PENDAL

Factsheet

Equity Strategies

January 2019

Pendal MidCap Fund

Previously known as 'BT Wholesale MidCap Fund'

ARSN: 130 466 581

About the Fund

The Pendal MidCap Fund (**Fund**) is an actively managed portfolio of Australian mid cap shares.

Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes) that exceeds the Pendal MidCap Custom Index over the medium to long term. The suggested investment timeframe is five years or more.

Description of Fund

This Fund is designed for investors who want the potential for long term capital growth and tax effective income from a portfolio of primarily 40-60 Australian mid cap shares and are prepared to accept higher variability of returns. Pendal defines the mid cap universe to include companies ranked between 51 and 150 of the S&P/ASX 200 Index. The Fund may also invest in equivalent companies listed on the New Zealand Stock Exchange, hold cash and may use derivatives.

Pendal's investment process for Australian shares is based on our core investment style and aims to add value through active stock selection and fundamental company research. Pendal's core investment style is to select stocks based on our assessment of their long term worth and ability to outperform the market, without being restricted by a growth or value bias. Our fundamental company research focuses on valuation, franchise, management quality and risk factors (both financial and non-financial risk).

The Fund may have assets denominated in foreign currencies. This means that changes in the value of the Australian dollar relative to foreign currencies may affect the value of the assets of the Fund. The Fund's foreign currency exposure may be hedged from time to time, in whole or part.

Derivatives may be used to reduce risk and can act as a hedge against adverse movements in a particular market and/or in the underlying assets. Derivatives can also be used to gain exposure to assets and markets.

Investment Team

Pendal's Equity team is headed up by Crispin Murray who has extensive experience and a strong record in equities research. Andrew Waddington is the portfolio manager for the Fund.

A combination of the Australian equities large cap and small cap teams' research is used to construct the Pendal MidCap Fund.

Investment Guidelines

Investable universe	ASX and NZX listed and soon to be listed companies, generally with a market capitalisation of A$0.5 billion to A$5 billion; derivatives; cash
Investment ranges	Australian shares 80 - 100% New Zealand shares 0 - 10% Cash 0 - 20%
Ex-ante tracking error	3 – 8%
Number of stocks	Typically 40 – 60
Absolute stock position	15%
Maximum active stock position	+/- 5%[1]
Maximum active sector position relative to index	+/- 10%[1]

[1] compared to benchmark.

Performance

(%)	Total Returns (post-fee)	Total Returns (pre-fee)	Benchmark Return
1 month	2.54	2.62	4.98
3 months	-3.32	-3.10	-1.14
6 months	-10.76	-10.36	-7.12
1 year (pa)	-5.49	-4.40	-2.09
3 years (pa)	11.13	12.25	12.95
5 years (pa)	11.84	13.23	11.61
7 years (pa)	12.51	14.24	10.55
10 years (pa)	13.85	15.75	10.95
Since Inception (pa)	9.39	11.55	5.27

Sector Allocation (as at 31 January 2019)

Energy	5.6%
Materials	19.8%
Industrials	12.9%
Consumer Discretionary	11.6%
Consumer Staples	8.7%
Health Care	4.5%
Information Technology	6.4%
Telecommunication Services	7.4%
Financials ex Property Trusts	5.9%
Property Trusts	2.0%
Cash & other	15.2%

Top 10 Holdings (as at 31 January 2019)

Metcash Trading Limited	4.7%
Nine Entertainment Co Ltd	4.0%
Xero Limited	3.9%
JB Hi-Fi Limited	3.8%
Bendigo & Adelaide Bank Limited	3.8%
Resmed Inc	3.7%
Northern Star Resources	3.1%
Flight Centre Limited	3.0%
Regis Resources Limited	2.9%
Seven Group Holdings Ltd	2.8%

Other Information

Fund size (as at 31 Jan 2019)	$475 million
Date of inception	June 2008
Minimum investment	$25,000
Buy-sell spread[2]	0.50% (0.25%/0.25%)
Distribution frequency	Quarterly
APIR code	BTA0313AU

[2] The buy-sell spread represents transaction costs incurred whenever you invest or withdraw funds, and may vary from time to time without notice.

Management Costs[3]

Issuer fee[4]	0.90% p.a.
Performance fee[5]	20% x the Fund's performance (before fees) in excess of the performance hurdle

[3] You should refer to the latest Product Disclosure Statement for full details of fees and other costs you may be charged.

[4] This is the fee we charge for overseeing the operations of the Fund and managing the assets of the Fund. The Issuer fee is paid from the assets of the Fund and is reflected in the unit price of your investment.

[5] The Fund's performance fee is 20% of the Fund's performance in excess of the performance hurdle. The performance hurdle is the performance of the benchmark (Pendal MidCap Custom Index) plus the issuer fee of 0.90% pa. If a performance fee is payable, it is charged in addition to the issuer fee. The fee is calculated each Business Day based on the investment performance and value of the Fund on that day. If we are entitled to a performance fee, it is paid to us as at 30 June each year.

Risks

An investment in the Fund involves risk, including:

- **Market risk**: The risk that factors affecting one or more countries that can influence the direction and volatility of an overall market, as opposed to security-specific risks.
- **Security specific risk**: The risks associated with an individual security.

Please read the Fund's Product Disclosure Statement (**PDS**) for a detailed explanation of each of these risks.

