Pendal Sustainable Balanced Fund

Factsheet

Multi-Asset Strategies

September 2019

About the Fund

The Pendal Sustainable Balanced Fund (**Fund**) is an actively managed diversified portfolio that invests in Australian and international shares, Australian and international property securities, Australian and international fixed interest, cash and alternative investments. Investments are selected based on a range of sustainable, ethical and financial criteria.

Investment Return Objective

The Fund aims to provide a return (before fees and expenses) that exceeds the Fund's benchmark over the medium to long term. The suggested investment timeframe is five years or more.

Description of Fund

For Australian and international shares and Australian and international fixed interest, the Fund uses an active security selection process that combines sustainable and ethical criteria with Pendal's financial analysis. We actively seek exposure to securities and industries that demonstrate leading environmental, social and corporate governance (ESG) and ethical practices while avoiding exposure to companies with activities or behaviour we consider to negatively impact the environment or society.

The Fund will not invest in companies with material business involvement in the following activities:

- production of tobacco or alcohol,
- manufacture or provision of gaming facilities,
- manufacture of weapons or armaments,
- manufacture or distribution of pornography,
- directly mine uranium for the purpose of weapons manufacturing,
- extraction of thermal coal and oil sands production.

We consider that a company or issuer has a material business involvement in an activity if 10% or more of its total revenue is derived from that activity.

The assets of the Fund are managed by Pendal together with a number of leading investment managers, such as AQR for international shares and AEW for international property securities. Pendal manages the asset allocation of the Fund.

Pendal actively engages with the management of the companies we invest in to manage risk, effect change and realise potential value over the long term.

Benchmark

The benchmark for the Fund is created from a range of published indices. The benchmark is based on the neutral position and the index returns for each asset class. Details of the particular market indices used for the Fund's benchmark can be found at http://www.pendalgroup.com/Pendal-Sustainable-Balanced-Fund.

Investment Team

The Fund is managed by Stuart Eliot who has more than 30 years' industry experience. The team has a diverse skill set; combining a range of global and domestic market experience and drawing on the resources of Pendal's other specialist teams.

CERTIFIED BY RIAA

The Pendal Sustainable Balanced Fund has been certified by RIAA according to the strict operational and disclosure practices required under the Responsible Investment Certification Program. See www.responsibleinvestment.org for details.

The Responsible Investment Certification Program does not constitute financial product advice. Neither the Certification Symbol nor RIAA recommends to any person that any financial product is a suitable investment or that returns are guaranteed. Appropriate professional advice should be sought prior to making an investment decision. RIAA does not hold an Australian Financial Services Licence.

Performance[1]

(%)	Total Returns (post-fee)	Total Returns (pre-fee)	Benchmark Return
1 month	0.83	0.91	1.04
3 months	2.08	2.31	2.45
6 months	5.95	6.43	7.26
1 year (pa)	5.44	6.39	9.44
2 years (pa)	7.05	8.01	10.32
3 years (pa)	7.02	7.99	9.28
5 years (pa)	6.94	7.90	8.90

Asset allocation (as at 30 September 2019)

Australian shares	34.8%
International shares	28.1%
Australian fixed interest	10.9%
International fixed interest	6.6%
Australian property securities	3.0%
International property securities	1.1%
Alternative investments	14.3%
Cash	1.2%

Investment Guidelines

Asset allocation ranges (%)	Neutral position	Ranges Min	Ranges Max
Australian shares	34	28	48
International shares	26	12	32
Australian fixed interest	12	5	32
International fixed interest	5	0	20
Australian property securities	3	0	10
International property securities	1	0	10
Alternative investments	15	0	20
Cash	4	0	10

Other Information

Fund size (as at 30 Sep 2019)	$692 million
Date of inception	August 1984
Minimum investment	$500,000
Buy-sell spread[2]	0.28% (0.14%/0.14%)
Distribution frequency	Quarterly
APIR code	BTA0122AU

[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% pa
Estimated indirect costs[5]	0.05% pa

[3] You should refer to the latest Information Memorandum 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] This is an estimate of the last financial year's indirect costs. These are reflected in the unit price of the Fund and are not charged to you as a fee or retained by us.

