PENDAL

Pendal Monthly Commentary

Pendal Australian Tax Effective Income Portfolio

November 2020

Market commentary

The S&P/ASX 300 posted its best month since 1988 in November – a gain of 10.2%.

Good news on the vaccine front – coupled with the prospect of a more predictable policy environment and a reasonable earnings season in the US – drove improvement in sentiment.

Investors seemed content to look through the latest Covid surge in the northern hemisphere and the risk of further lockdowns.

Resources (+10.7%) rebounded strongly for the month and marginally outperformed Industrials (+10.1%) as confidence in the economic recovery continued to drive commodity price gains.

Copper was up 11.7% and is well above pre-Covid levels. Brent Crude gained 29% for the month. Gold fell 4.9% as investors saw reduced need for portfolio insurance.

There was something of a catch-up trade in November – stocks and sectors that have generally lagged this year did well.

Energy (+28.2%) was the best-performing sector, driven by a rebound in the oil price.

Financials (+16.1%) were also strong. Updates from the major banks suggested bad and doubtful debts were tracking towards the more benign end of expectations, leaving capital in a strong position. Margins remain under pressure from low rates and strong competition, but all in all the updates were well received.

The more defensive sectors generally underperformed.

Consumer staples (-0.66%) was the only sector to go backwards, experiencing the twin impacts of a rotation away from defensives and a hit to Treasury Wines (TWE, -6.3%) as China imposed tariffs on Australian wine.

Utilities (+1.5%) and Health Care (+2.9%) lagged the market.

Technology growth stocks were generally muted.

The sector rose 4.1% but the portfolio's preferred position, Xero (XRO), was up 20.3% following a good result.

Subscriber growth in Xero's more mature markets of Australia and New Zealand suggest a post-Covid shift in mentality towards the importance of cloud-based administration for businesses.

Portfolio overview

Australian Tax Effective Portfolio	
Investment strategy	**Dual focus:** Deliver tax-effective capital & grossed-up income. **Broad hunting ground:** Core approach, drawing ideas from across the market cap spectrum. **Income focus:** Greater exposure to stocks with high grossed-up yield & dividend sustainability.
Investment objective	The objective of the Model Portfolio is to outperform the S&P/ASX300 (TR) Index on a rolling 3 year period by 3% per annum, while delivering a higher gross yield than the market.
Benchmark	S&P/ASX 300 (TR) Index
Number of stocks	15-35 (30 as at 30 November 2020)
Sector limits	A-REITS 0-30%, Cash 2-10%
Dividend Yield	3.64%[#]

Top 10 holdings

Code	Name	Weight
BHP	BHP Billiton Limited	9.34%
CSL	CSL Limited	8.04%
CBA	Commonwealth Bank of Australia Ltd	7.38%
NEC	Nine Entertainment Co Ltd	5.26%
TLS	Telstra Corporation Limited	5.01%
WBC	Westpac Banking Corporation	4.72%
ANZ	ANZ Banking Group Limited	4.53%
QAN	Qantas Airways Limited	4.17%
MTS	Metcash Trading Limited	3.62%
NAB	National Australia Bank Limited	3.33%

Source: Pendal as at 30 November 2020

Top 5 overweights versus S&P/ASX 300

Code	Name	Weight
NEC	Nine Entertainment Co Ltd	5.08%
QAN	Qantas Airways Limited	3.63%
MTS	Metcash Trading Limited	3.46%
BHP	BHP Billiton Limited	3.37%
TLS	Telstra Corporation Limited	3.06%

Top 5 underweights versus S&P/ASX 300

Code	Name	Weight
WES	Wesfarmers Limited (not held)	-2.99%
WOW	Woolworths Group Limited (not held)	-2.49%
GMG AE	Goodman Group (not held)	-1.66%
COL	Coles Group Limited (not held)	-1.27%
NCM	Newcrest Mining Limited (not held)	-1.17%

Source: Pendal as at 30 November 2020

[#]The Portfolio's dividend yield represents the weighted average 12-month forward-looking dividend yield of the portfolio holdings (excluding cash), as at the date of the Factsheet. Each individual security's dividend yield is calculated using market consensus Dividend Per Share (DPS) before tax and franking credits, collated by Pendal and divided by the closing market price of the security as at the date of the Factsheet. The portfolio dividend yield therefore is only an estimate, and does not reflect the actual returns of the Fund, which will be affected by market movements in the price of individual securities, the returns on other assets such as cash holdings and variances of individual security's actual dividends from the forecasted DPS.

Performance

	1 month	3 month	6 month	1 year	3 Year (p.a.)	5 year (p.a.)	Since Inception (p.a.)*
Pendal Australian Tax Effective Income Portfolio	11.40%	10.27%	15.36%	-0.14%	6.88%	8.79%	9.03%
S&P/ASX 300 (TR) Index	10.23%	8.27%	14.98%	-1.62%	7.05%	9.13%	9.32%
Active return	**1.17%**	**2.00%**	**0.39%**	**1.48%**	**-0.17%**	**-0.34%**	**-0.29%**

Source: Pendal as at 30 November 2020

*Since Inception - 14 September 2015

Performance returns are pre-fee. Investors should contact their platform provider for applicable fee rates.

Past performance is not a reliable indicator of future performance.

