Pendal Focus Australian Share Fund

ARSN: 113 232 812

Factsheet

Equity Strategies

31 July 2022

About the Fund

The Pendal Focus Australian Share Fund (**Fund**) is an actively managed concentrated portfolio of Australian shares.

Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes), that significantly exceeds the S&P/ASX300 (TR) Index over the medium to long term. The suggested investment timeframe is five years or more.

Description of Fund

This Fund is designed for investors who want the potential for long term capital growth and tax effective income from a concentrated portfolio of primarily 15-30 Australian shares and are prepared to accept higher variability of returns. The Fund may also hold cash and may use derivatives.

Pendal's investment process for Australian shares is based on our core investment style and aims to add value through active stock selection and fundamental company research. Pendal's core investment style is to select stocks based on our assessment of their long term worth and ability to outperform the market, without being restricted by a growth or value bias. Our fundamental company research focuses on valuation, franchise, management quality and risk factors (both financial and non-financial risk).

Derivatives may be used to reduce risk and can act as a hedge against adverse movements in a particular market and/or in the underlying assets. Derivatives can also be used to gain exposure to assets and markets.

Fund Positioning

The Fund is designed to complement a conventional, core share portfolio by providing satellite exposure to selected Australian equities with the potential for performance enhancement.

Investment Team

Pendal's nineteen member Equity team is one of the largest in the Australian fund's management industry. The portfolio manager for the Fund is Crispin Murray, who has more than 31 years' industry experience. Crispin is also Head of Equity.

Other Information

Fund size (as at 31 Jul 2022)	$1,501 million
Date of inception	April 2005
Minimum investment	$25,000
Buy-sell spread[1] For the Fund's current buy-sell spread information, visit www.pendalgroup.com	
Distribution frequency	Half-yearly
APIR code	RFA0059AU

[1] 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.

Investment Guidelines

Ex-ante tracking error	3.0% - 6.0%
Max absolute stock position	15%
Min/max sector position relative to index	+/- 15%
Min/Max BARRA style factors	+/- 0.5 SD
SIRA style factors	Within 1 SD
Maximum cash level	30%
Shorting	No
Borrowing	No

Performance

(%)	Total Returns		Benchmark
	(post-fee)	(pre-fee)	Return
1 month	4.19	4.25	5.95
3 months	-7.22	-7.06	-6.21
FYTD	4.19	4.25	5.95
6 months	-0.06	0.30	1.50
1 year (pa)	-4.17	-3.45	-2.31
2 years (pa)	12.91	13.94	12.32
3 years (pa)	5.54	6.54	4.43
5 years (pa)	8.67	9.69	8.15

Sector Allocation (as at 31 July 2022)

Energy	9.3%
Materials	18.8%
Industrials	7.2%
Consumer Discretionary	4.1%
Consumer Staples	2.9%
Health Care	10.1%
Information Technology	7.8%
Telecommunication Services	8.7%
Financials ex Property Trusts	26.1%
Property Trusts	3.1%
Cash & other	1.9%

Top 10 Holdings (as at 31 July 2022)

BHP Billiton Limited	10.7%
CSL Limited	9.3%
Santos Limited	7.1%
Commonwealth Bank of Australia Ltd	6.7%
Telstra Corporation Limited	6.6%
National Australia Bank Limited	5.7%
Westpac Banking Corporation	5.2%
Xero Limited	4.5%
Qantas Airways Limited	4.3%
Macquarie Group Limited	3.6%

Fees and costs

You should refer to the latest Product Disclosure Statement for full details of the ongoing fees and costs that you may be charged.

Management fee[2]	0.75% pa
Performance fee[3]	15% of the Fund's performance (before fees) in excess of the performance hurdle.

[2] This is the fee we charge for managing the assets and overseeing the operations of the Fund. The management fee is deducted from the Fund's assets and reflected in its unit price.

