PENDAL

Factsheet

Equity Strategies

November 2020

Pendal Ethical Share Fund

ARSN: 096 328 219

The future is worth investing in

About the Fund

The Pendal Ethical Share Fund (**Fund**) is an actively managed, high-conviction, values-orientated, concentrated portfolio of Australian shares. It seeks to invest in companies that enable, lead and participate in the transition to a more sustainable Australian economy, while avoiding those which cause significant harm, undermine a more sustainable economy, or that do not meet our minimum environmental, social and governance (ESG) performance standards. The investment process combines the potential to achieve strong performance over the long term through a diversified set of investment opportunities while also investing in companies whose practices and impacts are in our view aligned with an investor's own social, environmental and ethical preferences.

Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes) that exceeds the S&P/ASX 300 (TR) Index over rolling 5 year periods. The suggested investment timeframe is five years or more.

Investment Approach

We adopt a principles-based approach in defining our investment opportunity set. We have a set of exclusionary screens (see PDS for full details) and a framework to identify companies which are aligned with our Fund priorities of supporting a more sustainable, future-ready Australian economy.

We seek companies involved in…

- ✓ Innovation & technological advances (including climate solutions)
- ✓ More sustainable resource consumption
- ✓ Sustainable & resilient infrastructure
- ✓ Quality education
- ✓ Meeting basic needs
- ✓ Health & wellbeing
- ✓ Social inclusion & diversity
- ✓ Low carbon transportation

We avoid companies involved in…

- x Fossil Fuels
- x Tobacco
- x Weapons
- x Alcohol
- x Gambling
- x Animal testing
- x Pornography
- x Predatory lending
- x Logging
- x Uranium

Investment Process

The Fund uses the same investment process as Pendal's flagship Australian equities funds with the additional application of exclusionary screens and a sustainability-focused framework.

1. The negative screening process effectively determines the investment universe of the Pendal Ethical Share Fund.
2. Investment ideas are generated through our proprietary framework, identifying companies which contribute to a more sustainable economy.
3. We construct a portfolio with stocks which we believe will generate alpha and at a minimum 'do-no-harm'.

We also actively undertake targeted engagement with companies to support a more sustainable economy and to ensure ESG risks are being appropriately managed.

Investment Team

Pendal's nineteen member Australian Equities team is one of the largest in the industry. The portfolio manager is Head of Equities, Crispin Murray, assisted by Elise McKay, Oliver Renton and Patrick Teodorowski on the application of the Fund's investment framework.

Performance

(%)	Total Returns (post-fee)	Total Returns (pre-fee)	Benchmark Return
1 month	9.57	9.65	10.23
3 months	9.00	9.26	8.27
FYTD	12.46	12.91	12.25
6 months	13.90	14.45	14.98
1 year (pa)	-0.27	0.69	-1.62
2 years (pa)	11.42	12.48	11.35
3 years (pa)	6.79	7.81	7.06
5 years (pa)	8.21	9.24	9.14

Investment Guidelines

Ex-ante (forward looking) tracking error	3.0% - 8.0%
Min/max stock position	+/-10%
Min/max sector position	+/-10%

Management Costs[1]

Issuer fee[2]	0.95% pa

[1] You should refer to the latest Product Disclosure Statement for full details of fees and other costs you may be charged.

[2] 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.

Other Information

Fund size (as at 30 Nov 2020)	$206 million
Date of inception	May 2001
Minimum investment	$25,000
Buy-sell spread[3]	0.50 (0.25%/0.25%)
Distribution frequency	Quarterly
APIR code	RFA0025AU

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

Signatory of: PRI Principles for Responsible Investment

CERTIFIED RESPONSIBLE INVESTMENT ® CERTIFIED BY RIAA

The Pendal Ethical Share 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.

Sector Allocation (as at 30 November 2020)

Materials	15.1%
Industrials	9.8%
Consumer Discretionary	2.5%
Consumer Staples	1.2%
Health Care	15.4%
Information Technology	4.9%
Telecommunication Services	9.5%
Utilities	0.0%
Financials ex Property Trusts	28.4%
Property Trusts	6.4%
Cash & other	6.8%

Top 10 Holdings (as at 30 November 2020)

CSL Limited	10.5%
Commonwealth Bank of Australia Ltd	7.0%
ANZ Banking Group Limited	6.6%
Telstra Corporation Limited	5.1%
Fortescue Metals Group Limited	4.9%
Macquarie Group Limited	4.8%
Qantas Airways Limited	4.2%
Xero Limited	4.0%
National Australia Bank Limited	3.9%
Atlas Arteria	3.3%

Market review

The S&P/ASX 300 Accumulation index gained +10.2% over November – the best monthly return achieved since 1988. Resources (+10.7%) rebounded strongly during 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% for the month and is well above pre-Covid level. Brent Crude also gained +29% for the month. Demand remains a key difference between copper and oil – as the lack of air travel continues to weigh on the latter. In contrast, gold (-4.9%) continued to sell-off as need for safe haven has reduced for now.