Top 5 contributors - monthly

Code	Name	Value Added
QAN	Qantas Airways Limited	0.57%
STO	Santos Limited	0.42%
WOW	*Woolworths Group Limited (not held)*	*0.38%*
MND	Monadelphous Group Limited	0.37%
NCM	*Newcrest Mining Limited (not held)*	*0.25%*

Top 5 detractors - monthly

Code	Name	Value Added
EVN	Evolution Mining Limited	-0.49%
JBH	JB Hi-Fi Limited	-0.45%
MTS	Metcash Trading Limited	-0.39%
WPL	*Woodside Petroleum Limited (not held)*	*-0.17%*
AMC	Amcor Limited	-0.15%

Top 5 contributors - 1 year

Code	Name	Value Added
NEC	Nine Entertainment Co Ltd	1.46%
FMG	Fortescue Metals Group Limited	0.69%
JBH	JB Hi-Fi Limited	0.55%
MTS	Metcash Trading Limited	0.54%
WPL	*Woodside Petroleum Limited (not held)*	*0.53%*

Top 5 detractors - 1 year

Code	Name	Value Added
QAN	Qantas Airways Limited	-1.33%
STO	Santos Limited	-0.81%
APT	*Afterpay Limited (not held)*	*-0.75%*
IAG	Insurance Group Australia	-0.72%
WES	*Wesfarmers Limited (not held)*	*-0.58%*

Source: Pendal as at 30 November 2020

Underweight positions are in italics.

Stock specific drivers of monthly performance relative to benchmark

Three largest contributors

Overweight Qantas (QAN, +28.4%)

An easing of restrictions on interstate travel opened the way for QAN to start ramping up its domestic operations. While QAN has now returned close to its pre-Covid enterprise value, we see the opportunity for further upside with a material beneficial effect on working capital as operations normalise.

Overweight Santos (STO, +30.2%)

The surging oil price proved a strong tailwind for energy producers, including STO – our preferred holding in the space. STO has done a strong job of managing costs over the last few years and through the Covid period. It also has the most attractive portfolio of potential growth opportunities.

Underweight Woolworths (WOW, -3.1%)

Defensive consumer staples companies underperformed, including Woolworths and our preferred position in Metcash (MTS, +0.0%), as investor sentiment improved. We continue to see upside in MTS. Its supermarket is on an improving trajectory after several years of self-help, while its hardware and liquor segments continue to perform well.

Three largest detractors:

Overweight Evolution Mining (EVN, -10.3%)

The gold price sold off as sentiment improved – along with gold miners such as EVN. We still see an important place for gold exposure in the portfolio. It is a hedge against a downturn in sentiment – particularly with the Covid surge in the US and Europe. It could also perform well if we see an environment of negative real interest rates as inflation expectations increase but nominal rate remain low.

Overweight JB Hi-Fi (JBH, -3.6%)

Stocks such as JBH that did well during the Covid period tended to underperform in November as other parts of the market caught up. JBH has done well but remains our preferred retail exposure, given persistent tailwinds for retail spending and its strong competitive position.

Overweight Metcash (MTS, +0.0%)

As investor sentiment improved, defensive consumer staples companies underperformed – including Woolworths and our preferred position in Metcash (MTS, +0.0%). We continue to see upside in MTS. Its supermarket is on an improving trajectory as a result of several years of self-help, while its hardware and liquor segments continue to perform well.

Market outlook

The S&P/ASX 300 gained 10.23% in November – its best monthly return since March 1988. It was also a good month for the portfolio, which outperformed.

While improved sentiment toward US politics and vaccines drove markets, the move was supercharged by two surprises.

First, contrary to consensus expectations, there was no “Blue Wave” of change in US politics. The presidential race was very close and the Senate looks set to remain in Republican hands. This would leave the US with a far more moderate – and market-friendly – government than many expected. That said, we continue to watch the lead up to the Georgia Senate run-off with interest.

Second, on the vaccine front efficacy rates of around 95% reported by Modern and Pfizer were far higher than most expected.

These positive surprises – along with several negative ones which occurred in 2020 – emphasise the importance we place on building a robust portfolio. This has been the bedrock of the portfolio’s performance this year.

Our approach is to has been to keep different types of stocks in the portfolio – positions that could perform under a number of different scenarios. We then use our insight into companies to choose the best stocks to own. These were the companies where we saw relatively limited downside and potential for large upside gains.

Our performance in the market’s plunge was driven by defensive holdings such as Metcash (MTS) and Telstra (TLS); high-quality growth names such as CSL (CSL); and portfolio insurance provided by gold miners such as Evolution (EVN).

Performance in November was driven by a different part of the portfolio – cyclical, recovery-linked exposures such as Qantas (QAN), Santos (STO) and Monadelphous (MND).

At times this year the growth exposure has worked well – for example CSL and Xero (XRO). At other times it was the policy beneficiaries such as Fortescue Mining (FMG), JB Hi-Fi (JBH) and Atlas Arteria (ALX).

We did well as the market recognised the value offered in long-term winners such as Aristocrat (ALL), James Hardie (JHX) and Nine Entertainment (NEC).

The recent strong run may mean we are in for a period of consolidation, though not necessary any sort of material pull-back.

The risk of prolonged recession has receded. Policy-makers remain in the mindset of “whatever it takes” with policy settings supporting the economy and markets.

The world is in a better place than many feared in March. The economic rebound has been strong, helped by a surge in monetary and fiscal policy support. Strong industrial production in the US is helping offset weaker activity in services. Vaccines are on the horizon. The world is getting better at living with the virus and mitigating its economic damage.

Nevertheless, risks remain. The northern hemisphere Covid surge has led to renewed lockdowns and an impact on real-time economic activity. There is a great deal of complexity around the vaccines. How soon and how widespread will they be deployed? How quickly will we return to normal? Geopolitical risk – particularly in the relationship between China and Australia – is higher than usual.

The upshot is that we believe our balanced approach remains as valid now as it did earlier in the year.

New stocks added and/or stocks sold to zero during the month

No new stocks added or stocks sold to zero during the month.

For more information contact your
key account manager or visit **pendalgroup.com**