher profile growth companies in the Australian tech sector – such as Xero (XRO), Afterpay Touch (APT), and Altium (ALU) have grown out of the small cap index and are now in the ASX 100. However, we continue to like companies such as Technology One (TNE) and Nanosonics (NAN).

International Shares

Pendal Concentrated Global Share Fund

Market review

The major equity markets delivered mixed returns in July, with investors again preoccupied by macro developments around US-China trade which intensified over the course of the month, Meanwhile the UK installed a new Prime Minister but markets are none the wiser as to what form (if any) BREXIT will take. Anticipation of a rate cut in the US clearly helped to propel some markets higher during the month. The eventual 25 basis points (bp) cut delivered on the last day of July was accompanied by commentary indicating the move was not the start of a longer term easing cycle, which disappointed the market.

The US equity market saw investors largely focused on the latest quarterly reporting season, with particular interest in company outlook statements. As at the close of the month about 80% of the S&P500 had reported quarterly earnings, with approximately 70% of those companies beating consensus earnings (EPS) estimates by an average of 5%. However, average earnings growth for the quarter slowed to an average of 1.3%, and earnings estimates have fallen across most sectors in both the third and fourth quarters. Record highs in the US share market during the month belie the more muted commentary on the outlook for the year ahead from many corporates. At the month's close, the S&P500 registered a gain of 1.3%, while the NASDAQ rose by 2.1%.

European markets were also mixed in July, with investors moving to a risk-off stance amid continued uncertainty over the US-China trade dispute, the UK's change in leadership and its implications for an increasingly likely 'hard' Brexit, and expectations of renewed monetary easing as economic growth indicators remain weak. The latest quarterly growth reading for the Eurozone came in at 0.2%, half of the growth in the first quarter. The latest ECB press conference all but confirmed a return to quantitative easing later this year and a possible interest rate cut in September. In terms of market performance, the region's benchmark Euro Stoxx Index gained

0.2%, with gains in the UK (+2.2%), Italy (+0.8%) and Switzerland (+0.2%) contrasted with falls in Spain (-2.5%), Germany (-1.7%) and France (-0.4%).

Most major Asian equity markets declined on the continuing lack of confidence emanating from the trade issue. Social unrest in Hong Kong also diminished confidence in this market, considering the broader implications for the China relationship. Hong Kong's stock exchange lost 2.7% in value for the month, but was surpassed by Korea's 3.9% loss. Korea declined as a number of factors impacted confidence, including the Bank of Korea's surprise interest rate cut and lowering of its full year economic growth outlook, missile launches in North Korea, and a ramping up of regional trade frictions after Japan announced that it would tighten rules on exports to Korea of key materials used in the production of semiconductors. India (-4.9%) also experienced a sell-off as markets became concerned over a proposed increase in taxes for foreign investors. Elsewhere, Japan (+1.2%), Taiwan (+0.9%) and Indonesia (+0.5%) bucked the trend.

The Australian dollar weakened by 2.5% against the US dollar at the end of the month as the US lowered interest rates. The local unit also fell against the yen (-1.7%) but rose 1.8% against the British pound. Commodity markets were relatively uneventful, although the Australian trade weighted index fell 1%, weighed down by weaker iron ore prices.

Portfolio performance

The Pendal Concentrated Global Share Fund returned 1.68% (post fee, pre-tax) in July, underperforming its benchmark by 0.63%.

The end of July marks the three year anniversary of the Fund. Over three years the Fund has returned 14.43%pa outperforming its benchmark (after fees) by 0.30%.

ABI brews great products and a strong result

The Fund's outperformers this month include Anheuser-Busch InBev (ABI, +17%). ABI is the world's largest brewer, accounting for 30% of global volumes and 50% of the global industry profit pool. Following its US$107b acquisition of SAB Miller in 2016, ABI has increased its exposure to emerging markets from 55% to 60% and management have continued to pursue a strategy of 'premiumisation' in order to drive margin expansion in new and existing markets.

This strategy appears to be paying off. Second quarter results beat consensus estimates, with earnings (EBITDA) growth of 9.4% driven by the best volume growth in five years, pricing growth of 3.8% and 1% margin expansion.

As a result of the US$107b merger with SAB Miller in 2016, ABI's net debt/EBITDA ratio peaked at 6.6x. Since this time, management have focused on reducing debt, with a year-end debt-equity ratio target of 4x.

We believe the strong operating results, coupled with the announced intention to sell the company's lower margin Australian business - Carlton United Breweries - to Asahi for A$11.3b, will see ABI reduce debt by year end to a level beyond current guidance and consensus expectations.

We believe the stabilisation of earnings trends, the return to top-line growth and the reduction in debt will continue to drive a re-rating of the share price.

Google proves its earnings power

Another outperformer for the Fund this month was our holding in Alphabet (Google), which rose by 12.5% in the month. First-quarter results were interpreted by the market as signalling a longer term slow-down of growth in the core advertising business. However, second-quarter results appear to have dispelled those fears. The quarterly numbers exceeded market expectation, and more importantly from the market's perspective, Google website growth (adjusted for currency and hedging) accelerated to 20.5%, driven by mobile search and YouTube. YouTube is now the second-largest driver of revenue growth across the group.

Management cite ongoing product innovation, in part from the benefits of applying artificial intelligence (AI) as a key driver of their success. AI innovation applies to both the user and advertiser experience, and applies to functions within the core business as well as its 'other bets' collection of businesses. Google Cloud reached an annual revenue run rate of US$8b and continues to grow at a "significant pace", being the third-largest revenue driver for the broader business.

We continue to believe the market is underestimating not only the strength of the core digital advertising business, but the longer term revenue opportunities driven by other businesses such as YouTube, Google Cloud, and Maps.

