# Factsheet

Bond, Income & Defensive Strategies

October 2020

# Pendal Short Term Income Securities Fund

ARSN: 088 863 469

## About the Fund

The Pendal Short Term Income Securities Fund (**Fund**) is an actively managed portfolio of primarily Australian cash and fixed interest securities. The Fund invests in a combination of short-term money market instruments and medium-term floating and fixed rate securities.

The Fund invests in short-term and medium-term securities that are investment grade[1]. Duration is managed in a range of +/- 0.5 year around the index.

### Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes) that exceeds the Bloomberg AusBond Bank Bill Index. The recommended investment time frame is 12 months or more.

### Investment Approach

The Fund aims to add value through active management by exploiting market inefficiencies through the shape of the money market curve and the mispricing of credit securities. Research is focused on assessing economic factors, the likely direction of interest rates and credit analysis. Credit margin relative value is assessed with reference to rating, sector, maturity, liquidity and underlying credit fundamentals.

### Investment Team

Pendal's Bond, Income & Defensive team includes fifteen dedicated investment professionals. The team also draws on a wide range of knowledge resources including Pendal's other specialist investment teams: Equity and Multi-Asset. The portfolio manager of the Fund is George Bishay, who has more than 26 years industry experience.

### Portfolio Characteristics

| | |
|---|---|
| Weighted average maturity | +/- 0.5 years around the index |
| Minimum credit rating | Investment Grade |
| Liquidity | Following day access (before 2.30pm) |

### Portfolio Statistics (as at 31 October 2020)

| | |
|---|---|
| Yield to Maturity[2] | 0.68% |
| Modified duration | 0.17 years |

[2] The portfolio yield to maturity is an estimate of the fund's internal rate of return. It is calculated as the yield to maturity of all securities comprised in the benchmark at the relevant time (sourced from Bloomberg), plus our estimate of the weighted average traded margin over the swap rate for each of those securities based on observed market prices. The portfolio yield to maturity does not represent the actual return of the fund over any period.

### Management Costs[3]

| | |
|---|---|
| Issuer fee[4] | 0.25% 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.

### Performance

| (%) | Total Returns (post-fee) | Total Returns (pre-fee) | Benchmark Return |
|---|---|---|---|
| 1 month | 0.28 | 0.30 | 0.01 |
| 3 months | 0.44 | 0.51 | 0.03 |
| FYTD | 0.79 | 0.87 | 0.04 |
| 6 months | 1.33 | 1.46 | 0.05 |
| 1 year (pa) | 1.79 | 2.04 | 0.51 |
| 2 years (pa) | 2.02 | 2.28 | 1.08 |
| 3 years (pa) | 2.14 | 2.39 | 1.35 |
| 5 years (pa) | 2.44 | 2.70 | 1.59 |

Post-fee return is based on management fees deducted from the unit price: currently 0.25% (pa).

### Sector Allocation (as at 31 October 2020)

| | |
|---|---|
| Money market | 29.8% |
| Corporate | 64.9% |
| Residential mortgage backed | 5.3% |
| Government bond | 0.0% |
| Other asset backed securities | 0.0% |

### Security Credit Ratings (as at 31 October 2020)

| | |
|---|---|
| AAA | 8.6% |
| AA | 26.4% |
| A | 21.2% |
| BBB | 14.0% |
| Money market | 29.8% |

### Other Information

| | |
|---|---|
| Fund size (as at 31 Oct 2020) | $785 million |
| Date of inception | January 1994 |
| Minimum investment | $25,000 |
| Buy-sell spread[5]<br>For the Fund's current buy-sell spread information, visit www.pendalgroup.com | |
| Distribution frequency | Quarterly |
| APIR code | WFS0377AU |

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

[1] Investment grade securities refer to securities that are expected to have a high probability of payment of interest and repayment of principal.

**Market review**

The Reserve Bank of Australia (RBA) left the cash rate unchanged at their meeting in early October. They did however indicate that further monetary policy easing might be imminent when they stated that they were considering how additional monetary easing could support jobs as the economy opens up further.

A speech on the 15th October by Governor Lowe, endorsed by the Board, revealed more of the RBA's thinking. The RBA will now be putting a greater weight on actual, not forecast, inflation in their decision-making. In terms of unemployment, the RBA wants to see more than just progress towards full employment. Lowe stated also that the RBA would not increasing the cash rate until actual inflation is sustainably within the target range (2-3%) and that they do not expect to be increasing the cash rate for at least three years.

Third quarter inflation data was released after the speech, showing annual headline, trimmed mean and weighted median inflation rising by 0.7%, 1.2% and 1.3% respectively. Governor Lowe also referenced the additional yield that Australia's 10 year Government bonds trade at relative to other Western countries and whether there would be a benefit in the RBA buying bonds to reduce the yield on those bonds as they try to support Australian jobs. This has paved the way for quantitative easing at the RBA's meeting in early November.

Offshore events were dominated by the upcoming US election and the lack of progress on a fiscal stimulus package. Also weighing on risk markets were increasing COVID19 cases and resultant lockdowns in Europe, Brexit negotiations, US earnings and the trials and tribulations as companies race to find a vaccine. Positive developments occurred with Moderna stating that their vaccine could be available for emergency use in December and AstraZeneca resuming its phase 3 trials in the US.

In the US risk sentiment waxed and waned during the month on fiscal stimulus talks, with no agreement able to be reached prior to the election. The election occurs in early November with Joe Biden favoured to take office from Donald Trump according to the polls. The close Senate race will also be watched as it will impact on the next President's ability to push through fiscal stimulus.

