PENDAL

Factsheet

Equity Strategies

30 June 2022

Pendal Horizon Sustainable Australian Share Fund

ARSN: 096 328 219

The future is worth investing in

About the Fund

The Pendal Horizon Sustainable Australian 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 Horizon Sustainable Australian 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	-11.43	-11.36	-8.97
3 months	-14.33	-14.13	-12.22
FYTD	-13.29	-12.46	-6.78
6 months	-17.60	-17.21	-10.39
1 year (pa)	-13.29	-12.46	-6.78
2 years (pa)	4.85	5.85	9.45
3 years (pa)	1.22	2.19	3.44
5 years (pa)	4.96	5.97	6.90

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 Jun 2022)	$278 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 a contribution to the transaction costs incurred by the Fund, when the Fund is purchasing and selling assets. The buy-sell spread is generally 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 Horizon Sustainable Australian 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 June 2022)

Materials	17.2%
Industrials	9.8%
Consumer Discretionary	0.9%
Consumer Staples	1.2%
Health Care	12.9%
Information Technology	6.9%
Telecommunication Services	13.4%
Utilities	0.0%
Financials ex Property Trusts	26.6%
Property Trusts	3.4%
Cash & other	7.7%

Top 10 Holdings (as at 30 June 2022)

CSL Limited	10.5%
Telstra Corporation Limited	8.4%
Commonwealth Bank of Australia Limited	6.1%
National Australia Bank Limited	5.5%
QBE Insurance Group Limited	4.6%
Qantas Airways Limited	4.5%
Westpac Banking Corporation	4.4%
Xero Limited	3.9%
Downer EDI Limited	3.8%
Macquarie Group Limited	3.5%

Carbon performance

The estimated weighted average carbon intensity (WACI) of the portfolio, using greenhouse gas emissions (scope 1 and 2[1]) data supplied by ISS 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 metrics 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.

Weighted Average Carbon Intensity (tonnes CO_2e / $M revenue)

Pendal Horizon Sustainable Australian Share Fund	ASX 300	Relative to ASX300
113.99	227.43	-113.44

Source: ISS, Pendal holdings as at 30 June 2022. Report run on 05/07/2022 using latest ISS data. Currency AUD.

[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/

Market review

The US Federal Reserve's determination to bring inflation under control is stoking fears of recession. This was exacerbated in June by a CPI print which came in slightly higher than expected and showed inflation broadening across categories.

The Fed hiked rates 75bps in June and indicated that they could do the same again in July. They are now signalling that they could end the year at 3.4%, according to the "dot plot" of expected moves. Three months ago, this figure was 1.9%.

Other central banks are striking a similarly hawkish tone with regard to the pace of rate hikes. The Reserve Bank of Australia hiked 50bps.

This saw sharp falls in equity markets, as investors start to factor in the risk of earnings downgrades. It also saw a rotation away from value and the more cyclical sectors.

Australia underperformed as a result, with the S&P/ASX 300 off -9.1%. The S&P 500 fell -8.4% and the Euro Stoxx -8.8%. However the Australian market has still outperformed over the calendar year to date.

The two largest sectors of the Australian market – which had held up well thus far – were both hit hard. Materials fared worst as commodity prices tumbled and dragged on the miners. Iron ore fell -11.9% and copper -12.6%. BHP (BHP, -7.5%) held up better than most of the other miners, which saw double digit falls. The copper and lithium miners underperformed, having been among the sector better performers previously.

Financials fell as the RBA's rate hike triggered fears of domestic recession and saw some shorting of Australian banks, particularly by international investors. ANZ (ANZ, -12.0%) held up best of the Big Four, while Westpac (WBC, -18.3) fared worst. The insurers held up much better, with QBE (QBE, +1.0%) managing a small advance.

Consumer Staples held up well as investors sought defensive pockets. Woolworths (WOW, +2.7%), Coles (COL, +1.6%) and Endeavour (EDV, +4.3%), the three largest stocks in the sector, all made gains.

Energy also outperformed and held up well despite Brent crude oil falling -6.5%, thermal coal -9.6% and natural gas -23.2%. This was largely due to strength in the newly re-christened Woodside Energy (WDS, +7.0%), the largest stock in the sector. It did well in the wake of the tie up with BHP's oil and gas assets. Other energy producers such as Santos (STO, -9.5%) were softer. The fuel retailers such as Ampol (ALD, +2.6%) and Viva Energy (VEA, +1.8%) did well on the back of recovering volumes and strong refining margins.