Putting Boeing's grounding in perspective

We have written extensively about our holding in Boeing over the past few months. This month the share price declined by 6.3%. The company announced a US$5.6b write-down to earning for the next quarter related to the grounding of the 737 MAX. The inventory build-up resulting from the grounding has unsurprisingly led to lower operating cash flow and negative free cash flow for the quarter. Putting aside the 737 grounding, the rest of the business performed well, with 787 margins continuing to improve, the services business recording double-digit gains and the defence business benefitting from higher volumes.

However, we would expect the shares to underperform until there is clarity on the timing for returning the MAX 737 to service. Boeing have reiterated their timeline for an October 2019 return to service, although this is subject to receiving approvals by regulators and hence, the schedule is marred by uncertainty. We acknowledge the risks associated with further delays, but as long term investors we view the current issues as transitory. Over the longer term the strong fundamentals for airline travel and the duopoly nature of the business underpin the strong future cash flow potential of the company. Considering these supportive factors we remain committed to our investment.

Strategy and outlook

The Fund's cash weighting of about 6% continues to reflect some concern that there is a disconnection between current valuations for some companies and the earnings trajectory implied by consensus estimates. We believe the Fund is positioned to outperform over the longer term.

Markets reached new highs this month in spite of mixed economic data and uncertain macro conditions. On the last day of the month the US Federal Reserve cut interest rates for the first time since December 2008. We continue to hold the view that near term earnings expectations appear optimistic.

We believe the Fund is positioned to outperform over the longer term.

We expect volatility to increase and our current cash position continues to reflect some concern that second-half earnings growth expectations for a number of companies appears optimistic. Our focus remains 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 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 owning a concentrated portfolio of businesses, rather than having indiscriminate broader market exposure is the best way to optimise investment performance.

Pendal Core Global Share Fund

(managed by AQR Capital Management)

Market review

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European markets were also mixed in July, with investors moving to a risk-off stance amid continued uncertainty over the US-China trade dispute, the UK's change in leadership and its implications for an increasingly likely 'hard' Brexit, and expectations of renewed monetary easing as economic growth indicators remain weak. The latest quarterly growth reading for the Eurozone came in at 0.2%, half of the growth in the first quarter. The latest ECB press conference all but confirmed a return to quantitative easing later this year and a possible interest rate cut in September. In terms of market performance, the region's benchmark Euro Stoxx Index gained 0.2%, with gains in the UK (+2.2%), Italy (+0.8%) and Switzerland (+0.2%) contrasted with falls in Spain (-2.5%), Germany (-1.7%) and France (-0.4%).

Most major Asian equity markets declined on the continuing lack of confidence emanating from the trade issue. Social unrest in Hong Kong also diminished confidence in this market, considering the broader implications for the China relationship. Hong Kong's stock exchange lost 2.7% in value for the month, but was surpassed by Korea's 3.9% loss. Korea declined as a number of factors impacted confidence, including the Bank of Korea's surprise interest rate cut and lowering of its full year economic growth outlook, missile launches in North Korea, and a ramping up of regional trade frictions after Japan announced that it would tighten rules on exports to Korea of key materials used in the production of semiconductors. India (-4.9%) also experienced a sell-off as markets became concerned over a proposed increase in taxes for foreign investors. Elsewhere, Japan (+1.2%), Taiwan (+0.9%) and Indonesia (+0.5%) bucked the trend.

The Australian dollar weakened by 2.5% against the US dollar at the end of the month as the US lowered interest rates. The local unit also fell against the yen (-1.7%) but rose 1.8% against the British pound. Commodity markets were relatively uneventful, although the Australian trade weighted index fell 1%, weighed down by weaker iron ore prices.

Portfolio performance

The Pendal Core Global Share Fund returned 1.90% (post-fee, pre-tax) in July, underperforming its benchmark by 0.41%.

The Fund underperformed its benchmark over July 2019, with underperformance in Europe and developed Asia, while North America produced mild offsetting outperformance of its regional benchmark.

Thematically, weakness in Quality, across all regions, and Value in developed Asia and Europe were primarily responsible for overall underperformance over the month. In Europe, Momentum and Value drove underperformance, although all signals experienced negative returns for the month. In developed Asia, the underperformance was due to negative returns in Quality and Value outweighing strength in Momentum signals. In North America, Sentiment drove outperformance, offset somewhat by negative returns in Quality themes.

From a stock and industry attribution perspective, intra-industry stock selection drove underperformance, while industry tilts produced offsetting positive active returns over the month. Stock selection within industries was weakest within Industrials & Health Care, which outweighed the outperformance of active positioning within Consumer Discretionary. At a sector level, the overweight in Information Technology and underweight in Energy were the notable positive contributors, while an overweight in Health Care was the largest negative offset.

At a stock level, the largest detractors from active returns over the month came from: an overweight position in Pfizer Inc., an American multinational pharmaceutical corporation headquartered in New York City; an overweight position in Exelon Corporation, an American energy company headquartered in Chicago, Illinois; an underweight position in JP Morgan Chase & Co., an American multinational investment bank and financial services company headquartered in New York City; an underweight position in Bank of America Corporation, an American multinational investment bank; and an overweight position in Sandvik AB, a Swedish high-technology engineering company in tools and tooling systems. The largest positive contributors to active returns came from overweight positions in: Applied Industrial Technologies a US based company focused on the distribution of bearings, power transmission products and other industrial supplies; Synchrony Financial, a consumer financial services company headquartered in Connecticut, United States; Philip Morris International Inc., an American multinational cigarette and tobacco manufacturing company; Intuit Inc., an American business and financial software company that develops and sells financial, accounting, and tax preparation software; and Discover Financial Services, Inc., an American financial services company that owns and operates Discover Bank.

Strategy and outlook

Entering August, the largest sector tilts are overweights in Information Technology and Health Care and underweight positions in Financials and Energy.

