PENDAL

Factsheet

Bond, Income & Defensive Strategies

August 2019

Pendal Dynamic Income Fund

ARSN: 622 750 734

About the Fund

The Pendal Dynamic Income Fund (**Fund**) is an actively managed portfolio of fixed income securities, Australian and global credit indices and emerging market sovereign issuers.

Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes) that exceeds the RBA Cash Rate by 2-3% p.a. over the medium term. The suggested investment timeframe is three years or more.

Description of Fund

The Fund is designed for investors who seek income from a portfolio of fixed income securities across a range of market conditions and are prepared to accept some variability of returns.

The Fund is an actively managed portfolio that invests primarily in Australian issued investment grade corporate bonds#. The Fund may also invest in Australian and global credit indices and emerging market sovereign issuers to provide portfolio diversification and enhance returns when we believe market conditions are supportive. The Fund also has the ability to decrease its allocation to credit and invest in cash and interest rate duration strategies when we expect volatility to increase.

Pendal uses a combination of quantitative modelling and qualitative research to construct the Fund's portfolio.

The Fund's portfolio is constructed using the following three step approach:

1. Generate investment themes through quantitative models
2. Reaffirm investment themes with qualitative research
3. Asset Allocation

Investment Team

Pendal's Bond, Income & Defensive team comprises thirteen dedicated investment professionals with both global and domestic experience, invested across Income, Composite, Pure Alpha, Global and Australian Government strategies. The team also draws on a wide range of knowledge resources including Pendal's other specialist investment teams: Equity and Multi-Asset.

The Fund is managed by Vimal Gor, Head of Bond, Income & Defensive Strategies who has more than 24 years industry experience and 9 years at Pendal.

Other Information

Fund size (as at 31 Aug 2019)	$51 million
Date of inception	December 2017
Minimum investment	$25,000
Buy-sell spread[1]	0.14% (0.07%/0.07%)
Distribution frequency	Quarterly
APIR code	BTA8657AU

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

Performance

(%)	Total Returns		Benchmark
	(post-fee)	(pre-fee)	Return
1 month	-0.55	-0.50	0.08
3 months	1.03	1.15	0.28
6 months	3.42	3.61	0.66
1 year (pa)	5.70	6.03	1.41
Since Inception (pa)	4.13	4.44	1.45

Asset Allocation (as at 31 August 2019)

Australian Credit	81.8%
Emerging Market Credit	23.2%
Cash & other	-5.0%

Allocations may not add to 100% due to the use of derivatives to obtain credit exposure.

Top 10 Issuer Exposure

ANZ Banking Group Limited	6.4%
Macquarie Bank Limited	5.9%
Westpac Banking Corp	5.1%
AusNet Services	4.2%
WSO Finance Pty Ltd	3.9%
Toronto-Dominion Bank	3.7%
National Australia Bank	3.4%
Pacific National Finance	3.4%
DBNGP Finance Co Pty Limited	3.3%
AUSGRID Finance Pty Ltd	3.2%

Key Fund Metrics

Average Australian Credit Rating	A-

Portfolio Characteristics

Benchmark	RBA Cash rate
Liquidity	Daily

Management Costs[2]

Issuer fee[3]	0.55% p.a.

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

[3] 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.

#Corporate bonds held within the Fund are required to be rated investment grade at the time of investment. Downgraded securities can continue to be held up to 15% of the Fund (in aggregate). Investment grade bonds refer to securities that are expected to have a high probability of payment of interest and repayment of principal.

Risks

An investment in the Fund involves risk, including:

- **Market risk -** The risk associated with factors that can influence the direction and volatility of an overall market, as opposed to security-specific risks. These factors can affect one country or a number of countries.
- **Security specific risk –** The risk associated with an individual security.
- **International investments risk** – The risk arising from political and economic uncertainties, interest rate movements and differences in regulatory supervision associated with international investments.
- **Interest rate duration risk -** The risk associated with adverse changes in asset prices as a result of interest rate movements.
- **Credit risk -** The risk of an issuing entity defaulting on its obligation to pay interest/principal when due.
- **Emerging markets risk** – The risk of asset price volatility and higher currency, default and liquidity risk from investments in emerging markets
- **Liquidity risk -** The risk that an asset may not be converted to cash in a timely manner.
- **Derivatives risk** – The risks arising from use of derivatives to manage exposures to investment markets.
- **Counterparty risk -** The risk of another party to a transaction failing to meet its obligations.

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

Market review

Australian credit generated another positive return in August, driven by the continued fall in yields and healthy accruals. The drop in yields was alongside increased geopolitical risks and building concerns over a global growth slowdown.

Turning to issuance, August issuance totalled $10.5bn and was dominated by financials. The largest deal was from ANZ, who raised A$3bn of 3 and 5 year paper at 55bps and 77bps over swap respectively. Domestic rival WBC also tapped the market for tier 2 subordinated debt capital with an A$1bn deal. In contrast, issuance from corporates was very light amid the domestic earnings season. QIC Shopping Centres raised A$300 million in a green bond issue.

The Australian iTraxx index (Series 31 contract) traded in a wide 17bp range finishing the month 4bps wider to +63bps. Physical credit spreads also underperformed with the average spread moving out 3bps. The worst performing sector was domestic banks who widened out 9bps, whilst the best performing sector was real estate only widening 1bp. Semi-government bonds underperformed moving out 3bps to government bonds.

Fund performance

The Fund returned -0.50% (pre-fee), which was an underperformance of -0.58% versus the benchmark. This brought the one year return to 6.03% (pre-fee) and an active return of 4.62%.

The domestic credit component made another strong positive contribution on a combination of the continued decline in underlying yields and strong accruals. Infrastructure and utilities, where the fund is overweight, outperformed relative to other areas of Australian credit. Part of the fund's duration exposure was hedged given the strong rally in global bonds for the year, this was a small drag on performance.

The EM exposure was the largest detractor from returns for the month. In addition to weaker risk appetite globally, the EMBI+ Index suffered with concerns over one of its constituents, Argentina. The fund's exposure is solely through the index and there are presently no individual country positions.

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 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. That said, we note the small improvement in house prices recently, along with the tax refund should provide a measure of support. Overall, 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.

In emerging markets (EM), broad sentiment continues to grapple with the contending forces of support from speculation of central bank easing and fears of a global growth slowdown. On the former, we continue to expect renewed stimulus efforts from the influential hands of the Fed and ECB. This should put further pressure on underlying yields. However, EM spreads are likely to remain vulnerable to short-term fluctuations from developments on the Sino-US trade front, with uncertainty extending to the potential spillover effects.

On Argentina, investor concerns have stemmed from the surprise victory from a perceived market-unfriendly candidate in the country's primary elections. We note other South American countries have faced similar worries over policy promises from Presidential candidates, including Brazil and Mexico in recent years. However, these faded over time as the promises did not eventuate into the actions feared. Ultimately, such country-specific concerns have not shown a tendency to spread more broadly across emerging markets as an asset class.

As such, our EM index exposure (that is diversified across a number of countries) will be maintained at roughly 25%. The backdrop for domestic credit also remains supportive and the fund's target weight to the area is 85%. Market volatility will be seen as a potential opportunity to increase the allocation towards that target at more attractive levels.

For more information please call **1800 813 886**,
contact your key account manager or visit **pendalgroup.com**

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