

## Pendal Sustainable Balanced Fund

ARSN: 637 429 237

## Factsheet

Multi-Asset Strategies

June 2020

### 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](http://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<sup>1</sup>

(%)	Total Returns		Benchmark Return
	(post-fee)	(pre-fee)	
1 month	0.40	0.46	0.74
3 months	8.75	8.96	8.23
6 months	-5.42	-5.04	-3.70
1 year (pa)	-1.43	-0.59	0.05
2 years (pa)	1.78	2.67	4.69
3 years (pa)	4.05	4.97	6.34
5 years (pa)	4.34	5.27	6.49

### Asset allocation (as at 30 June 2020)

Australian shares	30.2%
International shares	32.5%
Australian fixed interest	5.3%
International fixed interest	4.5%
Australian property securities	4.3%
International property securities	1.0%
Alternative investments	16.9%
Cash	5.3%

### Investment Guidelines

Asset allocation ranges (%)	Neutral position	Ranges	
		Min	Max
Australian shares	30	20	40
International shares	30	20	40
Australian fixed interest	8	0	25
International fixed interest	5	0	25
Australian property securities	3	0	10
International property securities	1	0	10
Alternative investments	15	0	20
Cash	8	0	20

### Other Information

Fund size (as at 30 Jun 2020)	\$558 million
Date of inception	August 1984
Minimum investment	\$25,000
Buy-sell spread <sup>2</sup>	
For the Fund's current buy-sell spread information, visit <a href="http://www.pendalgroup.com">www.pendalgroup.com</a>	
Distribution frequency	Quarterly
APIR code	BTA0122AU

<sup>2</sup> 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<sup>3</sup>

Issuer fee <sup>4</sup>	0.80% pa
Estimated indirect costs <sup>5</sup>	0.05% pa

<sup>3</sup> You should refer to the latest Product Disclosure Statement for full details of fees and other costs you may be charged.

<sup>4</sup> 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.

<sup>5</sup> 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.

<sup>1</sup> 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.
- **Interest rate risk**: The risk associated with adverse changes in asset prices as a result of interest rate movements.
- **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 Product Disclosure Statement (**PDS**) for a detailed explanation of each of these risks.

## Market review

The S&P/ASX 300 continued to benefit from positive sentiment around the pace of the economic rebound and the degree of fiscal and monetary policy support. It gained +2.4% in June, to cap a very strong +16.8% return for the quarter. The index is now down -10.6% for the calendar year to date. This came despite some wobbles late in June as the market expressed some concern over the rise in cases in the US as it rolled back restrictions.

There was strong rotation from growth and defensives to value and more cyclical stocks during the quarter as confidence around the economy improved – although this rotation stalled late in the period.

Economic data continued to reflect the material blows inflicted by the shutdown. However in most respects it is not as bad as many as expected – while the rebound in activity and confidence indicators has also been sharp.

Continued easing of mobility restrictions saw global markets rally again in June. However, a surge in new cases, especially across large tracts of the US, has raised the spectre of a second wave of COVID-19 infections. This looming threat, coupled with an equity market that had largely shrugged off the epidemic, weighed on sentiment towards the end of June.

The shadow cast by the second wave has markets forecasting an 'incomplete' recovery. In late June, COVID-19 cases in the US were rising at a peak of c.40k per day. In particular, there has been a strong spike in cases in Florida, Louisiana, and Nevada. Overall, there have been 2.6 million cases and 127,425 recorded deaths in the United States, with this increase in cases leading to at least 16 US states reimposing restrictions.

Investor returns were softened as the AUD rose 2.5c to \$0.689, partly due to high iron ore prices and improving risk sentiment. A falling USD and a more optimistic growth outlook saw oil prices rise. Gold prices also rose US\$39.40/oz to US\$1,768.10/oz. Global bond yields were little changed through June.

In local currency terms, MSCI Asia ex-Japan index (7.4%) and MSCI World EM index (6.7%) were among the strongest performers while FTSE 100 index (1.7%) and Nikkei 225 index (2.0%) were two of the weakest.

## Fund performance

The Fund underperformed the benchmark over the month of June.