Market review

The midcap sector enjoyed a strong rebound in January, gaining +5.0% (S&P/ASX 51-150). The sharp positive reversal in market sentiment was underpinned by a shift in prevailing views on two of the key issues which weighed on markets in Q4 2018 – US Fed policy and Chinese economic growth. In the US, there has been a material shift in rhetoric from the Fed, its now more dove-ish stance suggesting that it is not as deaf to market feedback as many feared. We are still facing an environment of reduced liquidity, however investors are now less concerned that a sharp liquidity crunch could drive a more sustained correction. On the other side of the Pacific, China has continued to unveil piecemeal stimulus measures in response to a decelerating economy. This serves as reminder that Beijing does have several levers it can pull to maintain reasonable economic growth, without having to resort to the relatively blunt tool of property stimulus.Mid caps outperformed the broader market in January. Energy (+18.3%) surged on the back of a strong coal price and resurgent oil. A collapsing oil price also weighed on markets in late 2018 and here, too, we have seen a recovery, with the price up 17% as OPEC cuts begin to bite and fears of a major global slowdown recede. Oil companies form a significant part of global corporate credit markets and an improvement in the oil price has relieved some pressure here and seen corporate credit spreads narrow, signalling more confidence. Technology (+10.7%) also outperformed. It was interesting to note the strong performance from the software companies, which formed part of the high growth cohort which surged for much of the last year. The outperformance from companies such as Afterpay Touch (APT, +28.3%), Appen (APX, +24.4%) and Wisetech Global (WTC, +30.4%) shows that appetite for smaller growth stocks remains undiminished, ready to resurface at any signs of better market sentiment. We remain wary of valuations here. Only Health care (-4.3%) and Financials (-1.7%) lost ground. ResMed (RMD, -17.9%), the largest health care stock in the index, dragged it sector down in response to investor concerns at the growth profile for some of its recent technology-focused acquisitions. Challenger, (CGF, -23.7%) was the culprit in the case of Financials, as management downgraded earnings expectations ahead of its 1HFY19 result in February.

Fund performance

The Fund made good gains in January, with a strong surge from some of its exposures to mining and mining services, however it underperformed the index. The positions in Costa Group and ResMed dragged, as did the underweight exposure to the higher-profile technology stocks such as Afterpay Touch, Wisetech and Appen.

Contributors

Underweight Challenger (CGF)

CGF underperformed after management downgraded earnings ahead of its February result. While it continues to benefit from long dated demand for retirement products, recent sales have slowed and margins remain under pressure. Our research suggests pressure will continue both short and long term. CGF's normalised return on equity has fallen by roughly half over the last couple of years and at mark-to-market could fall further. Despite the substantial de-rating, we continue to see better opportunities elsewhere and maintain our underweight.

Overweight Whitehaven Coal (WHC)

WHC's quarterly production reports revealed record volumes for Q4 2018 and management remain positive on the outlook, with strong Asian demand expected to underpin coal prices. While the company continues to face some operational issues at its Narrabri mine, it continues to benefit from the tailwind of strong coal prices, which is feeding through to substantial cash flow and capital return to shareholders.

Detractors

Overweight RMD ResMed

Despite a strong 2QFY19 bottom-line result the stock ResMed (RMD, -17.9%) sold off on a revenue miss driven by weaker rest of the world (ROW) flow-generator (FG) growth and a slight miss from its recent acquisition Brightree. The mask business globally continues to do well and is supported by recent product launches. Issues around ROW FG growth are likely to persist over the next 2-3 quarters, in addition to concerns surrounding the growth rate declines in Brightree. That said, positives from other recent acquisitions are expected to feed through in coming halves.

Overweight CGC Costa Group

CGC downgraded earnings as a number of factors have combined to squeeze margins, including a mix of weaker demand and rising seasonal supply, plus issues with frost in Morocco and delays to its mushroom farm expansion. We maintain our conviction in the stock, which operates in one of the higher growth food categories and is diversifying its business across more produce and geographically, in a capital efficient way, generating high incremental returns, which both adds to earnings growth, but also dampens the usual cyclicality of ag related stocks.

Strategy and outlook

The upcoming reporting season will serve as an important gauge of Australian economic health. While a broad range of indicators suggest a softer environment, we are not seeing any signs of a drastic slump in growth. The Royal Commission's outcome reduces the risk of a credit-crunch inducing recession, while the housing market continues to see a relatively orderly slowdown rather than a catastrophic slump. Nevertheless, we are seeing housing weakness translate to a softer path in terms of retail consumer demand. In this vein, it is important to note that there is little sign of repayment stress or forced sales in the property market. While construction is likely to decline for a period, we are seeing a pick up in capex spending from the miners, while the transport infrastructure pipeline also offers an avenue of growth.

The market has seen a pick up in corporate activity in recent times, with private equity firms being very active and several companies coming under takeover offer. This does drive some opportunities, although it is important to note that the market has not been immediately responsive to new deals, with relatively muted stock responses suggesting a degree of investor scepticism.

Looking forward, while we seem to have shifted from a stance of fear to optimism in a few weeks, we remain mindful that we are in an environment of elevated macro uncertainty with some signs of a softer growth outlook and, as such, would not be surprised if the market moved into a consolidation phase as we shift into reporting season. We are continuing to find decent investments, with the recent market volatility providing attractive entry points in to some longer-term opportunities. IN recent months we have been adding to our position in mining services and infrastructure, via Seven Group. We have added to the existing position in Nine Entertainment, which we believe to be oversold on the back or recent concern about its tie up with Fairfax and softer data from the housing and television advertising markets. We have also been adding to new ideas in the form of Xero and Flight Centre.