Covid cases in the US remain a risk. However European restrictions are taking swift effect – with far less economic impact than previously. Coupled with vaccine upon the horizon, the market seems to be looking through near term Covid risks to focus on a more positive 2021.

On the vaccine front questions emerged over the quality of the most recent AstraZeneca trials, which appear to have a small sample size and a skew in terms of age profile. This may lead to a delay in approval as more data on different trial groups is collected. This is a material issue in terms of the vaccination plans for countries outside the US. The latter's plan is skewed more towards Pfizer and Moderna. However in places like the EU, UK and Australia the AstraZeneca vaccine formed a much larger proportion of the proposed plan. In Australia, in particular, this places far more significance on the Novavax trials. Ultimately, this could see a vaccination programme rolled out faster in the US than in other parts of the world, with implications for relative rates of economic growth.

Turning to sector performance, Energy (+28.2%) was the best performing sector on the back of the stronger oil price; followed by Financials (+16.1%), Communication Services (+14.4%), Real Estate (+13.2%) and Industrials (+12.0%). The big four banks all performed strongly during November, ranging from +14.3% (WBC) to +24.8% (NAB), as their latest updates got well received by the market. The outlook remains unconvincing - revenue trends remain challenged, credit growth - while stabilising - is still low, margins remain under pressure and any tangible benefit from cost out is an FY22 story. However, they remain propped up by the likelihood of lower bad and doubtful debts (BDDs), which supports the capital position and headline earnings, bolstering the dividend yield. Without BDD deterioration it is hard to see the sector underperform materially.

In terms of more stock-specific news, Telstra (TLS) gained +14.6% following the AGM update, where management clarified that the return-on-invested-capital (ROIC) target was 8%, up from the "above 7%" range outlined at their result. This is important as it removes much of the doubt around the dividend sustainability. They also outlined a restructuring which will provide better scope for splitting out parts of the business, allowing monetisation of the value in areas such as infrastructure assets.

Elsewhere, Xero (XRO, +20.3%) delivered a good result. New subscriber growth softened in the US and UK, in line with expectations given the challenges in attracting new customers during the Covid period. However, there was stronger than expected subscriber growth in Australia – and particularly in New Zealand – which was surprising given that these are already heavily penetrated markets. This may suggest a further post-Covid shift in mentality towards the importance of online cloud-based accounting. There were also constructive signals around the development of the broader platform and ancillary services.

In contrast, Treasury Wines (TWE, -6.3%) took a hit over the month and dragged on Consumer Staples (-0.7%). The company went into a trading halt as its stock price fell on the news of Chinese tariffs on Australian wine. With interim tariffs in the region of 170% on its Chinese imports, this is a huge blow to TWE. Exports to China and HK accounted for 38% of Group EBIT in FY19, with material implications for wine supply more broadly.

Fund performance

The Fund underperformed its benchmark over the month of November.

Contributors

Overweight Qantas (QAN)

Travel stocks responded to expectations of further domestic re-opening, which saw our key position Qantas (QAN, +28.4%) outperform. With the national airliner set to ramp up domestic capacity in the near-term, and we see more upside from its current price levels.

Not Held Woolworths (WOW)

Supermarket giant Woolworths (WOW, -3.1%) pulled back amongst the market defensives as investors turned risk-on over the month. This is in spite of the company reporting a good set of sales numbers for 1Q21. We do not hold WOW and this helped on the portfolio's relative performance. We retain exposure to the supermarket sector via the position in Metcash and its IGA franchise. This provides exposure to a defensive earnings stream, coupled with company-specific factors such as improvements in market share on the back of improved store formats and an increase in neighbourhood-style convenience shopping.

Detractors

Overweight Saracen Minerals (SAR)

Gold continues to sell-off amid the rise of the long-term bond yields, as investor's need for safe haven reduces for now. This saw gold miners, including Saracen Minerals (SAR, -16.5%) pull back during the month.

Overweight Evolution Mining (EVN)

Gold continues to sell-off amid the rise of the long-term bond yields, as investor's need for safe haven reduces for now. This saw gold miners, including Evolution Mining (EVN, -10.3%) pull back during the month.

