Pendal Enhanced Cash Fund

ARSN: 088 863 469

Factsheet

Bond, Income & Defensive Strategies

August 2019

About the Fund

The Pendal Enhanced Cash Fund (**Fund**) is an actively managed portfolio of debt securities such as short-term money market instruments and medium term notes. Key features of the Fund include next day access to funds and quarterly distribution.

The Fund invests in medium-term securities that are investment graded rated and short-term securities with a credit rating of A-3 or higher by Standard and Poor's or equivalent rating agency. Duration is managed in a range of +/- 0.5 year around the index.

Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes) that exceeds the Bloomberg AusBond Bank Bill Index. The recommended investment time frame is 12 months or more.

Investment Approach

The Fund aims to add value through active management by exploiting market inefficiencies through the shape of the money market curve and the mispricing of credit securities. Research is focused on assessing economic factors, the likely direction of interest rates and credit analysis. Credit margin relative value is assessed with reference to rating, sector, maturity, liquidity and underlying credit fundamentals.

Investment Team

Pendal's Bond, Income & Defensive team includes thirteen dedicated investment professionals. The team also draws on a wide range of knowledge resources including Pendal's other specialist investment teams: Equity and Multi-Asset. The portfolio manager of the Fund is George Bishay, who has more than 23 years industry experience.

Portfolio Characteristics

Weighted average maturity	+/- 0.5 years around the index
Minimum credit rating	BBB- (Long term rating) A-3 (Short term rating)
Liquidity	Following day access (before 2.30pm)

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 asset.
- **Interest rate 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.
- **Liquidity risk -** The risk that an asset may not be converted to cash in a timely manner.
- **Valuation risk -** The risk that the value of an investment in a less active or liquid market is lower than what is reflected in the Fund's unit price.

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

Performance

(%)	Total Returns (post-fee)	Total Returns (pre-fee)	Benchmark Return
1 month	0.04	0.06	0.08
3 months	0.53	0.59	0.34
FYTD	0.32	0.36	0.20
6 months	1.25	1.37	0.82
1 year (pa)	2.36	2.61	1.82
2 years (pa)	2.45	2.70	1.84
3 years (pa)	2.68	2.93	1.81
5 years (pa)	2.62	2.88	2.03

Post-fee return is based on management fees deducted from the unit price: currently 0.25% (pa).

Sector Allocation (as at 31 August 2019)

Money market	36.2%
Corporate	61.3%
Residential mortgage backed	2.5%
Government bond	0.0%
Other asset backed securities	0.0%

Security Credit Ratings (as at 31 August 2019)

AAA	2.5%
AA	40.8%
A	13.4%
BBB	7.1%
Money market	36.2%

Statistics (as at 31 August 2019)

Modified duration	0.11 years

Other Information

Fund size (as at 31 Aug 2019)	$720 million
Date of inception	January 1994
Minimum investment	$25,000
Buy-sell spread[1]	0.06% (0.03%/0.03%)
Distribution frequency	Quarterly
APIR code	WFS0377AU

[1] 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[2]

Issuer fee[3]	0.25% pa

[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.

Market review

Australian bonds extended their rally in August as yields tumbled globally on a combination of factors. This included geopolitical risks with the further intensification of the trade war, as well as building concerns over weaker global growth. Such downside risks were noted by the RBA in its August policy statement. In the wake of two back-to-back cuts from the Board, it opted to keep rates on hold at 1.0% during the month and indicated it could "ease monetary policy further if needed". At month-end, markets were pricing a further 50 basis points in reduction by early next year.

Domestic data was mixed over the month. The NAB Business Conditions survey eased 2 points to +2, while confidence did the opposite. Retail sales (+0.4%) surprised to the upside and consumer confidence bounced back to 100 from 96.5. In contrast, the CBA August Composite PMI dropped into contractionary territory (49.3 from 52.1). Meanwhile among the lagging data, job additions of 41.1K beat expectations and were driven by full-time positions. However, an increase in the participation rate to 66.1% kept the unemployment rate steady at 5.2%.

Offshore, investors' attention was focused on the latest escalation of trade conflict that in turn stirred another wave of safe-haven demand for bonds. Concerns were ignited at the outset of the month as President Trump announced an additional 10% tariff on the US$300bn of remaining Chinese imports, to take effect on September 1st. China responded in-kind by halting its purchases of US agricultural goods. A series of small concessions, followed by renewed threats saw sentiment swing considerably through the remainder of the month. Adding to investor worries were a litany of regional events; Hong Kong protests, Argentina default speculation, Brexit uncertainty and another Italian political drama.

Beyond the politics, the Fed did not meet during the month after delivering a cut at the end of July, its first in more than a decade. Communication including an address by Chairman Powell at Jackson Hole was underwhelming, but suggested the central bank remained tilted towards further easing. The lack of a more explicit stimulus signal was heavily criticised by President Trump.

