PENDAL

Factsheet

Pendal Australian Share Fund

ARSN: 089 935 964

Equity Strategies

November 2019

About the Fund

The Pendal Australian Share Fund (**Fund**) is an actively managed portfolio of Australian shares.

Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes) that exceeds the S&P/ASX 300 (TR) 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, diversification across a broad range of Australian companies and industries and are prepared to accept higher variability of returns. The Fund may also 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).

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. Derivative can also be used to gain exposure to assets and markets.

Investment Team

Pendal's nineteen member Equity team is one of the largest in the Australian fund's management industry. The portfolio manager for the Fund is Crispin Murray, who has more than 28 years' industry experience. Crispin is also Head of Equity.

Investment Guidelines

Ex-ante (forward looking) tracking error	2.0% - 6.0%
Min/max stock position	+/-4%
Min/max sector position	+/-8%

Other Information

Fund size (as at 30 Nov 2019)	$1,013 million
Date of inception	September 1992
Minimum investment	$25,000
Buy-sell spread[1]	0.50% (0.25%/0.25%)
Distribution frequency	Quarterly
APIR code	RFA0818AU

[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]	0.79% 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.

Performance

(%)	Total Returns		Benchmark
	(post-fee)	(pre-fee)	Return
1 month	4.35	4.42	3.18
3 months	6.54	6.74	4.75
FYTD	6.43	6.78	5.41
6 months	9.49	9.92	9.25
1 year (pa)	24.78	25.79	26.04
2 years (pa)	10.97	11.85	11.69
3 years (pa)	12.93	13.84	12.67
5 years (pa)	9.74	10.62	9.96

Sector Allocation (as at 30 November 2019)

Energy	8.3%
Materials	18.7%
Industrials	11.6%
Consumer Discretionary	5.8%
Consumer Staples	2.7%
Health Care	12.4%
Information Technology	2.3%
Telecommunication Services	7.3%
Financials ex Property Trusts	23.3%
Property Trusts	4.4%
Cash & other	3.2%

Top 10 Holdings (as at 30 November 2019)

CSL Limited	9.2%
Commonwealth Bank of Australia Ltd	6.5%
BHP Billiton Limited	6.3%
Telstra Corporation Limited	5.3%
ANZ Banking Group Limited	4.3%
Qantas Airways Limited	4.1%
Westpac Banking Corporation	3.7%
Santos Limited	3.2%
Transurban Group	3.2%
Macquarie Group Limited	3.1%

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

Australian equities, as measured by the S&P/ASX 300 Accumulation index (+3.2%) rebounded strongly in November, with the major GICS sectors all recording gains except for Financials (-2.0%), which were dragged down by Banks (-3.7%). As a result, the MSCI Australia IMI Value index underperformed its Growth counterpart by -4.2% over the month.

Within Banks, three of the "big four" recorded losses, with the exception of Commonwealth Bank (CBA, +2.7%). The share price of Westpac (WBC, -10.5%) dropped by the most over the month, as civil proceedings were brought by AUSTRAC. The regulator accused the bank of a raft of failures in oversight and reporting on international fund transfers under obligations to anti-money laundering and counter-terrorism financing laws. Management had previously flagged the AUSTRAC investigation, while claiming the issue was not of the scale and gravity as that faced by CBA in 2017. Many of the key facts of AUSTRAC's claims against WBC remain unclear. Some issues, such as ASIC's interest in the timing of WBC's capital raise, may drag on for some time. However it appears likely there will be onerous financial implications in the form of a fine, potential capital charge, and the need to invest in system improvements. The bank has taken a decisive step with the removal of the CEO and acceleration of the Chairman's retirement. Several other directors are also in line for election at the upcoming AGM.

The "regional duo" also fared worse in November. Bank of Queensland (BOQ, -10.4%) recorded a double-digit loss after announcing a $275m capital raising. The raising will be 8% dilutive and – in combination with cost-driven headwinds to NPAT and expected payout ratio – implies a reasonable cut to the per-share dividend. There was little detail around the bank's intentions for the additional capital. The new CEO is expected to outline his strategy in February next year. Bendigo & Adelaide Bank (BEN, -3.9%) fell in sympathy. While the focus of regulatory and political pressure has been on changing behaviour at the Big Four banks, there is no doubt regional banks are also feeling the pinch of the current environment, making it harder for them to improve their competitive position.

On the other side of the spectrum, Health Care (+9.6%) and Information Technology (+11.1%) are the two best performing sectors, with the former also being the largest contributor to the headline index's gain. Xero (XRO, +17.8%) was amongst the best performers, after delivering a well-received result. Revenue gained 32% over the year but subscriber strength drove the reaction. XRO now boasts 2.06m subscribers, after 478,000 new additions over the year. Highlights included an additional 73,000 new subscribers in the UK in 1H FY20, which suggests XRO's strategy of focusing on the one-off opportunity afforded by a shift to mandatory online tax for businesses is playing out.