Australian Fixed Income

Pendal Fixed Interest Fund

Market review

It was another strong month for the local bond market as yields continued their slide. This was driven in part by the RBA's second consecutive rate cut as well as growing expectations of further easing by major central banks. The labour market data during the month revealed the unemployment rate remained static at 5.2% with a meagre 0.5K jobs added over the period. Second quarter CPI was also soft with the RBA's preferred gauge, the trimmed mean, rising 0.4% over the quarter and 1.6% year-on-year. Leading indicators were also weak with the NAB Business Confidence figure dropping back to +2 from its bounce to +7 in the prior month. Consumer

confidence also dropped with a slide back below 100, the level separating optimism and pessimism. Similarly, retail sales rose by an anaemic 0.1% month-on-month.

Turning to market movements, the Australian 3 and 10 year yields fell by 15bp and 13bp to 0.80% and 1.20% respectively. At the very front-end, 90 day BBSW dropped by a larger 20bp to 1.01% in response to the RBA cut.

Portfolio performance

The Pendal Fixed Interest Fund returned 1.10% in July (post-fees, pre-tax), outperforming its benchmark by 0.15%.

The Fund outperformed its benchmark during July, which was driven by the alpha overlay. The Duration strategy was again the largest contributor from long duration exposures that continued to benefit from the large fall in yields. This included positions in Australia and New Zealand, while US exposures were a small detractor. The Yield Curve strategy also added value from an Australian front-end curve flattener. Finally, the credit and government components both outperformed their benchmarks.

Strategy and outlook

After back-to-back cuts in June and July, the Reserve Bank left the cash rate unchanged at its meeting in early August. In their accompanying statement they referred to monitoring developments in the labour market closely and that they will ease monetary policy further if needed to support growth and achieve the inflation target over time. They do expect an extended period of low interest rates.

Our outlook remains consistent with prior months. Central banks globally have become more dovish, weighed down by slowing global trade and falling inflation expectations. The Reserve Bank's adjustment to monetary policy has to-date been in response to domestic factors.

The Reserve Bank sees the non-accelerating inflation rate of unemployment (NAIRU) as being 4.5%, well-below the current unemployment rate of 5.2%. A further increase in the unemployment rate would most likely be met with further policy easing. A deteriorating external environment would only add to the case for further monetary policy accommodation. The risks to global growth are clearly tilted towards growth disappointing. We expect further policy easing, most likely occurring in the fourth quarter.

International Fixed Income

Pendal Global Fixed Interest Fund

Market review

Global bond yields experienced a mixed month as three month US yields fell while the 10 year rate rose slightly. Moves at the very front-end were driven by a 25bp cut by the Federal Reserve, its first reduction in more than a decade. Further, the FOMC announced it would halt its quantitative tightening at the start of August. Data for the world's largest economy was mixed overall. The advance second quarter GDP reading revealed slower growth of only 2.1% annualised and core inflation of 1.8%. Similarly, the ISM Manufacturing gauge dropped from 52.1 to 51.7. However, at the same time retail sales, durable goods orders and the monthly payrolls report were more constructive and beat expectations. Elsewhere, ECB President Mario Draghi delivered a dovish post-meeting press conference during July. The prospect of new stimulus, including deeper

negative interest rates, was raised in response to a sluggish economy (particularly evident in manufacturing) and persistent subdued inflation. Beyond monetary policy developments, trade war worries were less prevalent than previous months. A gathering of US and China trade officials was held in Shanghai during the month with little major progress. Finally on market movements, the US 2 and 10 year yields rose 12bp and 1bp to 1.87% and 2.02%.

Portfolio performance

The Pendal Global Fixed Interest Fund returned 0.78% in July (post-fees, pre-tax), outperforming its benchmark by 0.10%.

Over the month, the Duration strategy was the strongest performer while FX and Yield Curve strategies also contributed positively. The Cross-Market and Macro strategies were roughly flat. The portfolio risk level started at 3 risk units and stayed at a low level before ending the month at 4 risk units.

The Duration strategy was the largest contributor over the month. We maintained long duration positions in various markets through the month. The main contributors of the gains were long duration positions in the front end of the Australian, New Zealand and European curves. Positions in the US front end were down-sized earlier in the month. In Emerging Markets, we continued to hold the long positions in China and Korea, with the latter making significant profits over the month. In the middle of the month we initiated a long duration position in Singaporean front end with flat performance for the month.

The FX strategy added to performance over the month. For most of the month we held long USD short Emerging Market currencies. All positions contributed positively to the portfolio. The short position in SGD were closed earlier in the month, and short positions in KRW and TWD were closed towards month-end. As of the end of the month we held no FX positions.

The Yield Curve strategy contributed positively to the portfolio this month. All gains were from the flattening position in the front end of the Australian curve, which we continue to hold.

In the Macro strategy we added a modest sell protection position in iTraxx Australian with the expectation of tightening credit spread in the near future. The position were roughly flat in performance.

In the Cross-Market strategy we added a trade from our quantitative process at the end of the month.

There were no trades in Relative Value in the month.

Strategy and outlook

Accompanying the Fed's first rate cut in over a decade there was a message that it was an insurance measure amid a mid-cycle environment. The lucky thing for Chairman Powell is that outside of manufacturing, the US economy is healthy enough to buy the FOMC some time. However, it is unpredictable when weakness in manufacturing tips over to the rest of the economy (even one as consumption-driven as the US) and the tightness in labour markets suddenly reverses. At the same time Chinese tax cuts and talks of monetary reform to-date resemble something akin to moving the deck chairs around on the Titanic, whilst the trajectory of real economic activity continues to sink ever lower. The upshot of all of this for our positioning is that our long duration bias remains, but in more measured size as risk-reward has moved into more balanced territory for the near term. However, the forward-looking indicators remain sufficiently weak that we would welcome any meaningful sell off in yields to re-engage with the same themes at better prices.

Credit

Pendal Enhanced Credit Fund

Market review

Australian credit generated another positive return in July, driven by the continued fall in yields and healthy accruals. The drop in yields was alongside the second consecutive RBA cut and growing expectations of further easing by global central banks.