Strategy and outlook

The S&P/ASX 300 gained 10.23% in November – its best monthly return since March 1988. 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, leaving the US with a far more moderate – and market friendly – government than many expected. Second, on the vaccine front, the ~95% efficacy rates reported by Modern and Pfizer were far higher than most expected.

The portfolio made strong gains in absolute terms, but lagged the index a little over the month. The key detractions came from the more defensive positions, such as gold miners Evolution and Saracen Minerals.

Some growth stocks also tended to lag more cyclical names. The portfolio's position in CSL dragged. Two of the new smaller-cap additions to Fund – Pushpay and Pro Medicus – also detracted in November. We retain our long term conviction in these stocks, which we believe offer significant valuation upside as well as being strongly aligned the with Fund's goal of investing in companies which enable the transition to a more sustainable future economy.

These drags on relative performance were largely offset by strong performance from the Fund's positions in Qantas – which should benefit from a relaxation of domestic restrictions – as well as ANZ and Xero.

The month's positive surprises – and the several, more negative ones which occurred through 2020 - emphasise the importance we place on building a robust portfolio. This has been the bedrock of the Fund's performance this year. Our approach has been to have 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, but the potential for large upside gains.

Despite a more positive market outlook, we continue to hold some insurance against a material downturn in sentiment. These more defensive positions include Evolution, Amcor and Costa.

Growth stocks may lag value in the near term, however should remain underpinned by low bond yields. Our preferred names include CSL and Xero. We consider these companies to be both Leaders and Enablers within the Fund's new framework of identifying and investing in stocks which are aligned with the transition to a more sustainable economy.

Accommodative monetary and fiscal policy remains the single greatest factor supporting markets. It also particularly benefits stocks within it, including our positions in Fortescue, Atlas Arteria, and JB Hi-Fi.

We also continue to hold companies which may have seen some short-term impact from Covid, but which should emerge in an even stronger market position – such as James Hardie, Nine, and Goodman Group.

Finally, we have exposure to more cyclical and value names, which can continue to do well as sentiment improves regarding economic recovery and normalisation. These include Cochlear, Qantas and Seek.

Looking forward, risks remain. The surge in Covid in the Northern Hemisphere has led to lockdowns – with perhaps more coming – and is having an impact on real-time economic activity. There is a great deal of complexity around the vaccines – how soon and widespread will they be used? How quickly will we return to normal? Geopolitical risk – particularly around the relationship between China and Australia – is higher than usual.

Nevertheless, 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. In The US, strong industrial production 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.

The risk of prolonged recession has receded. Policy-makers remains in the mindset of "whatever it takes" – with the policy settings supporting both the economy and markets.

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

Carbon Footprint

The estimated weighted average carbon intensity (WACI) of the portfolio, using greenhouse gas emissions (scope 1 and 2[1]) data supplied by MSCI and weighted by the size of our holding in each company, is shown in the table below. In other words, this provides an indication of a portfolio's exposure to carbon intensive companies. We also compare this to the weighted average emissions for the companies in the aggregated ASX300 index.

We caution that there are limitations of using carbon footprinting measures as an indicator of a portfolio's overall exposure to climate-related risks. For example, not all companies report their emissions data and hence some of the below analysis includes estimates. Also, it does not include scope 3 emissions. Further, portfolio carbon analysis does not capture exposure to physical climate-related risks, or the unique transition risks some companies within the portfolio face. Nevertheless, the WACI metric is recommended by the Task Force on Climate-related Financial Disclosures (TCFD)[2], noting it supports greater comparability of investor reporting.

Carbon Intensity (tonnes CO2e / $M sales)

Pendal Ethical Share Fund	ASX 300	Relative to ASX300
115.5	206.9	-91.4

Source: Pendal, MSCI as at 30 November 2020

[1] Scope 1 emissions result from sources directly owned or controlled by the company. Scope 2 accounts for GHG emissions from the generation of purchased electricity consumed by the company. Scope 3 emissions result from activities not directly owned or controlled by the company but are associated with its operation such as business travel, waste management, commuting, and the use of sold products and services. https://ghgprotocol.org/sites/default/files/standards/ghg-protocol-revised.pdf

[2] *Recommendations of the Task Force on Climate-Related Financial Disclosures, June 2017* https://www.fsb-tcfd.org/recommendations/

Risks

An investment in the Fund involves risk, including:

- **Market risk**: The risk that factors affecting one or more countries that can influence the direction and volatility of an overall market, as opposed to security-specific risks.
- **Security specific risk**: The risks associated with an individual security.
- **Concentration risk:** The Fund's investment strategy of seeking to generate high returns by investing in a concentrated portfolio of Australian shares makes the Fund more volatile than a diversified Australian share fund.

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

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

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