Fund performance

The Fund underperformed the benchmark over the month of June.

Key contributors

Overweight Telstra (TLS, -0.8%)

Telstra held up much better than the broader market in June as investors sought defensive exposure. The company announced price increases across mobile phone contracts, to take place from July. Improvement in this division underpins a more predictable outlook for the company's earnings and cash flow, which should be seen favourably in the current environment.

Overweight QBE Insurance (QBE, +1.0%)

The insurance sector has generally outperformed in the last few months, as higher bond yields should provide a tailwind for margins. At the same time, premium pricing have been rising, helping offset rising claims inflation and structural issues posed by higher provisioning and reinsurance costs for weather-related events. QBE has done better than the domestically-focused insurers, where the market has been concerned about exposure to recent flooding events.

Key detractors

Overweight Evolution Mining (EVN, -38.0%)

Gold miners are faced with a squeeze as cost inflation – for labour, diesel and power – continues to rise while the price of gold has remained steady. This has dragged on the gold mining sector as a whole, though EVN took an additional hit as management downgraded production guidance as Covid has disrupted labour supply. EVN remains among the lowest cost gold producers.

Overweight Oz Minerals (OZL, -26.3%)

Concern that central bank tightening could drive the US economy into recession weighed on commodity prices in June and saw the copper price come off, along with miners such as OZL. The medium term outlook for copper remains positive, underpinned by constrained supply and structural demand as part of the renewable energy thematic. However concerns over demand, coupled with input cost inflation in areas like labour, diesel and power, may weigh in the near term.

Outlook

We maintain a cautious near term outlook for equities. It is increasingly hard to see how the US avoids a recession from here.

First the lagged effect of inflationary pressures means we are unlikely to see much relief on this front given the fuel, food, and shelter components are still rising. This gives the Fed little room to back off hikes. Second, while overall economic activity remains reasonable, the lead indicators are deteriorating.

These include the “rule of ten” observation of mortgage rates and petrol prices - which has a good track record of predicting recessions – and falling house prices which can affect consumption. This is feeding through to a fall in the Altanta Fed’s GDP tracker and other GDP forecasts rolling over.

This economic risk has implications for the market. The market is currently discounting a material drop in earnings, while the latter continue to hold up. Since 1987 we have only seen this disconnection twice, in 2002 and 2011, where markets overstated risk.

However in 2000, 2008 and 2020 the earnings caught up with the market and therein lies the risk if the US and global economy go into a recession.

Valuations in the markets other than the US - including Australia - are lower and provide some protection. But we remain wary of how the market performs as downgrades come through.

While the risk is material, this bearish scenario is not a certainty. Factors which could see a better outcome include:

- Inflation momentum slows more quickly than now expected. There are some signs of hope with higher inventory at US retailers and evidence of discounting appearing. The fall in the oil price is a very important lead if sustained.
- Labour markets loosen up sooner. We have seen announcements from the tech sector on layoffs, but collectively this is not sufficient. On the supply side perhaps inflation and the crypto bust help drive participation higher.
- Supply chains begin to ease up as China re-opens and demand softens.

Should these factors start to play out we may see the Fed swerve again and not be as aggressive on rates. It would still be unclear whether this is enough to avoid a recession; but in the market’s eyes it would at least signal the depth of the downturn could be lower.

One flag which is likely to mark the low in this cycle is the passing of time. This market looks closer in nature to 2000 and 2008 where the market had to consolidate near its lows for a number of months before sentiment improved – unlike the sharp policy-driven bounce of 2020.

This is a challenging environment for portfolio construction, however we believe it plays to the strength of our approach.

Our strategy is underpinned by identifying mis-priced stocks by “anticipating change,” and building a portfolio that manages thematic risk and is primarily dependent on stock-specific alpha – rather than a particular macro pathway or outcome – to perform.

Both elements can be seen in the way we approach portfolio construction in this environment. We have a range of thematic exposures, such that performance is not dependent on a particular outcome or pathway in terms of the key macroeconomic uncertainties currently at play.

Within this framework, we are finding stocks which have a company-specific aspect which can support valuation and/or drive outperformance. A key element of this at the moment is an emphasis on pricing power and of cash flow that has resilience even if we do see economic momentum start to slow.

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 **1300 346 821**,
contact your key account manager or visit **pendalgroup.com**

PENDAL