Turning to issuance, July represented the largest volumes for calendar year 2019 thus far. Financials drove the bulk of new deals during the month as ANZ and a string of offshore issuers tapped the market. ANZ issued A$1.75bn, Macquarie raised A$1.35bn, TD bank did A$1.25bn while a number of others were above the A$500m mark. In contrast, deals from non-financials were relatively light and included Ausnet (A$350m) and GPT (A$200m).

The Australian iTraxx index (Series 31 contract) traded in a tight 7.5bp range finishing the month 4.5bp tighter to +59ps. Physical credit spreads had a constructive month with most sectors performing strongly. The best performing sectors were domestic banks, real estate and telcos tightening 14, 9 and 9bp respectively. The worst performing sector was supranationals which widened 1bp. Semi-government bonds performed well tightening 3bp to government bonds.

Portfolio performance

The Pendal Enhanced Credit Fund returned 0.98% in July (post-fees, pre-tax), outperforming the benchmark return by 0.06%.

A fall in underlying rates and accruals made a positive contribution. Positions in infrastructure and utilities, where the Fund is overweight, were middle of the pack relative to other Australian credit sectors. Portfolio purchases over the period included issuance from BNP Paribas and utilities provider SA Power Networks.

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 and Q2 reporting seasons. 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, volatility has quickly spiked then evaporated over the past year. Elevated levels during 2018 (particularly December), subsided in January and were relatively subdued until the flare-up in early August. This has been alongside shifting perspectives towards the trade war and 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 battles.

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

It was another strong month for the local bond market as yields continued their slide. This was driven in part by the RBA's second consecutive rate cut as well as growing expectations of further easing by major central banks. The Reserve Bank's decision was supported by the persistent slack in the labour market, which was flagged after the Board's estimated full employment rate was revised lower from 5% to 4.5%. However, messaging from Governor Lowe suggested further rate reductions would be on pause over the next several months in order to allow the impact of previous action to be assessed.

The labour market data during the month revealed the unemployment rate remained static at 5.2% with a meagre 0.5K jobs added over the period. Second quarter CPI was also soft with the RBA's preferred gauge, the trimmed mean, rising 0.4% over the quarter and 1.6% year-on-year. Leading indicators were also weak with the NAB Business Confidence figure dropping back to +2 from its bounce to +7 in the prior month. Consumer confidence also dropped with a slide back below 100, the level separating optimism and pessimism. Similarly, Retail Sales rose by an anaemic 0.1% month-on-month.

In the US, the Fed also cut its key policy rate by 25bp during the month, its first reduction in more than a decade. Further, the FOMC announced it would halt its quantitative tightening at the start of August. Data for the world's largest economy was mixed overall. The advance second quarter GDP reading revealed slower growth of only 2.1% annualised and core inflation of 1.8%. Similarly, the ISM Manufacturing gauge dropped from 52.1 to 51.7. However, at the same time retail sales, durable goods orders and the monthly payrolls report were more constructive and beat expectations.

Elsewhere, ECB President Mario Draghi delivered a dovish post-meeting press conference during July. The prospect of new stimulus, including deeper negative interest rates, was raised in response to a sluggish economy (particularly evident in manufacturing) and persistent subdued inflation.

Beyond monetary policy developments, trade war worries were less prevalent than previous months. A gathering of US and China trade officials was held in Shanghai during the month with little major progress.

Turning to market movements, the Australian 3 and 10 year yields fell by 15bp and 13bp to 0.80% and 1.20% respectively. At the very front-end, 90 day BBSW dropped by a larger 20bp to 1.01% in response to the RBA cut. In contrast, the US 2 and 10 year yields rose 12bp and 1bp to 1.87% and 2.02%, despite the rate reduction by the Federal Reserve. In turn, the AU-US interest rate differential fell deeper into negative territory, which dragged on the Australian Dollar versus its US counterpart.

In credit markets, Australian spreads continued to tighten in July alongside expectations of further easing from major central banks. At the same time, trade war developments were of less concern to investors with few major updates over the month.

Australian physical credit spreads had a strong month after the announcement by APRA that the Australian major banks will need to increase their capital buffer through tier 2 sub-debt issuance. This surprised the market, which was expecting tier 3 senior non-preferred issuance to fill the capital buffer requirement. A strong rally in major bank senior preferred securities followed as near term new issuance by the major banks will primarily be tier 2 supply, whilst senior issuance will be scarce. The perceived scarcity factor saw strong demand for major bank senior paper. The second order effect of this saw other sectors perform as investors looked for relative value opportunities in those areas.

The Australian iTraxx index (Series 31 contract) traded in a tight 7.5bp range finishing the month 4.5bp tighter to +59ps. Physical credit spreads had a constructive month with most sectors performing strongly. The best performing sectors were domestic banks, real estate and telcos tightening 14, 9 & 9bp respectively. The worst performing sector was supranationals which widened 1bp. Semi-government bonds performed well tightening 3bp to government bonds.

Portfolio performance

Managed Cash

The Pendal Managed Cash Fund returned 0.12% in July (post-fees, pre-tax), matching the benchmark return.

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 65 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 Pendal Enhanced Cash Fund returned 0.28% in July (post-fees, pre-tax) outperforming the benchmark by 0.16%.

Positive performance came primarily from financials and industrials sectors. Activity during the month included investing in three new primary market deals, all from the financials sector. These were funded out of cash.

As at the end of the month, the portfolio had a credit spread of 56bp over bank bills, interest rate duration of 0.13 years and credit spread duration of 1.54 years.

Strategy and outlook

After back-to-back cuts in June and July, the Reserve Bank left the cash rate unchanged at its meeting in early August. In their accompanying statement they referred to monitoring developments in the labour market closely and that they will ease monetary policy further if needed

to support growth and achieve the inflation target over time. They do expect an extended period of low interest rates.

