PENDAL

Factsheet

Multi-Asset Strategies

July 2020

Pendal Sustainable Conservative Fund

ARSN: 090 651 924

About the Fund

The Pendal Sustainable Conservative 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 real return over inflation over the medium term to meet the objectives of conservative investors including tax exempt entities whilst screening for investments which meet the Fund's sustainable guidelines. The suggested investment timeframe is three 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.

Fixed interest securities issued by Government related entities are generally considered to meet the Fund's sustainable and ethical investment guidelines.

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 asset allocation 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-Conservative-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 RESPONSIBLE INVESTMENT ®
CERTIFIED BY RIAA

The Pendal Sustainable Conservative 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

(%)	Total Returns (post-fee)	Total Returns (pre-fee)	Benchmark Return
1 month	0.55	0.61	0.47
3 months	1.79	1.97	2.00
6 months	-2.42	-2.08	-1.61
1 year (pa)	0.02	0.74	1.09
2 years (pa)	2.45	3.29	4.32
3 years (pa)	3.07	3.94	4.67
5 years (pa)	2.71	3.60	4.13

Asset allocation (as at 31 July 2020)

Australian shares	9.9%
International shares	11.7%
Australian fixed interest	17.6%
International fixed interest	18.8%
Australian property securities	3.5%
International property securities	1.5%
Alternative investments	15.5%
Cash	21.5%

Investment Guidelines

Asset allocation ranges (%)	Neutral Position	Ranges Min	Ranges Max
Australian shares	10	0	20
International shares	10	0	20
Australian fixed interest	18	10	40
International fixed interest	18	10	40
Australian property securities	3	0	10
International property securities	1	0	10
Alternative investments	15	0	20
Cash	25	0	40

Other Information

Fund size (as at 31 Jul 2020)	$318 million
Date of inception	September 1989
Minimum investment	$25,000
Buy-sell spread[2] For the Fund's current buy-sell spread information, visit www.pendalgroup.com	
Distribution frequency	Quarterly
APIR code	RFA0811AU

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]	0.70% pa
Estimated indirect costs[5]	0.05% pa

3 You should refer to the latest Product Disclosure Statement 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.
- **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

Performance of the S&P/ASX 300 Accumulation index (+0.6%) was somewhat muted in July. Whilst Resources (+4.5%) continued to gain on the back of the elevated iron ore and gold prices; Industrials (-0.4%) offset these gains. The development of a viable vaccine remains the most important medium term issue for both the economy and markets.

Sector performance was divergent over the month. Materials (+5.9%), Information Technology (+4.8%) and Communication Services (+3.5%) recorded the largest gains; whereas Energy (-6.3%), Healthcare (-3.8%) and Industrials (-3.8%) finished the period in the red. The gold price continued to edge higher on the back of geopolitical uncertainty around China-US relations; as well as the emergence of negative real yield – the precious metal acts like a two-way hedge against any risk-off events or an unexpected spike in inflation. As such, gold miners (+10.7%) led the gainers within Materials. Similarly, iron ore miners, including BHP (+2.6%), Rio Tinto (RIO, +4.1%) and Fortescue Metals (FMG, +25.7%) also outperformed as demand for iron ore remains strong from China. In particular, FMG provided its quarterly update for 4QFY20, where both production shipment and costs beat market expectations. Management also provided guidance for FY21, with 175-180Mt shipments, and C1 costs of US$13-13.5/wmt. Capital expenditure is expected to come in at US$3.0 - US$3.4b, including investment in growth projects and energy infrastructure.

Global equity markets recorded another solid rise in July. Materials (7.3%), Consumer Discretionary (7.2%) and Utilities (6.9%) outperformed, while Energy (-3.8%), Financials (2.4%) and Industrials (3.4%) underperformed. Continuing from a strong June, EM delivered another strong month of returns, outperforming DM by 374bp. Multiple factors contributed to the region's outperformance, with strong virus containment, rallying commodities key elements and a weaker USD. July saw the continuation of strength for the AUD, following the currency's third-best quarter since 2000 in 2Q20. The AUD gained 3.5% during the month, and broke through 0.70 mid-July, diminishing returns to Australian investors.