[1] The asset allocation neutral position, asset allocation ranges and the benchmark have changed over time. As it is historical information, the Fund performance reflects the asset allocation neutral positions and ranges that have applied over time. The benchmark performance shown is that of the combined benchmarks that the Fund has aimed to exceed over time.

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.
- **International investments risk** – The risk arising from political and economic uncertainties, interest rate movements and differences in regulatory supervision associated with international investments.
- **Currency risk -** Currency exchange rate fluctuation risk arising from investing across multiple countries.
- **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.
- **Counterparty risk -** The risk of another party to a transaction failing to meet its obligations.

Please read the Fund's Information Memorandum (**IM**) for a detailed explanation of each of these risks.

Markets review

Australian equities (S&P/ASX 300 Accumulation Index) rose 1.9% in September, with seven out of the eleven GICS sector ending positive. August laggards, Financials (+4.2%) and Energy (+4.5%) lead the market this month as a rotation to value saw many growth and long rallied defensive stocks fall. Within Energy, Oil Search (OSH, +11.5%) performed the strongest, after the Papua New Guinean government confirmed the development of the Papau LNG Project – where Oil Search has a 23% stake in the project. Although Oil Search's Alaskan asset reported a higher than anticipated cost base, the negative update did not infringe much on share price gain. Additionally, Oil Search also benefited from the surge up in oil price after the drone attacks upon the Abqaiq and Khurais oil facilities in Saudi Arabia – disrupting 5% of global oil supply. Other companies such as Beach Energy (BPT, +3.3%), Origin Energy (+6.6%), Worley Parsons (WOR, +5.9%) and Caltex Australia (CTX, +11.3%) also benefited from the uptick in price. Caltex Australia had earlier in the month experienced unexpected weakness in its retail fuel margins and Worley Parsons result had revealed the effects of a weaker oil price and a reduction in capex on new production.

The major offshore equity markets generated a positive return for September, buoyed by an easing of concerns on the US-China trade issue and further monetary easing by the US Federal Reserve (Fed) and European Central Bank (ECB). Tensions on the political front remained a prevalent theme, illustrated by a move to establish a Congressional investigation for the impeachment of President Trump. Investors have developed a degree of immunity to these issues but retain focus on the implications of an economic slowdown. Large sectoral rotation was evident this month through sizeable shifts away from defensive low volatility stocks and higher growth technology towards energy and financials which have underperformed in recent years. Despite the UK Brexit negotiations appearing to go from bad to worse, European markets outperformed their US counterparts, and Asian markets underperformed developed markets. The MSCI World (A$) TR Index ended the month with a 2% return, with contributions from the US (+1.7%), Europe (+4.2%) and Japan (+5.0%).

The US equity market advanced without continuing its leadership evidenced through much of the year, explained in part by the rotation out of mega cap technology stocks into cheaper, unloved sectors. US energy companies received a boost from a spike in the oil price after a drone attack on Saudi Arabian oil processing systems, said to account for 10 million barrels of crude-oil production. In terms of the broader economy, signs of some weakness emerging appeared with the latest data, indicating a 0.1% decline in consumer spending for the month and a slower than expected growth in employment numbers. The sector rotation was evident in the divergent performance of the market, with the S&P500 index 1.7% higher while the tech-laden Nasdaq ended September with a 0.5% return.

European equity markets responded positively to the latest ECB policy initiatives to reduce the deposit interest rate by 0.10%, restart quantitative easing and provide more favourable bank funding to incentivise lending to businesses and consumers plus introduce deposit tiering to reduce the impact of negative interest rates on banks' profitability. Coinciding with the announcement were comments from ECB President Draghi to emphasise the importance of fiscal responses, acknowledging limitations of monetary policy. These comments came amid the latest data release on the closely followed industrial survey – the PMI, which declined to a reading of 50.4 from 51.9 in August, indicating the European economy is dangerously close to contraction. Still, the markets retained an optimistic stance, with Germany (+4.1%), France (+3.6%) and Spain (+4.9%) contributing the region's performance.