Key economic data out of the US included third quarter GDP, which rose by a better than expected annualised rate of 33.1%. The unemployment rate fell from 8.4% to 7.9%, largely due to the participation rate.

The ECB was more dovish than expected and has signalled that further monetary policy stimulus with occur at their December meeting. ECB President Christine Lagarde outlined a regional economy that was losing momentum and is now facing deeper downside risks, with the ECB to 'recalibrate its instruments' at its next meeting following the release of the ECB's economic projections.

The Bank of England continues to weigh up the case for negative rates. MPC member Vlieghe warned that the banks' ability to stimulate growth was beginning to wane and that negative rates need to be included in the BoE's armoury once technical issues were overcome. BoE Deputy Governor Ramsden stated that whilst there might be an appropriate time to use negative rates, now is not the time.

Risk sentiment, particularly in Europe, suffered as the number of COVID cases rose sharply and led to restrictions in Spain, Italy, Germany, France and the UK amongst others. German equities were down by almost 10% over the month, with software maker SAP falling 22% in one session on a disappointing outlook for the company. In the United States the S&P 500 fell by 2.8%, China's Shanghai Composite was little changed and in Australia, the S&P/ASX 200 ended 1.9% higher.

Australian yields ended marginally lower on the month as US yields drifted higher and markets became largely priced for the potential RBA moves in November. US treasury yields sold off late in the month despite the sharp fall in US equity markets with the 10 year bond yield ending 19 basis points higher at 0.87%. However, German 10 year yields fell by 11 basis points to -0.63%.

Credit markets had a strong month in October. We saw a firm start to the month on an expectation of an uncontested Biden win in the US elections with control of the Senate which would allow a large fiscal stimulus package to be passed.

In local news, a landmark change announced in a speech by the RBA's Governor Lowe, talking to the RBA shifting its focus from forecast to actual inflation with a focus on keeping the Australian dollar in check and supporting financial stability and economic growth. This suggests that future rate hikes would be pushed out further than before. This is very supportive for credit markets in Australia as lower rates for longer will see investors continue to allocate to yielding credit securities.

However, risk markets lost momentum in the second half of the month on the back of rising Coronavirus cases, lack of US stimulus talks and increasing concern over the risk of a tighter US election outcome. The increase in new covid-19 cases in European and US pressured risk markets; this saw lockdown announcements from France, Germany and England to try to reduce the spread of the virus thereby stalling their economic recovery. In addition, the lack of breakthrough on US stimulus talks and a potential contested US election result drove whippy markets late in the month.

The Australian iTraxx index (Series 34 contract) traded in at 12p range finishing the month 5bps tighter to +71bps. Physical credit spreads had a strong month narrowing 7bps on average. The best performing sectors were industrials and domestic banks tightening 10 and 9bps respectively, whilst the worst performing sector was offshore banks that only narrowed 5bps. Semi-government bonds performed well narrowing 4bps to commonwealth government bonds.

**Fund performance and activity**

The Fund had a strong month in October outperforming the benchmark by 0.29% (pre-fee). Financials and industrials drove the performance.

As at the end of the month, the portfolio had a credit spread of 59bps over bank bills, interest rate duration of 0.17 years and credit spread duration of 2.11 years.

**Outlook**

The Reserve Bank of Australia (RBA) eased monetary policy further in early November, cutting the cash rate, term funding facility and yield curve control by 0.15% to 0.10%. In addition, the RBA announced quantitative easing, purchasing $100bn of government and semi government bonds over the next 6 months.

The RBA governor Philip Lowe held a press conference following their decision. In the Q&A session, he mentioned that 0.10% is the effective lower bound and there is little appetite to go into negative territory. He also stated that if major central banks went into negative territory, then it is something that the RBA would have to consider. The Reserve Bank of New Zealand and Bank of England are preparing for a move into negative rates. Those central banks moving will not be enough to see the RBA join the negative interest rate policy club. The actions of the Federal Reserve in the US will be the more likely catalyst for the RBA to cut the rate further. The RBA are clearly concerned about financial stability risks associated with an elevated unemployment rate. They have stated that they will not be increasing the cash rate until full employment is reached and actual inflation is sustainably within their 2-3% target band. That is something that won't be happening anytime soon.

We maintain our positive view on investment grade credit on the back of the exceptional support measures by global central banks and governments. Companies across the globe are supporting their balance sheets and improving their credit quality through raising equity, which is positive from a fundamental credit perspective.

The excess liquidity in the Australian banking system and wide credit spreads against a very low cash rate will continue to attract buyers to the sector supporting credit markets.

We still have concerns around Covid-19 and the uncertainty related to the flow on effects to the global economy and company earnings. However, we believe a more educated/experienced global community will better manage mortality rates, which will ultimately support markets. We will continue to closely scrutinise developments and assess the potential ramifications as they occur.

We are also focused on the US elections and the potential impact on markets as well as US-China tensions and the follow on effect of global trade. However, over the medium to longer term, policy measures should be supportive for risk assets which leaves us with a constructive stance on credit markets.

**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 asset.
- **Interest rate 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.
- **Liquidity risk -** The risk that an asset may not be converted to cash in a timely manner.
- **Valuation risk -** The risk that the value of an investment in a less active or liquid market is lower than what is reflected in the Fund's unit price.

Please read the Fund's Product Disclosure Statement (**PDS**) for a detailed explanation of each of these risks.

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

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