Elsewhere, James Hardie (JHX, +17.0%) was the standout from Materials (+5.5%), after delivering a strong half-year result. Profit was up 17% and there was an upgraded outlook for the full financial year. While the outlook for the Australian housing market remained muted, management expected to continue winning more share. At the same time James Hardie continues to benefit from modest growth in the US housing market. Lastly, Caltex Australia (CTX, +26.7%) helped lift the Energy sector (+7.5%). The company upgraded earnings for the half year, an early call which suggests a high degree of management confidence given the volatility in petrol prices. It also announced plans to spin 250 petrol stations out into a REIT, of which CTX would retain a 51% holding. Subsequently, it transpired that the world's largest petrol retailer, Canada's Alimentation Couche-Tard, had made a takeover off in October. CTX does own one of Australia's four refineries, which means the deal will attract scrutiny from the Foreign Investment Review Board.

Fund performance

The Fund outperformed its benchmark over the month of November.

Contributors

Overweight Qantas

Qantas (QAN, +13.9%) announced new long-term margin targets at its investor day, with a strategy to lift the Qantas domestic margin from 12% to 18% and Jetstar's domestic margin from 14% to 22% in 2024. This would be considered a stretch by many people. However these targets are also in line with margins in other domestic markets with a stable industry structure. Even if these targets are not achieved, there is a sense that efforts to do so will still lead to material margin improvement. The national airliner remains one of our highest conviction positions.

Underweight NAB

Investor sentiment for the banking sector was dampened over the month, first by the somewhat weaker than expected full-year results from ANZ (-4.2%); and then the civil proceedings brought by AUSTRAC against Westpac (WBC, -10.5%). The share price of NAB (-6.8%) fell in sympathy. We see the operating environment for the banks as cyclically challenged, and remain underweight to the sector.

Detractors

Do not hold Woolworths

The share price of Woolworths (WOW, +6.5%) advanced in November, and not owning it weighed on the portfolio's relative performance. Our preferred company from the sector remains Metcash (MTS, +6.4%). Despite the loss of its 7-eleven contract, which will see MTS lose some low-margin revenue, we retain confidence in MTS – and the belief that the more important issue for MTS is the sales trends and price inflation returning to groceries. In both instances there have been reassuring signs. Metcash is due to deliver is HY20 results on December 5.

Overweight Nine Entertainment

Nine Entertainment (NEC, -4.1%) fell over the month, after Management downgraded the outlook for FY20 at the AGM as TV advertising revenue remained weaker-than-expected. The free-to-air ad market has been in structural decline for several years. But this has been exacerbated in the past 12 months by cyclical issues as companies cut their ad budgets given a soft domestic economy. This issue is well-known, but there was some expectation NEC would be cycling the start of this downturn – in Q4 2018 – and that the -5% to -6% trend would moderate to -1% to -2%. However management flagged that the decline remains in the minus 5-6% range and have now baked that rate into their expectations for FY20. It is important to remember that free-to-air TV advertising revenue has declined to around a third of NEC's revenue since the merger with Fairfax Media. Stan and Nine Now continue to do well, as does the newspaper division. Domain Group (DHG, +10.4%), which makes up another third of the company's value, has also been doing well in recent times.

Strategy and outlook

The portfolio delivered a strong month both in absolute terms and relative to the index. Recent outperformance has been driven by a combination of different kinds of stocks. There has been strong gains in some of the portfolio's industrial cyclicals such as Qantas (QAN) and James Hardie (JHX), as the market has gained confidence in the longer term outlook despite some concerns around near-term demand. Telstra (TLS), a relatively defensive yield stock, has also done well. At the same time, some of the growth names have also done well, notably CSL (CSL) and Xero (XRO).

The performance of the growth stocks in the portfolio has been particularly interesting. Growth, as an investment style, has outperformed value globally by a significant margin over the last few years, driven by a regime of falling interest rates and abundant liquidity. It has done particularly well for much of the last year, as expectations around the outlook for rate cuts in the US have shifted.

However there has been something of a rotation away from growth stocks to value, at a global level, in the last couple of months. This can be tied to bond yields retreating from their lows of mid-August when the outlook for global economic growth hit something of a nadir. However in Australia this rotation has not been as apparent. Performance has been mixed among growth stocks, with CSL and XRO, in particular, continuing the recent run of performance.

The thematic effect of the bifurcation between growth and value has been as strong as anything we have seen for many years and has been a challenge for active managers. Growth style investors have generally done well - the risk here is that it is difficult to consistently time the rotation between thematic tailwinds. Value based investors have generally had a difficult period for an extended time.

For us, this emphasises the importance of a core, or style neutral, approach. Given the strength of the recent growth tailwinds it has been a challenge at times in the last twelve months to immunise the portfolio against the thematic risks and allow stock specific risk to dominate. However the strength coming through in some of the more cyclical stocks in recent months demonstrates that we have been able to build and maintain these positions, while also gaining exposure to the growth thematic via the careful selection of individual growth names.

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

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