Pendal Dynamic Income Fund

ARSN: 622 750 734

Factsheet

Bond, Income & Defensive Strategies

August 2020

About the Fund

The Pendal Dynamic Income Fund (**Fund**) is an actively managed portfolio of fixed income securities, Australian and global credit indices and emerging market sovereign issuers.

Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes) that exceeds the RBA Cash Rate by 2-3% p.a. over the medium term. The suggested investment timeframe is three years or more.

Description of Fund

The Fund is designed for investors who seek income from a portfolio of fixed income securities across a range of market conditions and are prepared to accept some variability of returns.

The Fund is an actively managed portfolio that invests primarily in Australian issued investment grade corporate bonds#. The Fund may also invest in Australian and global credit indices and emerging market sovereign issuers to provide portfolio diversification and enhance returns when we believe market conditions are supportive. The Fund also has the ability to decrease its allocation to credit and invest in cash and interest rate duration strategies when we expect volatility to increase.

Pendal uses a combination of quantitative modelling and qualitative research to construct the Fund's portfolio.

The Fund's portfolio is constructed using the following three step approach:

1. Generate investment themes through quantitative models
2. Reaffirm investment themes with qualitative research
3. Asset Allocation

Investment Team

Pendal's Bond, Income & Defensive team comprises thirteen dedicated investment professionals with both global and domestic experience, invested across Income, Composite, Pure Alpha, Global and Australian Government strategies. The team also draws on a wide range of knowledge resources including Pendal's other specialist investment teams: Equity and Multi-Asset.

The Fund is managed by Vimal Gor, Head of Bond, Income & Defensive Strategies who has more than 24 years industry experience and 9 years at Pendal.

Other Information

Fund size (as at 31 Aug 2020)	$90 million
Date of inception	December 2017
Minimum investment	$25,000
Buy-sell spread[1] For the Fund's current buy-sell spread information, visit www.pendalgroup.com	
Distribution frequency	Quarterly
APIR code	BTA8657AU

[1] The buy-sell spread represents transaction costs incurred whenever you invest or withdraw funds, and may vary from time to time without notice.

Performance

(%)	Total Returns (post-fee)	(pre-fee)	Benchmark Return
1 month	0.39	0.44	0.02
3 months	2.34	2.48	0.06
6 months	-1.24	-0.96	0.14
1 year (pa)	1.00	1.56	0.54
2 years (pa)	3.32	3.77	0.97
Since Inception (pa)	2.96	3.36	1.11

Asset Allocation (as at 31 August 2020)

Australian Credit	85.2%
Emerging Market Credit	23.7%
Cash	15.1%

Allocations may not add to 100% due to the use of derivatives to obtain credit exposure.

Top 10 Issuer Exposure

Macquarie Bank Limited	7.3%
National Australia Bank	4.2%
Ausgrid Finance Pty Ltd	4.1%
Connecteast Finance Pty Ltd	4.0%
Pacific National Finance	3.9%
Ausnet Services	3.7%
Brisbane Airport Corporation Ltd	3.5%
Wso Fin Westlink M7	3.4%
Toronto-Dominion Bank	3.3%
Anz Banking Group Limited	2.9%

Key Fund Metrics

Average Australian Credit Rating	A

Portfolio Characteristics

Benchmark	RBA Cash rate
Liquidity	Daily

Management Costs[2]

Issuer fee[3]	0.55% p.a.

[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.

#Corporate bonds held within the Fund are required to be rated investment grade at the time of investment. Downgraded securities can continue to be held up to 15% of the Fund (in aggregate). Investment grade bonds refer to securities that are expected to have a high probability of payment of interest and repayment of principal.

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 security.
- **International investments risk** – The risk arising from political and economic uncertainties, interest rate movements and differences in regulatory supervision associated with international investments.
- **Interest rate duration 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.
- **Emerging markets risk** – The risk of asset price volatility and higher currency, default and liquidity risk from investments in emerging markets
- **Liquidity risk -** The risk that an asset may not be converted to cash in a timely manner.
- **Derivatives risk** – The risks arising from use of derivatives to manage exposures to investment markets.
- **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

Credit markets continued to strengthen in August. Drivers of the strength came from stronger than expected US economic data (manufacturing, payrolls & CPI), progress on Covid-19 vaccines, and finally better than expected earnings results out of the US and Europe, offset by weaker Australian results.