Our outlook remains consistent with prior months. Central banks globally have become more dovish, weighed down by slowing global trade and falling inflation expectations. The Reserve Bank's adjustment to monetary policy has to-date been in response to domestic factors.

The Reserve Bank sees the non-accelerating inflation rate of unemployment (NAIRU) as being 4.5%, well-below the current unemployment rate of 5.2%. A further increase in the unemployment rate would most likely be met with further policy easing. A deteriorating external environment would only add to the case for further monetary policy accommodation. The risks to global growth are clearly tilted towards growth disappointing. We expect further policy easing, most likely occurring in the fourth quarter.

Australian Property

Pendal Property Securities Fund

Market review

The ASX 300 AREIT index was up 2.6% in July, underperforming the broader market by 40bp. On a rolling 12 month basis, AREITS are +21.4%, outperforming the broader market by 8.1%. Globally REITs were up 0.2% for the month, with year rolling performance up 9.9%. Australian REITs have been the best performing market, followed by the US (+17.7%) with the laggard being Europe (-10.4%).

The best performing AREITs in July were Stockland (+9.6%) following the sale of 50% of its Aura residential development project on the Sunshine Coast at a 30% premium to book value and Vicinity Centres (+6.5%) following substantial underperformance over the last few years. The worst performers for the month were National Storage REIT (-6.3%) with concerns about occupancy levels, particularly given the low level of residential turnover Australia wide as well as Goodman Group (-1.5%), unwinding a very small portion of substantial outperformance in 1H19. REITs were driven by the 10 year bond yield falling 19bp to an all-time low of 1.18% and a 25bp cash rate cut with the cash rate now at 1%.

During the month Abacus raised $250m in equity with the proceeds to be used to fund its bid for Australian Unity Office Fund (jointly with Charter Hall), self-storage opportunities and a Sydney CBD office asset. Year to date the REITs have raised a total of $4.1b in equity. Also during the month Charter Hall and its managed unlisted funds acquired 242 Exhibition St, Melbourne for $830m, representing a 4.6% yield. The property is leased to Telstra with a weighted average expiry of 12 years.

Macro data continues to disappoint with weak global PMI's, particularly in manufacturing (now in contraction mode). The S&P500 finished the month broadly flat, however bond markets were well supported during the period with Bunds finishing the month at -0.44bp and UST at 2.01%. In Australia the unemployment rate remained steady at 5.2%, however business confidence gave back most of its post-election bounce and retail sales were sluggish +0.1%, validating the RBA's rate cut.

Portfolio performance

The Pendal Property Securities Fund returned 2.14% in July (post-fee, pre-tax), underperforming its benchmark by 0.47%.

The portfolio underperformed for the month. Positive attribution came from underweight positions in National Storage REIT and Abacus Property Group and overweight positions in Charter Hall Group, Centuria Industrial REIT and Charter Hall Long WALE. Underweight positions in Vicinity Centres and Stockland Trust Group and overweight positions in Japara Healthcare, Precinct Properties and Goodman Group detracted from performance.

Over the month we participated in the Abacus equity raising, reducing our underweight. We also reduced our underweight in Stockland and increased our overweight in Centuria Industrial Trust. Funding was sourced from increasing our underweight in Dexus Property Group and cash.

Strategy and outlook

The AREIT sector is now priced on an FY20 dividend yield of 4.6%, a PE ratio of 18.7 times and a 45% premium to NTA, well above its long-term average of 17%. Cap rates are unlikely to compress much 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

Pendal 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 continued to climb in July, posting a total return of 0.4%. North America (up 1.5%) was the only positive performing region during the month while Europe (down 1.5%) and Asia Pacific (down 1.2%) underperformed. Within the Asia Pacific region, results were mixed. Hong Kong (down 5.3%) was the weakest performer, followed by Singapore (down 1.4%) and New Zealand (down 0.5%), while Japan (up 1.6%) outperformed. In Europe, results were similarly mixed across the region. The Netherlands (down 6.5%) posted the largest decline, followed by the United Kingdom (down 6.4%) and Norway (down 4.7%). Conversely, Israel (up 5.5%), Sweden (up 3.3%), and Belgium (up 1.9%) were notable positive performers. In North America, the U.S. and Canada returned 1.6% and 0.9%, respectively.

Portfolio performance

The Pendal Global Property Securities Fund returned 0.94% in July (post-fee, pre-tax), outperforming the benchmark by 0.01%.

North America

The North America portfolio returned 1.29% in July before fees and withholding taxes, trailing the FTSE EPRA Nareit North America Index by 26 basis points. Underperformance relative to the benchmark was driven by negative stock selection results, while sector allocation results were largely neutral. In terms of stock selection, results were weakest in the office, triple net lease, and storage sectors and were strongest in the industrial, regional mall, and apartment sectors. Among the portfolio's holdings, top individual contributors to relative performance included overweight positions in outperforming Duke Realty (DRE) and Howard Hughes (HHC), and a lack of exposure to underperforming Ventas (VTR). Detractors most notably included an overweight position in

underperforming Host Hotels & Resorts (HST) and a lack of exposure to outperforming W.P. Carey (WPC) and Equity Residential (EQR).

Europe

The European portfolio returned -0.13% in July before fees and withholding taxes, outperforming the regional EPRA benchmark by 143 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 United Kingdom, France, and Netherlands and were weakest in Ireland, Spain, and Austria. Regarding country allocation, negative results were attributable to the portfolio's lack of exposure to the outperforming Switzerland and Belgium. Among the portfolio's holdings, top contributors to relative performance included overweight positions in outperforming Gecina SA (France), Vonovia SE (Germany), and Fabege AB (Sweden). Detractors most notably included a lack of exposure to outperforming Castellum AB (Sweden) and Aedifica SA (Belgium), and an overweight position in underperforming Grainger PLC (United Kingdom).