[3] This is the fee we charge if the Fund's investment performance exceeds its performance hurdle, and any performance deficit has been recouped. The Fund's performance fee is 15% of the Fund's performance in excess of the performance return hurdle. The performance hurdle is the performance of the Fund's benchmark (S&P/ASX 300 (TR) Index) plus the management fee of 0.75% pa. If a performance fee is payable, it is charged in addition to the management fee. The performance fee is calculated in dollar terms each Business Day based on the investment performance and value of the Fund on that day. If we are entitled to a performance fee, it is paid to us as at 30 June each year.

Market review

The market took a positive turn in July. Signs that inflation may be peaking and that growth is slowing is seen as opening the door to the Fed scaling back the speed and scale of interest rate hikes. In this environment, bad news on the economic front is being seen as good news.

The S&PASX 300 gained 6.0% with every sector apart from materials (-0.4%) making gains. This rebound was seen across international markets more broadly with the MSCI World Index returning 6.4% and the S&P 500 7.6% in AUD terms. Emerging markets lagged far behind the rest of the world. China was in the red as the economy had its smallest growth rate since the beginning of 2020. A weakening property market alongside new lockdown measures in several cities were some of the primary factors.

We saw central banks again hike rates this month – the Fed up 75 bps, the ECB and RBA both up 50 bps. Softer US economic data, particularly in housing activity suggests a slowdown which saw bond yields fall. This alleviated some pressure seen year-to-date as investors considered less intense rate rises a possibility in the future. In response, the Australian and US 10-year bond yields fell 60 bps to 3.06% and 33 bps to 2.64%, respectively.

The market generally saw a sharp rotation away from areas which had been doing well to those which have previously lagged. As a result, small caps outperformed, as did growth.

Information Technology (+15.4%) did well on the back of this and was the best performing sector. Computershare (CPU), now the largest tech stock in the index, only ground out a 1.38% gain as beneficiaries of higher rates underperformed. However, Xero (XRO, +20.83%) and Wisetech (WTC, +32.36%) were some of the top performers. Additionally, financial software provider Iress Limited (IRE, -1.39%) was down after announcing its CEO of 13 years will be leaving the company.

Real Estate (+12.0%) also saw a solid rebound. This was across the board - although retail mall owners did particularly well, office, residential and industrial were also strong. Goodman (GMG), the largest REIT in the index, was also up 16.0%.

Materials underperformed as commodity prices were generally softer. This was driven by the large miners, with BHP (BHP) off -6.23%, Rio Tinto (RIO) -4.74% and South32 (S32) -3.30%. Fortescue Metals (FMG, +4.62%) managed to buck the trend. This offset strength in the lithium sector, with Mineral Resources (MIN) up 11.33% and Pilbar Mineral (PLS) up 20.96%. The rest of the sector, including the packaging companies and chemical producers, was generally stronger.

Energy (2.2%) also lagged the index. The price of Brent crude oil fell -4.2%, however thermal coal rose 5.7% and natural gas 28.2%. The oil and gas players were generally softer; Woodside Energy (WDS) rose only 0.44% while Santos (STO) fell -1.6%. However, the pure coal names such as Whitehaven (WHC, +28.31%) were strong. WHC also benefitted from an upgrade from brokers, citing significant cash flow generation and a positive Q4 update.

Within Financials (9.4%), BNPL stocks had one of its strongest months of the year, with Zip Co (ZIP, +157.96%) and recent owner of Afterpay; Block (SQ2, +19.87%) recouping some losses from previous months.

Fund performance

The fund underperformed its benchmark over the month of July.

Contributors

Overweight Xero (XRO, +20.8%)

A more positive tone in markets, on the view that slower growth and some signs of inflation rolling over opens the door to the Fed scaling back tighter policy, was accompanied by a rotation from value to growth stocks. Xero benefited from this trend. We continue to see a material fundamental growth opportunity for XRO in the UK, where regulatory changes are forcing small to medium business to complete tax on-line.