Supporting risk markets were positive test updates on Covid-19 vaccines from a number of pharma companies, two of which were from Novovax and Moderna. The results showing positive immunity responses. Also the approval of the Abbott Labs rapid antigen Covid test is a positive for markets as it supports going back to work and education sooner. It provides a quick 15 minute result at a very cheap price of $5 with accuracy in the high 90% range. Finally the lower daily new cases for coronavirus in the US also help sentiment, from 67 thousand as at the end of July to 34 thousand by the end of August. The virus hospitalizations also fell in US.

Second quarter US company earnings saw 84% of businesses beating expectations by 23% on average, with actual earnings only falling 7% vs the previous corresponding period. European companies also surpassed expectations by 34% with earnings falling 19% pcp. On the flip side the ASX200 underwhelmed with company earning falling 24% pcp.

The Australian iTraxx index (Series 33 contract) traded in an 13bp range finishing the month 12bps tighter to +64bps. Physical credit spreads also narrowed, on average tightening 5bps for the month. The best performing sectors were telcos, industrials and resources narrowing 14, 11 & 11bps respectively, whilst the worst performing sector was reits that only tightened 1bp. Semi-government bonds had a very strong month tightening 11bps to commonwealth government bonds.

Fund performance

The Fund returned 0.44% (pre-fee), which was an outperformance of 0.42% versus the benchmark.

Driving the returns were continued positive returns for both EM and Australian Physical credit over August, although somewhat moderated compared to the rally in July. Offsetting this was small negative returns from both the US and Australian rates positions. EM Sovereign bonds returns over 0.5% for the month continuing their recent strong run of performance after spreads widened during the volatility of March and April as liquidity has started to find its way to higher yielding markets like EM. With a weaker US dollar, rising commodity prices and stronger GDP growth out of China also continued

In Australian credit markets, the BBB sector outperformed and within that infrastructure and utlilties did well. The fund continued to benefit from its exposure to infrastructure given its strong comparative accrual. Infrastructure bonds are increasingly buoyed by increased information provided to the market on their liquidity and operations whilst also gaining a bid from optimistic expectations on lock-downs dissipating.

Over the month the Bloomberg Credit Index tightened 11bp on a spread-to-swap basis. Building on the contraction in May, the month of June saw both the Infrastructure and Utilities sectors spread rally in the mid-teens, outpacing many of the other sectors. Real estate continued to underperform in July as investors retail outlook diminished as government COVID infection rates appeared to bloom in Victoria. The month end state of Disaster in Victoria will have a chilling effect on retail sales as restrictions are enacted. There will also be a negative impact on toll roads and Melbourne Airport activity. The portfolio has relatively limited direct infrastructure exposure in Victoria, amounting to under 5% of the portfolio and the majority of this being the Port of Melbourne which has been relatively unscathed from the negative impacts of COVID.

Outlook

We continue to have a constructive stance on credit markets given the 'whatever it takes' mantra by global Central Banks and governments. Further, companies across the globe have actively moved to shore up their credit quality by raising equity to support their balance sheets while also paring back operating and capital costs.

There are also some technical dynamics that will continue to support credit markets in Australia. These include the excess liquidity in the banking system and wider credit spreads against a 0.25% cash rate is attracting buyers.

The continued positive news on vaccine candidates eliciting positive trial results is suggestive there is an end date for our temporary hermit style lifestyles and a resumption of normal economic activity in the next few years.

However, we still have concerns around the uncertainty related to the flow on effect to the global economy and company earnings of Covid-19. Obviously in the wash of the pandemic there will be unintended consequences to monetary and fiscal government responses and we will continue to closely scrutinise developments and assess the potential ramifications as they occur. We are also focused on the US-China tensions on the follow on effect of global trade. Over the longer-term, policy measures should be supportive for risk assets which leaves us with a constructive stance on credit markets.

After a strong rally since April in Emerging market bond yields and with increased volatility within equity markets especially the more growth orientated tech stocks a period of consolidation is to be expected. On the positive side is continued impressive growth coming out of China and parts of Asia, combined with a weaker dollar. Offsetting this is increasing geo-political risks with US election, messy brexit as well as simmaring US/China tensions.

As we have reiterated before whilst EM spreads today look less of a slam-dunk than three months ago, the arguments for having a manageable EM allocation in portfolios have not changed. These include the diversification benefits that sovereign credit brings to most portfolios that are corporate risk-heavy. Also, bear in mind that very wide spreads only ever look attractive through the rear view mirror. What's more important going forward is that even at lower spreads than prior months, EM sovereigns as an asset class may present a higher Sharpe in future returns.

As central banks globally push bond yields even lower with new expectations for some to head into negative territory for the first time, the search for yield will continue to see demand for EM Sovereign bonds hold up and place a bid for lower yields.

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