Asia

The Asia portfolio returned -0.92% in July before fees and withholding taxes, exceeding the regional EPRA benchmark by 30 basis points. Outperformance relative to the benchmark was driven by positive stock selection results in Japan and Singapore, which were partially offset by negative results in Hong Kong. Country allocation results were also positive and were driven by the portfolio's underweight to the underperforming Hong Kong. Among the portfolio's holdings, top contributors to relative performance included overweight positions in outperforming Invincible Investment (Japan), ORIX JREIT (Japan), and Japan Rental Housing Investments (Japan). Detractors most notably included an overweight position in underperforming New World Development (Hong Kong) and a lack of exposure to outperforming Nomura Real Estate Master Fund (Japan) and Nippon Prologis REIT (Japan).

Active Balanced

Pendal Active Balanced Fund

Markets review

Performance was strong for the Australian market in July, with the S&P/ASX 300 Accumulation index recording another 3%. While all sectors finished the month in the black, both index heavyweights Financials (-1.8%) and Materials (+1.2%) were laggards. The latter's muted performance was also in a stark contrast to the stronger iron ore price over the period (+10%).

Within Financials, bank performance remained muted: CBA (-0.6%) received several downgrades from brokers ahead of August reporting season, as it was trading at a valuation premium to its Big Four peers, which is getting harder to justify given the subdued operating environment domestically. NAB (+6.7%) was the standout from the cohort, as its appointment of the new CEO was well received by the market. Outside of the banks, AMP (AMP, -15.6%) came under pressure as management announced that the sale of its life insurance and mature business to Resolution Life is unlikely to proceed following intervention by the Reserve Bank of New Zealand (RBNZ). The RBNZ requires New Zealand-related assets to be ring-fenced, which would require a renegotiation of terms with Resolution Life. Management cancelled its interim dividend as a result.

Consumer Staples (+9.6%) led the gainers, with Woolworths (WOW, +7.2%) being the largest contributor.

The major equity markets delivered mixed returns in July, with investors again preoccupied by macro developments around US-China trade which intensified over the course of the month, Meanwhile the UK installed a new Prime Minister but markets are none the wiser as to what form (if any) BREXIT will take. Anticipation of a rate cut in the US clearly helped to propel some markets higher during the month. The eventual 25 basis points (bp) cut delivered on the last day of July was accompanied by commentary indicating the move was not the start of a longer term easing cycle, which disappointed the market.

European markets were also mixed in July, with investors moving to a risk-off stance amid continued uncertainty over the US-China trade dispute, the UK's change in leadership and its implications for an increasingly likely 'hard' Brexit, and expectations of renewed monetary easing as economic growth indicators remain weak.

The Australian dollar weakened by 2.5% against the US dollar at the end of the month as the US lowered interest rates. The local unit also fell against the yen (-1.7%) but rose 1.8% against the British pound. Commodity markets were relatively uneventful, although the Australian trade weighted index fell 1%, weighed down by weaker iron ore prices.

It was another strong month for the local bond market as yields continued their slide. This was driven in part by the RBA's second consecutive rate cut as well as growing expectations of further easing by major central banks. The labour market data during the month revealed the unemployment rate remained static at 5.2% with a meagre 0.5K jobs added over the period. Second quarter CPI was also soft with the RBA's preferred gauge, the trimmed mean, rising 0.4% over the quarter and 1.6% year-on-year. Leading indicators were also weak with the NAB Business Confidence figure dropping back to +2 from its bounce to +7 in the prior month. Consumer confidence also dropped with a slide back below 100, the level separating optimism and pessimism. Similarly, retail sales rose by an anaemic 0.1% month-on-month.

Turning to market movements, the Australian 3 and 10 year yields fell by 15bp and 13bp to 0.80% and 1.20% respectively. At the very front-end, 90 day BBSW dropped by a larger 20bp to 1.01% in response to the RBA cut.

Global bond yields experienced a mixed month as three month US yields fell while the 10 year rate rose slightly. Moves at the very front-end were driven by a 25bp cut by the Federal Reserve, its first reduction in more than a decade. Further, the FOMC announced it would halt its quantitative tightening at the start of August.

ECB President Mario Draghi delivered a dovish post-meeting press conference during July. The prospect of new stimulus, including deeper negative interest rates, was raised in response to a sluggish economy (particularly evident in manufacturing) and persistent subdued inflation. Beyond monetary policy developments, trade war worries were less prevalent than previous months. A gathering of US and China trade officials was held in Shanghai during the month with little major progress. Finally on market movements, the US 2 and 10 year yields rose 12bp and 1bp to 1.87% and 2.02%.

Portfolio performance

The Pendal Active Balanced Fund returned 1.52% (post-fee, pre-tax) for the month of July, underperforming its benchmark by 0.26%.

The Fund's return for July was driven by contributions from all asset classes, while higher returns from the Fund's exposure to Australian and offshore equity and property markets contributed the most to returns. Australian and international fixed income again generated positive returns following downward pressure on bond yields.

Performance relative to the benchmark broadly reflected the application of our active asset allocation processes. Our tactical decisions saw the Fund's overweight exposure to global equities

move to an underweight position which had a marginal impact on performance, while asset allocation across other sectors delivered a fairly neutral impact.

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 Viva Energy and Metcash detracted from performance, as did holding no exposure to Woodside Petroleum, while overweight positions in Fortescue Metals and Amcor together with holding no exposure to A2 Milk detracted from performance.

Within the global equities portfolio the Core, Concentrated and Emerging Markets strategies delivered gains, although they underperformed their benchmarks (pre fees), while the European Value strategy outperformed.

The Alternatives strategy delivered a total return (before fees) of 0.48% versus a cash return of 0.12%. Within our Alternatives core portfolio the Managed Futures, Event Driven and Dedicated Short Bias strategies generated positive returns, while the notable offsetting detractor was the Opportunistic strategy which experienced a net loss on its portfolio of deep value trades.