Also in the US, a collection of leading indicators from the world's largest economy pointed to a further softening. ISM Manufacturing missed expectations and fell further to 51.2 while Markit's gauge edged down to 50.3 and closer to contractionary territory. Consumer confidence also fell, while retail sales beat expectations and rose a healthy +0.7%.

In Europe, there was no gathering for the ECB during the month. However, deteriorating data for the region reinforced speculation that the central bank would provide additional stimulus at their September meeting. Second quarter GDP growth for Germany, the region's largest economy, contracted alongside a weakening of more forward-looking indicators.

Turning to market data, Australian bond yields plumbed fresh record lows during the month and the curve flattened materially. The 3 year yield fell -13bps to 0.67% and the 10 year by -31bps to 0.90%. Meanwhile at the very front-end, 90 day BBSW slid a relatively marginal 3bps to 0.97%. US yields experienced more sizeable declines with the 2 and 10 year falling -37bps and -52bps to 1.51% and 1.50% respectively. Outside of rates, the AUD/USD dropped by 1.6% as risk appetite soured and iron ore plunged by -24%.

Credit markets felt the negative effects from softer risk sentiment over the month. The global geopolitical risks, chiefly the trade war tit-for-tat, dominated the market's direction and swings through August. This overshadowed more corporate-specific factors, including the domestic full-year reporting season.

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 and activity

The Fund underperformed the benchmark by 2 basis points (pre fee) in August after a very strong seven month period. Negative performance came from financials whilst industrials added to performance.

Activity during the month included investing in 3 year maturity major banks funded out of cash.

As at the end of the month, the portfolio had a credit spread of 63bps over bank bills, interest rate duration of 0.11 years and credit spread duration of 1.92 years.

Outlook

The Reserve Bank left the cash rate unchanged at its meeting in early September. There was a minor change in the accompanying statement with the reference to monitoring developments in the labour market closely watered down. This was most likely done to avoid the assumption that a rise in the unemployment rate will automatically result in further monetary policy easing. The Reserve Bank continues to see an extended period of low interest rates, not surprising given their most recent forecasts in the Statement on Monetary Policy. Annual underlying inflation is not expected to reach 2% until mid 2021 and the unemployment rate is expected to remain above 5% for 2020 due to sub trend economic growth. The risks to global growth are also clearly tilted towards the downside. Given the benign state of the domestic economy and the offshore headwinds posed we expect further policy easing, most likely occurring prior to the end of the year.

The global macro environment continues to offer the greatest guidance to domestic credit and it has proven a very dynamic and fast-evolving backdrop. The two key elements of influence remain trade wars and expectations of more dovish central banks, including the Fed and ECB. Attitudes towards the former have shown a tendency to shift quickly and overshadow growing expectations for a more dovish Fed. As such our positioning remains tactical in nature and we prefer to maintain flexibility to adapt should the environment change.

We are wary that the underlying issues behind the trade wars threaten to devolve into a more prolonged "cold war". As illustrated throughout August, any perceived progress can evaporate quickly along with a positive perspective from investors. It is also increasingly evident that US-China relations have not materially improved despite some small progress at the G20 summit earlier in the year. As such, there is a risk that the relationship between the world's two largest economies may remain frosty.

The negative impact of tariffs has become more evident on both the Chinese and US economies as visible in the deterioration of activity indicators like manufacturing surveys and a slowdown in GDP growth. In Asia, this has flow-on effects for China's neighbours, particularly those that are highly dependent on exports to the Asian giant (such as South Korea). The knock-on effect to the US has also become more apparent, as evident in several earnings results from US corporates. However we also note that in aggregate, US earnings have shown resilience with Q1 and Q2 earnings surprising to the upside.

On the Fed, the more dovish stance adopted in January and subsequent cut in July represented a significant shift from last year and in turn is more of a tailwind for credit than a headwind as in 2018. The prospect of further easing has resurfaced the idea of the "Fed put" that would effectively limit the extent of a sell-off in risk assets. If policymakers continue to swing to the more dovish end of the spectrum, it may more than compensate for concerns over the trade war.

The local market has also been afforded some support from positive domestic developments that may contribute to an outperformance compared to offshore credit. This includes more supportive fiscal policy in the wake of the Coalition's win in the Federal Election, as well as easing of monetary policy by the RBA. The weight of the Royal Commission has also been lifted from the shoulders of the major banks. Moreover, new issuance has been well-bid and supply relatively light compared with prior years.

Overall, the backdrop for risk assets continues to fluctuate as investors balance the risks posed by trade wars against the outlook for more flexible central banks. We are wary that sentiment towards the trade war can shift with each individual battle and the underlying issues are yet to be resolved. As such we maintain a cautious stance and prefer tactical positioning in order to remain nimble.

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

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