Asian equity markets delivered mixed responses in September, despite signs of goodwill emerging between the Trump and Xi camps. China's Central Bank supported the market with a 0.5% cut to the Reserve Requirement Ratio that impacts bank lending. Korea (+5.8%), Taiwan (2.0%) and India (+3.6%) were among the better performers in September. Korea and Taiwan did well on support from a number of technology names, while India performed well after the Government announced a surprise cut to the corporate tax rate from 30% to 22%, in addition to the Central Bank of India cutting its official; interest rate.

The Australian dollar was relatively unchanged against the US dollar but 1% stronger against the euro and 1.9% higher against the yen. Gold (-3.2%) took a breather after its strong run while crude oil also declined after the mid-month spike, closing at US$54 per barrel.

Australian bonds gave back some of their prior month's gains during September. This was amid a global sell-off in rates at the long end of curves as investors shifted back into risk-assets. Meanwhile at the very front-end, yields were pulled slightly lower in several markets due to central bank action. This included Australia, where speculation of a cut by the RBA increased through the month and was ultimately delivered at the outset of October. Governor Lowe cited increased downside risks, particularly tied to greater uncertainty over the global outlook, in his statement. There was also a greater emphasis on the labour market and achieving full employment. The gap between the unemployment rate and that associated with full employment widened during September with a slight increase in the former of 0.1% to 5.3%. Broader domestic data was weaker overall. Among the leading indicators, the NAB Conditions and Confidence measures both retreated to +1 from +2 and +4 respectively. Finally in terms of market movements, Australian 3 and 10 year yields rose 6bps and 13bps respectively to 0.74% and 1.02%. However expectations for the RBA rate reduction saw 3 month BBSW fall 3bps to 0.95%.

Global bonds gave back some of their prior month's gains during September. This was amid a sell-off in rates at the long end of curves as investors shifted back into risk-assets. Meanwhile at the very front-end, yields were pulled slightly lower in several markets due to central bank action. This included in the US, where the Federal Reserve cut its benchmark rate by 25bps to 1.75%. However, the accompanying projections and address from Chairman Powell suggested a less dovish message than anticipated. Meanwhile, US data continued to paint a mixed picture with a weaker manufacturing sector at one end offset by a healthy consumer at the other. In Europe, the ECB also eased policy further with a 10bps cut to its deposit rate to -0.50% and unveiled a new open-ended quantitative easing programme. Beyond monetary policy developments and the economic data, investors appeared less concerned over geopolitics through most of the month. Finally in terms of market movements, the US 2 and 10 year added 12bps and 17bps to 1.62% and 1.67%, while the 3 month LIBOR rate fell 5bps to 2.09%.

Fund performance

The Fund's return for September reflected the contribution from exposure to growth assets, primarily within listed equities. Domestic listed property (-3.0%) was the exception as the sector surrendered some of its recent gains. Exposure to bonds detracted from returns this month, in keeping with their diversifying role.

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 Atlas Arteria, Evolution Mining, Telstra and CSL detracted from performance while overweight positions in Fortescue Metals, Oil Search and Qantas contributed to performance.

The Alternatives strategy delivered a total return (before fees) of -0.09% versus a cash return of 0.08%. Within our Alternatives core portfolio the Global Macro, Equity Market Neutral and Opportunistic strategies delivered gains, while the Managed Futures, Long-short equity and Fixed Income Relative Value strategies detracted part of the sector's return.

In relation to our tactical positioning within the Alternatives component of the Fund, the Fund profited from a short volatility position which offset detractions from defensive overweight gold and bond positions. At the end of September we closed an overweight US equities position, leaving the portfolio tilts as overweight Australian equities, gold and bonds together with a short volatility and copper position.