In relation to our tactical positioning within the Alternatives component of the Fund, holding long positions in Gold and US, German and Australian bond markets made contributions. Since the end of July we have added short positions in German equities and copper.

Strategy and outlook

The Australian market appears to have passed the initial impact of the post-election improvement in sentiment, although there are clear signals that domestic demand has not recovered since this time. Hence, a cautious approach to economically-sensitive assets is warranted.

Signals from outside of our shores add further weight to the cautious stance, considering the prospects of weaker growth from the world's main economic engines. Further monetary as well as fiscal policy responses will be required and these will have varying implications – both positive and negative – for asset markets.

Central banks globally have become more dovish, weighed down by slowing global trade and falling inflation expectations. The Reserve Bank of Australia's (RBA) adjustment to monetary policy has come in response to domestic factors, while a key focus remains on the labour market. The RBA sees the non-accelerating inflation rate of unemployment (NAIRU) as being 4.5%, well-below the current unemployment rate of 5.2%. A further increase in the unemployment rate would most likely be met with further policy easing. A deteriorating external environment would only add to the case for further monetary policy accommodation. The risks to global growth are clearly tilted towards growth disappointing.

The Fund's performance exhibits the benefit of having a well-diversified and disciplined investment strategy that can smooth returns from underlying assets which tend to be more volatile in isolation. We also structure the Fund to adequately diversify on many levels to capture opportunities for generating long term gains within a tightly controlled risk management framework.

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

We remain confident that our tried and tested investment philosophy and asset allocation processes will continue to deliver favourable investment outcomes over the long term. We continue to employ an active approach to modelling scenarios and assessing market technical factors to identify opportunities and limit risks for our investors.