Active positioning contributed slightly negatively to returns due to the ongoing trend-reversal in copper prices and choppiness in equity implied volatility. Portfolios started June positioned fairly risk-neutral with overweights in several under-valued equity markets but also with a small net underweight in equity trend-following, overweight positions in Australian and Canadian 10-year

bonds, hedged by an underweight in US Treasury Notes, long gold and short copper and VIX.

In equities, our active positioning driven by valuation insights held modest overweight positions in UK's FTSE 100, Japan's Topix, a long position in the futures of EURO STOXX 50 dividends paid in the calendar year 2024 and an overweight to Australian Listed Property, all of which screened amongst the most under-valued markets in the universe which we monitor. Early in the month we took profit on our long-held Topix overweight, which had made a small positive contribution over its lifetime, as the rising price and deteriorating fundamentals converged such that the investment was no longer attractive. Early in June we added overweights to India's Nifty 50 and Mexico's Bolsa indices as they had become attractively cheap. Later in the month the Dow Jones Index moved into very expensive territory, at which time we initiated a short position. Our trend models held underweight equities in S&P/ASX-200 and STOXX® Europe 600 ESG-X futures and overweight S&P-500 during June, closing the short positions at the end of the month.

In fixed income, the portfolio was directionally neutral with modest overweights in Australian and Canadian 10-year bonds offset by an underweight in US 10-year Notes, with trend-driven long positions offset in aggregate by valuation-based underweights. We continue to hold an Australian "curve flattener" in which hold a long position in 10-year bond futures, combined with a larger notional short position in 3-year bond futures. The interest rate exposure of the long and short positions are equal and opposite and so neutralise one another if the yield curve moves up and down in a parallel fashion, however we forecast that the slope of the yield curve will fall (i.e. the difference between 3- and 10-year yields will narrow) in time, and importantly the position earns carry returns while we wait for this to happen.

In alternatives, the portfolio was long gold and short copper, both of which rose over the course of the month. Our models reduced the size of the short position in copper at the end of the month and gold moved to square due to offsetting signals between price and futures-basis momentum (i.e. the movement in the shape of the futures term structure). A 1-day drop in the S&P-500 of more than 5% caused a brief spike in S&P realised and implied volatility during the month resulting in our VIX positioning switching from short to long before turning short again.

Our active positioning at the start of July is slightly risk-on. The portfolio is positioned with overweights in several under-valued equity markets plus an overweight to S&P-500 in equity trend-following, partially offset by an underweight in Dow Jones. Fixed income positions are all relative value in nature and we hold small short positions in copper and VIX.

## Market outlook

The economic rebound as restrictions roll off has generally beaten expectations. Coupled with supportive data and strong policy support, it has driven a rapid bounce in equity markets.

While second wave clusters in China and Germany appear to have been contained, cases continue to rise in the US. This in itself is not causing economic issues at this point. However the fear is that we will see a re-run of March/April, with cases leading to stress on hospitals and ICUs and a surge in mortality. This would likely be a material setback for market sentiment and confidence.

As China and Germany have demonstrated, a replay of April - in terms of case-loads, hospitalisations and mortality – is not a foregone conclusion. Today's situation is different from then in several important ways.

1. The outbreaks are in less densely populated areas than New York.
2. The age profile of new cases is a lot lower this time – an average of 20 years younger.
3. There is substantially more testing. This may result in worse-looking numbers but does mean that the problem is being identified earlier than in April.
4. There is more physical distancing and use of face masks – despite well-publicised incidents to the contrary.

5. Knowledge of how to treat the virus is far better now. Previously, treatment had focused on the lungs, which are now believed to be more symptomatic in nature. Instead, treatment is now focused more on anti-inflammatories, with better outcomes as a result.

If the US is able to successfully deal with this wave without reimposing broad-based restriction or a severe spike in mortality, then it should bolster market confidence. Nevertheless, this issue comes with material risk for sentiment and potential consequences for markets in the near term.

While we remain watchful on this issue, at this point we do not expect that recent weakness will morph into a second sharp drop in markets. We are mindful that:

1. We believe that sufficient measures are being - or will be taken - to avoid the resurgence in US cases from triggering material new shutdowns, which would see a large hit to confidence. However, this remains a key risk.
2. The Victorian outbreak should be containable and - while delaying border re-opening - does not represent a significant deterioration in the economic outlook.
3. The current case rise will likely cement the need for more policy stimulus in US and Australia.
4. Economic momentum is still positive.
5. Significant liquidity remains on the sidelines in cash, which can support equity markets.