Strategy and outlook

The Australian market has now moved past some concerns felt earlier in the year, mainly in relation to the Federal election, developments in the housing market and policy direction of the RBA. With economic monetary and fiscal policy now proceeding together towards stimulatory settings, growth assets like shares and property are well placed to benefit, albeit to a degree.

The labour market needs to be a key area of focus, considering the bearing it has on management of related pressures such as household debt, low inflation and benign wages growth. Further easing of monetary policy in conjunction with tax relief can play its role in shoring up a weakening economy. Expansionary settings employed in the past few economic cycles have generally had the desired effect, although the record low level of the cash rate and external factors relating to trade warrant a degree of caution for investors, particularly those with a greater reliance on cash-based yields.

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.

Regnan Sustainability Snapshots[#]

Atlas Arteria Group (ALX)

Atlas Arteria Group is an Australia-based global toll road developer, operator and investor, with assets in France, Germany and USA.

Customer safety is a key priority for the company. In addressing customer safety, subsidiary Autoroutes Paris Rhin Rhône (APRR) in France is testing new safety systems including dynamic speed limits, wrong-way driving detectors, automatic incident detection in tunnels, and an "SOS Autoroute" mobile app that serves as an on-board emergency roadside telephone. These efforts have seen the number of accidents resulting in injuries or fatalities drop by more than 50% since 2003. The Warnow Tunnel in Germany has been named one of the safest tunnels in Europe, thanks to leading safety initiatives such as communication systems that are able to transmit radio frequency into vehicles, lighting to improve visibility in the tunnel, and radar cameras that detect potentially risky behaviour.

ALX is adapting to a low carbon future by offering to reduce the carbon footprints of its customers on APRR services, including parking for carpooling and carpooling routes, electric charging stations, and discounted tolls for customers using electric vehicles.

Conduct culture processes have been strengthened with the introduction of whistleblower policies for all operating regions – Australia, Europe and USA – underpinned by an independent whistleblower service.

Charter Hall Group (CHC)

Charter Hall Group (CHC) is an integrated property group involved in investment management, and property development, leasing, and management. CHC invests across all major property segments including office, industrial, retail, and social infrastructure.

Ongoing improvement in building energy and GHG performance is increasingly important to portfolio resilience. CHC has evidenced improvements across property segments over 2018-19. Average NABERS ratings in the office segment improved to 4.77 (from 4.66). Demand for sustainable office tenancies is now considered a minimum requirement in the A-grade office segment.

CHC also entered a Power Purchase Agreement to install solar PV across 14 shopping centre assets, expected to deliver 40% of energy needs. Current Group retail portfolio NABERS Energy rating of 3.9 should improve markedly once fully implemented. CHC has also set a target of 100% reduction of emissions within the Group's direct control (Scope 1 and 2) by 2030, which brings the company in line with leading peers.

Year-on-year improvements to workplace culture are positive in our view, given previous concerns with talent attraction and retention. Regnan has observed marked improvement to the Group's human capital management practices since 2015, which include greater focus on role support and development for high performing employees. Improved practices appear to be driving higher employee satisfaction and retention. Employee engagement improved to 87%. Voluntary employee turnover was 14.2% in FY19 which is in line with sector averages. Improved performance on these metrics suggests human capital strategies are achieving desired results. Human capital metrics are included in the executive remuneration, supporting continued management focus.

CHC has also progressed its response to modern slavery and protection of human rights, with implementation of a human rights framework. The framework includes a human rights policy, a supplier code of conduct, and a modern slavery working group which was set up to improve governance and drive practice improvements across procurement.

[#] The information in the Sustainability Snapshots is provided by Regnan Governance Research and Engagement Pty Limited (ABN 93 125 320 041). It should not be relied upon in making a decision to invest or a decision in relation to an existing investment. The information relates only to Regnan's assessment, based on its research and the information available to it, of the performance of the company in relation to environmental and social issues and should ***not*** be regarded as a recommendation or statement of opinion by Regnan on:

i. any other aspect of the company's performance;
ii. the prospects of the company; or
iii. the company's suitability or attractiveness from an investment perspective.

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