Performance as at 31 July 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)	2.51	7.62	17.64	2.51	8.66	12.36	11.87	8.50	10.08
Total Return (pre-fee, pre-tax)	2.58	7.83	18.12	2.58	9.54	13.27	12.77	9.36	11.07
Benchmark	2.97	8.58	18.81	2.97	13.25	13.97	11.61	8.57	10.16
Pendal Imputation Fund									APIR - RFA0103AU
Total Return (post-fee, pre-tax)	2.07	7.16	16.86	2.07	9.14	12.15	11.27	7.46	9.69
Total Return (pre-fee, pre-tax)	2.15	7.40	17.39	2.15	10.13	13.16	12.28	8.43	10.70
Benchmark	2.97	8.58	18.81	2.97	13.25	13.97	11.61	8.57	9.07
Pendal Focus Australian Share Fund									APIR - RFA0059AU
Total Return (post-fee, pre-tax)	2.85	8.74	19.86	2.85	9.72	13.54	13.55	10.30	9.65
Total Return (pre-fee, pre-tax)	2.91	8.95	20.31	2.91	10.46	14.58	14.79	11.41	10.76
Benchmark	2.97	8.58	18.81	2.97	13.25	13.97	11.61	8.57	8.11
Pendal Ethical Share Fund									APIR - RFA0025AU
Total Return (post-fee, pre-tax)	2.60	7.38	17.73	2.60	8.67	11.87	11.60	8.75	8.77
Total Return (pre-fee, pre-tax)	2.68	7.63	18.28	2.68	9.71	12.93	12.66	9.79	9.83
Benchmark	2.97	8.58	18.81	2.97	13.25	13.97	11.61	8.57	8.51
Australian Shares - Mid Cap									
Pendal MidCap Fund									APIR - BTA0313AU
Total Return (post-fee, pre-tax)	4.39	6.32	14.40	4.39	2.08	12.20	10.61	12.25	10.28
Total Return (pre-fee, pre-tax)	4.47	6.56	14.90	4.47	3.00	13.64	11.89	13.62	12.40
Benchmark	5.00	5.63	14.97	5.00	6.79	13.38	10.45	12.12	6.36
Australian Shares - Small Cap									
Pendal Smaller Companies Fund									APIR - RFA0819AU
Total Return (post-fee, pre-tax)	4.63	3.03	12.89	4.63	2.00	11.68	7.64	9.46	12.90
Total Return (pre-fee, pre-tax)	4.74	3.35	13.59	4.74	3.27	13.08	8.99	10.83	14.20
Benchmark	4.51	4.15	15.65	4.51	7.61	14.85	9.27	9.18	7.91
Australian Shares - Micro Cap									
Pendal MicroCap Opportunities Fund									APIR - RFA0061AU
Total Return (post-fee, pre-tax)	6.34	7.36	20.18	6.34	13.82	16.16	13.63	16.87	18.12
Total Return (pre-fee, pre-tax)	6.85	8.56	21.88	6.85	16.08	17.80	16.00	20.18	23.06
Benchmark	4.51	4.15	15.65	4.51	7.61	14.85	9.27	9.18	3.79
International Shares									
Pendal Core Global Share Fund									APIR - RFA0821AU
Total Return (post-fee, pre-tax)	1.90	1.25	10.10	1.90	2.72	10.03	10.61	11.15	5.87
Total Return (pre-fee, pre-tax)	1.99	1.46	10.59	1.99	3.68	11.07	11.66	12.21	7.02
Benchmark	2.31	2.94	15.31	2.31	11.73	15.94	14.13	13.82	7.64
Pendal Global Emerging Markets Opportunities Fund - WS									APIR - BTA0419AU
Total Return (post-fee, pre-tax)	-0.93	0.60	8.44	-0.93	5.35	8.58	11.62	9.11	10.35
Total Return (pre-fee, pre-tax)	-0.80	0.95	9.18	-0.80	6.84	10.10	13.18	10.74	12.46
Benchmark	0.57	-0.61	6.25	0.57	5.51	8.74	12.01	8.13	9.94
Pendal Concentrated Global Share Fund									APIR - BTA0503AU
Total Return (post-fee, pre-tax)	1.68	1.85	11.02	1.68	9.28	15.05	14.43	N/A	14.45
Total Return (pre-fee, pre-tax)	1.78	2.13	11.62	1.78	10.40	16.28	15.72	N/A	15.74
Benchmark	2.31	2.94	15.31	2.31	11.73	15.94	14.13	N/A	14.14
Property									
Pendal Property Securities Fund									APIR - BTA0061AU
Total Return (post-fee, pre-tax)	2.14	10.20	17.80	2.14	24.84	19.32	8.60	13.76	8.34
Total Return (pre-fee, pre-tax)	2.19	10.39	18.17	2.19	25.65	20.09	9.31	14.50	9.16
Benchmark	2.61	9.35	15.33	2.61	21.34	17.85	7.49	13.30	8.09
Pendal Global Property Securities Fund									APIR - RFA0051AU
Total Return (post-fee, pre-tax)	0.94	1.24	4.40	0.94	7.71	7.12	4.38	7.54	9.16
Total Return (pre-fee, pre-tax)	1.03	1.46	4.87	1.03	8.70	8.11	5.35	8.54	10.16
Benchmark	0.93	1.23	4.17	0.93	7.08	6.58	3.99	7.53	8.85
Fixed Interest									
Pendal Fixed Interest Fund									APIR - RFA0813AU
Total Return (post-fee, pre-tax)	1.10	4.48	7.15	1.10	9.02	5.98	3.53	4.64	6.48
Total Return (pre-fee, pre-tax)	1.14	4.61	7.41	1.14	9.57	6.51	4.05	5.16	7.03
Benchmark	0.95	3.73	6.92	0.95	10.44	6.65	4.30	5.20	6.73
Pendal Global Fixed Interest Fund									APIR - RFA0032AU
Total Return (post-fee, pre-tax)	0.78	4.46	5.66	0.78	7.25	4.03	1.84	4.30	5.98
Total Return (pre-fee, pre-tax)	0.83	4.59	5.93	0.83	7.82	4.58	2.38	4.86	6.56
Benchmark	0.68	3.84	5.39	0.68	8.37	4.93	2.73	5.02	6.89
Pendal Enhanced Credit Fund									APIR - RFA0100AU
Total Return (post-fee, pre-tax)	0.98	2.96	5.73	0.98	8.27	5.61	4.44	4.78	5.82
Total Return (pre-fee, pre-tax)	1.02	3.07	5.96	1.02	8.75	6.09	4.91	5.26	6.34
Benchmark	0.86	2.85	5.56	0.86	8.24	5.64	4.43	4.85	5.93
Cash & Income									
Pendal Enhanced Cash Fund									APIR - WFS0377AU
Total Return (post-fee, pre-tax)	0.28	0.69	1.47	0.28	2.53	2.56	2.76	2.67	4.82
Total Return (pre-fee, pre-tax)	0.30	0.76	1.59	0.30	2.78	2.82	3.02	2.92	5.15
Benchmark	0.12	0.40	0.91	0.12	1.90	1.87	1.84	2.06	4.73
Pendal Managed Cash Fund									APIR - WFS0245AU
Total Return (post-fee, pre-tax)	0.12	0.43	0.90	0.12	1.88	1.84	1.84	2.04	6.27
Total Return (pre-fee, pre-tax)	0.14	0.49	1.01	0.14	2.10	2.06	2.06	2.26	6.57
Benchmark	0.12	0.40	0.91	0.12	1.90	1.87	1.84	2.06	6.34
Pendal Monthly Income Plus Fund									APIR - BTA0318AU
Total Return (post-fee, pre-tax)	1.17	3.61	6.82	1.17	7.14	6.00	4.77	4.84	5.65
Total Return (pre-fee, pre-tax)	1.23	3.78	7.17	1.23	7.84	6.69	5.45	5.53	6.32
Benchmark	0.09	0.32	0.69	0.09	1.45	1.48	1.49	1.76	2.74
Diversified									
Pendal Active Balanced Fund									APIR - RFA0815AU
Total Return (post-fee, pre-tax)	1.52	3.73	9.85	1.52	4.91	7.82	7.42	7.22	7.62
Total Return (pre-fee, pre-tax)	1.61	3.97	10.37	1.61	5.91	8.85	8.44	8.24	8.70
Benchmark	1.76	4.48	11.49	1.76	9.98	10.54	8.70	8.14	7.64

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Performance figures are calculated in accordance with the Financial Services Council (FSC) standards. Performance data (post-fee) assumes reinvestment of distributions and is calculated using exit prices, net of management costs. Performance data (pre-fee) is calculated by adding back management costs to the (post-fee) performance. Past performance is not a reliable indicator of future performance. The term 'benchmark' refers to the index or measurements used by an investment manager to assess the relative risk and the performance of an investment portfolio.

Pendal is the issuer of the following products:

Pendal Australian Share Fund ARSN 089 935 964

Pendal Smaller Companies Fund ARSN 089 939 328

Pendal Concentrated Global Share Fund ARSN 613 608 085

Pendal Core Global Share Fund ARSN 089 938 492 #

Pendal Global Fixed Interest Fund ARSN 099 567 558

Pendal Enhanced Credit Fund ARSN 089 937 815

Pendal Fixed Interest Fund ARSN 089 939 542

Pendal Property Securities Fund ARSN 089 939 819

Pendal Global Property Securities Fund ARSN 108 227 005

Pendal Managed Cash Fund ARSN 088 832 491

Pendal Enhanced Cash Fund ARSN 088 863 469

Pendal Active Balanced Fund ARSN 088 251 496

A product disclosure statement (PDS) is available for each of the above products and can be obtained by contacting Pendal on 1800 813 886, or by visiting www.pendalgroup.com. You should consider the relevant PDS in deciding whether to acquire, or to continue to hold, the product.

AQR began managing international equity for BT Financial Group in September 2006.