In the US market, the Nasdaq rose 6.8% in local currency terms, as the broader S&P 500 also rose (5.5%). Across Europe, the German DAX (4.9%) and the UK FTSE100 (1.2%) markets climbed. While Asian markets also rose in July with the MSCI Asia ex-Japan index returning 8.6% in US dollar terms, Japan had a weak month as the Nikkei fell -0.8% in US dollar terms.

July saw infection rates increase sharply across large swathes of the US, as well as in Japan, Spain, Hong Kong, Australia. Global cases are closing in on the 18m mark, with the US approaching 5m cases and Brazil near 3m. However, the only countries to see a meaningful rise above the lows in new cases in May are the US, Spain, Japan and Australia, suggesting that many countries are managing to reopen without triggering fresh outbreaks

Gold prices surged US$196.8/oz to a record high of US$1,964.90/oz. Three factors have combined in recent months to launch gold to an all-time high: negative real yields across the entirety of the US curve; a faltering USD and an element of safe-haven seeking.

Fund performance

The Fund outperformed the benchmark over the month of July.

Active positioning contributed positively to returns in July. Portfolios started the month 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 held small short positions in copper and VIX.

In equities, our active positioning driven by valuation insights held modest overweight positions in UK's FTSE 100, India's Nifty 50 and Mexico's Bolsa, 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 added an option strategy to hedge possible downside in Australian equities which consists of buying a put spread, funded by selling an out-of-the money call option, all with an expiry in December: beyond the US presidential election and the associated event risk. Attractive features of this hedging strategy are that the net premium cost was approximately zero and that the strike price of the sold call option is where we would be reducing exposure to Australian equities on a valuation basis. In mid-July we increased our exposure to the Mexican equity market and added a new overweight to hedged global listed property. Our trend-following process held overweights to STOXX Europe 600 ESG-X and S&P-500 during July.

In fixed income, the portfolio was directionally neutral with a modest overweight in Canadian 10-year bonds offset by an underweight in US 10-year Notes, as our trend-driven long positions remain offset in aggregate by valuation-based underweights. We took profit on part of the Australian "curve flattener" which holds a long position in 10-year bond futures combined with a larger notional short position in 3-year bond futures.

In alternatives the portfolio was short VIX and copper which added value in aggregate. The copper position was closed at the end of the month.

Our active positioning at the start of August is more risk-on. The portfolio is positioned with overweights in a range of under-valued equity markets plus an overweight to S&P-500 and STOXX Europe 600 ESG-X in equity trend-following, partially offset by an underweight in Dow Jones and meaningfully protected via options. Fixed income positions are all relative value in nature and we hold small short positions in VIX.

Market Outlook

July saw the swift spread of the second wave of Covid-19 infections in the US and an outbreak in Victoria which has led to a reinstated lockdown. This has derailed the view the more optimistic expectations for the economic outlook, as it seems that the virus - and the restrictions to curtail it - will have a social and economic impact for longer than some might have expected a few months ago.

Despite this, markets have managed to hold up reasonably well.

There have been two key reasons for this. The first is the nature of the second wave. In the US, case load numbers have more than doubled from the previous peak in April but hospitalisation rates only reached the same peak levels. This suggests under-reported levels of cases in April, but also the current skew towards cases among younger age cohorts.

Mortality rates, while still tragic, have been much better than in April – around half the previous peak. This is again down in part to the age skew – but also to the broader geographical spread, which has allowed hospitals to cope better, as well as a better understanding of how to treat the virus

All three rates have declined in the last couple of weeks as the health situation shows signs of improvement. Looking forward, we expect to see a Swedish-style outcome in the US, where cases remain persistently high but as long as people are confident that it won't lead to a third major surge and acute cases are being managed better, then activity will start ramping up again, supporting markets.

This is different to Australia, where reinstatement of the lockdown in Victoria demonstrates that authorities are prepared to accept more near-term economic damage in order to achieve effective elimination. This should ultimately allow a larger part of the economy to return to normal.