Underweight Rio Tinto (RIO, -4.74%)

China's near-term economic outlook is clouded by the ongoing effects of Covid restrictions and concerns over the property sector. At this point, Beijing has introduced policies to try and stem further deterioration, but has not launched a widespread stimulus. This is against a broader background of concerns about the impact of higher rates on global economic growth. This is weighing on commodity prices, with iron ore and copper prices both falling just over 4% in July, weighing on the miners.

Detractors

Overweight Santos (STO, -1.6%)

Brent crude oil prices fell -4.2% in July. This was part of a broader shift away from sectors which had done well – and which are exposed to slowing economic growth – to areas such as growth which had been under pressure. This weighed on STO. We continue to see supportive fundamentals dynamics in energy over the medium term. STO is well positioned as a reliable, low cost producer with a good suite of development opportunities.

Overweight QBE Insurance (QBE, -5.1%)

The shift in market sentiment saw rotation away from the beneficiaries of higher rates which had previously been doing well, such as QBE. We continue to see opportunity in QBE as part of our preferred exposure to financials. It gains a margin benefit from higher rates, while at the same time the insurance sector is benefiting from higher premium prices.

Market Outlook

The big debate is whether July's rebound is a bear market rally or whether we have put in the lows for this cycle.

At this point, the rebound is almost bang on the average bear market rally – in terms of rebound and length - in the S&P 500 since 1950.

The market breadth of the rally is not yet consistent with a change in trend. The rule of thumb is you need to see 90% of stocks above the fifty day moving average to signal a change in market direction. We are at 73%. However this could continue to climb.

The yield curve is also sending a negative signal. Its inversion is signalling recession, which would lead to a decline in earnings and pull the markets lower. The challenge to this perspective is the unusual speed and scale of the increases and the market's current confidence that inflation will be brought back down, which is reflected in long bond yields.

On the other hand, the bull case for equity markets is that;

1) The S&P 500 has bounced off long term technical support levels
2) Oil prices have peaked, with demand weakening
3) Bond yields have peaked, helped by lower commodity prices

The positive case is underpinned by the view that oil prices won't bounce back. We see this as a potential negative surprise for markets. There are several reasons why oil could behave differently in this cycle.

1) Inventories are low, despite tapping the US Strategic Petroleum Reserve (SPR). The latter probably has capacity for three more months of contributions to supply, with the run rate falling in that time.

2) Spare capacity is very limited, as shown in OPEC's only increasing output by 100,000 barrels per day (bpd) in September. There is no buffer for demand recovering, nor for any geopolitical shock.

3) Europe plans on tightening sanctions on Russian oil in December, which could limit access to .01 to 1.5m bpd

4) China at some point will re-open its economy, increasing oil demand by 500k – 1m bpd

5) Oil demand may surprise on the upside due to fuel oil. This is the first downturn where alternate fuel prices – notably gas and coal - are far higher than oil. This is likely to see some substitution to oil – not away from it as is normally the case. The US gas market has remained surprisingly tight despite the closure of the Freeport LNG export facility.

We are mindful that this may not play out for a few more months, given SPR still being released, China is set to run with zero Covid for another few months and the global economy is slowing.

So for time being, the weaker oil/lower bond signal could remain in place, but it is something to watch.

It is also important to remember that equity markets form part of the overall total financial conditions index which has an impact on the pace of economic growth.

The Fed's plan is firstly to slow growth below trend, which in turn should loosen the job market, leading to lower wage growth and inflation.

The Fed had shifted this sufficiently to be consistent with 1% GDP growth, in-line with the aim of a soft landing.

However the reaction to Chair Powell's press conference in July meant total financial conditions were beginning to ease. The Fed needed to check that move to keep conditions conducive to below trend growth.

All in all, at this point it is too early for a heroic call either way with regard to the near-term outlook. We maintain our balanced portfolio positioning, which is not dependent on a binary call on the outcome.

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.
- **Concentrated portfolio 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.

For more information please call **1300 346 821**,
contact your key account manager or visit **pendalgroup.com**

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