That said, we do expect the current period of consolidation to continue as the rate of improvement in economic data is likely to slow down, the market's short term positioning remains bullish, and policy news flow is in a lull to the end of July.

At this point it appears the worst case scenario has been avoided and that Australia has been reasonably successful in suppressing Covid-19, paving the way to a resumption in domestic economic activity.

However there will be divergences between industries in terms of the degree to which they recover. Some will only partially recover, while others may get back to previous capacity – or more – in relatively quick time. The uncertainty here – and mis-pricing that results – coupled with the divergence in responses to the crisis at a company level, is driving material opportunity for active management.

## **Regnan Sustainability Snapshots#**

### **CSR Limited (CSR)**

CSR manufactures and distributes building products, including bricks, plaster, tiles, insulation and glass, for residential and commercial construction in Australia and New Zealand.

Key ESG issues relate to opportunities in sustainable buildings, management of human capital, and risks from energy prices and management of legacy asbestos liabilities.

In FY19, over 75% of employees completed the two-yearly Organisational Cultural Inventory / Effectiveness Inventory which CSR argues helps drive cultural improvements across the organisation. Safety management has been enhanced with the adoption of a system in 2018 to proactively identify and eliminate unsafe practices. The company acknowledges the link between deterioration in mental health and increased safety incidents, and in response is developing programs to support good mental health. As a result of these programs, since FY15, TRIFR has fallen 22% and LTIFR 7%. Diversity performance continues to show improvement, with women now comprising 21% of the workforce (up from 18% in FY18) and 50% of the board. Objectives are in place to improve diversity that cover pay, recruitment and career planning.

In contrast to sector peer James Hardie (JHX), CSR has internally managed asbestos liabilities, and has not been subject to the same degree of negative publicity. CSR does not face the same commitments to make a defined contribution (as with JHX's 35% of free cash flow), and as such has greater flexibility than JHX in how it handles liabilities. CSR provides good disclosure of liability estimation and claims received and settled.

CSR has adopted the TCFD recommendations and undertaken scenario analysis for its largest business, Gyprock. Overall, the company has performed well against its four 2020 environmental targets, exceeding waste production and emissions, but falling slightly short of energy and water consumption objectives. New environmental targets are being set for 2030. Product innovations increasingly reflect sustainable building trends by improving, for example, recycled content and acoustic comfort.

### **Cleanaway Waste Management Limited (CWY)**

CWY provides waste management, industrial and environmental services. It is Australia's largest waste, recycling, industrial and liquids service provider with a network of facilities, transfer stations, engineered landfills, liquid treatment plants and refineries across the country.

Key ESG issues include workplace health and safety, management of human capital, and environmental management.

Strong safety performance continued in FY19 with TRIFR down 8.1% from FY18 and an overall 78.6% reduction since FY12. In Regnan's view, these metrics are proof of the effectiveness of a focus shift towards the quality leading safety indicators such as safety leadership, inspections and verifying corrective actions.

Lessons learned from the annual Workplace Gender Equality Agency (WGEA) report are being implemented via programs to increase female representation at senior levels, with a particular emphasis on promoting from within, and new programs to improve the attraction and retention of high potential female employees. Metrics suggest programs are proving to be effective, with women in management roles increasing to 20% from 18% the previous year.

CWY's management of GHG emissions focus is on landfill gas capture systems and improving the efficiency of heavy vehicles, including the introduction of electric vehicles, demonstrating efforts to address emissions. CWY offers customers a waste assessment service to drive improvements in diversion and achieve waste reduction and resource efficiency goals.

<sup>#</sup>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](http://pendalgroup.com)

**PENDAL**

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If market movements, cash flows or changes in the nature of an investment (e.g. a change in credit rating) cause the Fund to exceed any of the investment ranges or limits specified, this will be rectified by PFSL as soon as reasonably practicable after becoming aware of it. If PFSL does so, it will have no other obligations in relation to these circumstances. The procedures, investment ranges, benchmarks and limits specified are accurate as at the date of this factsheet and PFSL reserves the right to vary these from time to time.