The Victorian lockdown is likely to take several weeks to show effects, although at this point there is little reason to fear that it won't succeed based on prior experience. Small outbreaks in NSW bear watching – but at this point swift identification and contact tracing are helping the state "hold the line" in terms of overall cases.

The second key factor supporting the markets is the ongoing scale of policy response.

In Australia the Federal government extended support packages and emphasised the point that it intends to absorb as much of the economic impact of the virus as possible. This was echoed by comments from the RBA, which said that the social costs and degradation from recession and persistent unemployment are too high to allow the normal clearing mechanism of labour and capital markets. Instead, policy makers must do everything in their power to mitigate the effects of this crisis.

This shift in thinking away from a more free market approach may be driven by considerations around the social effects of income inequality and/or by a view that labour markets are too rigid to react in a timely fashion to a shock of this nature. Regardless, it suggests that policy makers will continue to shore up growth, which is helping support markets.

In the US, there is some risk around the negotiations of the next tranche of fiscal support. Resolution is expected, however a prolonged delay could start to hurt market sentiment.

One important aspect of policy support is that much of it is designed to support the economy until a vaccine is available which can help normalise economic activity. The development of a viable vaccine remains the most important medium term issue for both the economy and markets.

Recent trials remain encouraging, however the widespread delivery of an effective vaccine is still not expected until some time in 2021.

Regnan Sustainability Snapshots[#]

Downer EDI Limited (DOW)

Downer EDI engages in the provision of integrated services. It operates business segments including transport, utilities, rail, engineering, construction, maintenance, mining services, and Spotless.

Key ESG issues relate to workplace health and safety and management of human capital across DOW's diverse range of businesses, and management of environmental impacts, including energy use and emissions intensity.

The company has improved metrics related to human capital management, supportive of the expansion of service offerings. For example, employee engagement score has risen to 72%, an improvement of 3% from prior year, employee progress score has risen by 4% to 65%, while females in management roles has increased by 5% to 22%. Workplace health and safety metrics have also improved, with both Lost Time Injury Frequency Rate and Total Recordable Injury Frequency Rate falling significantly in 2019. The company did not record any fatalities and reduced the occurrence of high potential incidents by 33% compared to prior year. DOW reports that 1123 employees participated in its internal mental heal first aid program during the year.

DOW has also managed to reduce its environmental impact in the most recent year. Greenhouse gas emissions intensity declined to 32.9 ktCO2-e/$m, a 9% decline from the prior year, while energy intensity also fell 9%. Renewable energy consumption increased 145% to 5266 GJ. The company did not record any significant environmental incidents and has not recorded an environmental prosecution over the last three years.

Fortescue Metals Group Limited (FMG)

FMG is an Australian based iron ore miner focused on the Pilbara Region of WA where its larger peers Rio Tinto and BHP also have the bulk of their iron ore operations.

Key ESG issues include management of a predominantly fly-in fly out workforce (with additional challenges currently due to Covid), host community relations, and the impacts of climate change on its geographically concentrated operations.

Most of FMG's iron ore is consumed alongside large amounts of coal in steel making. The resulting high emissions of FMG's customers could present risks to future demand for its iron ore under a carbon constrained future, especially if alternative products or steel making technologies emerge. Positively, FMG has turned its attention to the emergent technologies for green hydrogen production – hydrogen suits the company's own operations (it can be used as a fuel for mining machinery and shipping) as well as having potential to displace coal in steel making and reduce its customers' emissions.

The company also recently set ambitious climate change targets for its direct (scope 1 and 2) emissions of net zero by 2040 (with an interim target of 26% reduction by 2030) and is pursuing reductions through renewable energy projects, battery storage, and more efficient mobile fleets.

The company has adopted a leadership position on modern slavery and indigenous employment. However, FMG's singular focus on jobs, and aversion to direct compensation (oft described by the company as "a hand up, not a hand out") has brought the company into conflict with the host community at its strategically significant Solomon Hub operations, nor has it been immune from concerns about cultural heritage protection.

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

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[#] 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.

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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.