

Pendal Smaller Companies Fund

ARSN: 089 939 328

Factsheet

Equity Strategies

29 February 2024

About the Fund

The Pendal Smaller Companies Fund (**Fund**) is an actively managed portfolio investing in companies outside the top 100 listed on the Australian Stock Exchange and their equivalent on the New Zealand Stock Exchange that we believe are trading below their assessed valuation, and which we expect to grow their profits quickly.

Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes) that exceeds the S&P/ASX Small Ordinaries (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, diversification across a broad range of smaller companies and industries and are prepared to accept higher variability of returns. The Fund invests primarily in companies outside the top 100 listed on the Australian Securities Exchange. The Fund may also invest in equivalent companies listed on the New Zealand Stock Exchange, 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).

The Fund may have assets denominated in foreign currencies. This means that changes in the value of the Australian dollar relative to foreign currencies may affect the value of the assets of the Fund. The Fund's foreign currency exposure may be hedged from time to time, in whole or part.

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.

Investment Team

The Pendal Smaller Companies Fund is managed by Pendal's experienced Small Cap team. The Fund is managed by Lewis Edgley and Patrick Teodorowski. They are supported by an experience Small Cap team as well as the insight of Pendal's broader Australian equities team.

Portfolio characteristics

Benchmark	S&P/ASX Small Ordinaries (TR) Index
Number of stocks	Between 60 -90
Maximum cash weighting	20%
Ex-ante tracking error	Typically between 0% - 9%
Active single stock position	+/-5%

Performance

(%)	Total Returns (post-fee)	Total Returns (pre-fee)	Benchmark Return
1 month	2.83	2.93	1.72
3 months	9.72	10.06	10.05
6 months	11.23	11.92	6.88
1 year	17.81	19.28	7.84
2 years (p.a)	5.83	7.15	-0.37
3 years (p.a)	6.49	7.81	1.39
5 years (p.a)	6.90	8.22	4.42
Since Inception (p.a)	11.86	13.16	7.17

Source: Pendal as at 29 February 2024

"Post-fee" returns assume reinvestment of distributions and is calculated using exit prices. "Pre-fee" returns exclude the effects of management costs and any taxes. Returns for periods greater than one year are annualised. Fund inception: December 1992.

Past performance is not a reliable indicator of future performance.

Sector Allocation (as at 29 February 2024)

Energy	2.1%
Materials	15.6%
Industrials	15.4%
Consumer Discretionary	20.3%
Consumer Staples	1.7%
Health Care	2.3%
Information Technology	13.7%
Telecommunication Services	3.1%
Utilities	0.0%
Financials ex Property Trusts	15.2%
Property Trusts	6.2%
Cash & other	4.2%

Other Information

Fund size (as at 29 February 2024)	\$317 million
Date of inception	December 1992
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	RFA0819AU

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.

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	1.22% pa
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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.

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.
- **Liquidity risk** - The risk that an asset may not be converted to cash in a timely manner.
- **Small company risk** - Shares in smaller companies may trade less frequently and in smaller volumes and may experience greater price volatility than shares in larger companies.

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

Market review

Australian equities bounced around in February before ultimately rallying into the month's end. The S&P/ASX Small Ordinaries returned 1.72%, outperforming the 0.98% gain for the S&P/ASX 300.

The broad underlying picture of disinflation opening the way to rate cuts in 2024 remains in place.

However some stronger than expected economic and inflation data in the US have tempered previous expectations around the timing and scale of rate cuts.

In Australia the RBA kept rates on hold. Governor Bullock noted that inflation remains too high, but that recent developments are encouraging. She also noted that the CPI will not necessarily need to be back within the 2-3% target range before the first cut.

The outlook from Australian earnings season was slightly better than average, with 28% of stocks seeing EPS upgrades for FY24 – versus a long-term average of 22%. 33% saw downgrades, just under the long-term average for 34%.

The consensus FY24 earnings-per-share outlook for the ASX 200 remains unchanged following reporting season, with slight upgrades for banks and industrials offsetting slight downgrades for resources.

Information technology (+12.30%) was the stand-out sector, helped by good results from Megaport (MP1, +13.85%) and Audinate (AD8).

Consumer Discretionary (+6.52%) also outperformed as the revenue environment for retailers such as Harvey Norman (HVN, +11.99%) and Premier Investments (PMV, +7.29%) remains better than expected, while they are also generally maintaining good control of costs.

Energy (-6.52%) underperformed as the LNG/oil, coal and uranium names all pulled back. Fuel refiner and distributor Viva Energy (VEA, +4.56%) was one of very few names to buck this trend.

Consumer Staples (-2.63%) also underperformed, dragged down by Graincorp (GNC, -3.71%) and Inghams (ING, -15.35%).

Fund performance

The Fund outperformed the index in February. There was a good mix of performance drivers - in addition to Nick Scali and Service Stream, positions in Aussie Broadband (ABB) and specialist tech and communication company Codan (CDA) made good contributions, as did not owning Neuren Pharmaceuticals.

Key contributors

Overweight Service Stream (SSM, +20.97%)

Service Stream designs, constructs and operates infrastructure such as wireless and fixed-line telecom as well as gas and water networks. It saw earnings upgrades on the back of a well-received H1 FY24 result, with the company delivering 18.1% revenue growth and 46.9% profit growth versus the same half last year. Management cited continued strength in the telecom division and noted that performance continues to improve and margins expand within the utilities division.

Overweight Nick Scali (NCK, +17.95%)

Furniture retailer Nick Scali also delivered a strong set of results for the December half. It saw orders pick up in the second quarter, with momentum continuing into January. Gross margins rose 360bps to 65.6%, which was ahead of consensus. These also sit 280bps above the pre-Covid period and are expected to remain structurally higher due to better buying terms following its acquisition of the Plush franchise, which saw a large expansion in sales volumes and store numbers.

Key detractors

Overweight Kelsian (KLS, -15.88%)

Kelsian delivered a 44.9% increase in revenue in 1H FY24, however margins were weaker which meant that the 20.4% increase in underlying profit missed expectations. Management noted that weather disruptions and softer domestic demand for travel in December played a role. The company remained optimistic on the growth outlook on the back of both organic growth and potential acquisition opportunities.

Overweight Corporate Travel management (CTD, -21.73%)

CTD's half -yearly results were a little under consensus expectations and management downgraded the FY24 earnings guidance on the back of softer-than-expected performance from its UK Bridging Contract. This is a contract from the UK government to manage the travel and accommodation of asylum seekers in the UK. Issues with immigration have seen management take a conservative stance and assume no growth from this contract in 2H. The remainder of the business is generally performing well.

Outlook

The market is currently being supported by the prevailing view that inflation is slowing fast enough (in both the US and Australia) to support rate cuts later in the year.

In the US the question is whether lagged monetary policy will result in recession – dragging on earnings estimates and the market – or whether easing financial conditions, rising real wages and fiscal support drives continued growth. At this point the data suggest an economy remaining in good shape, though real-time “pulse” signals suggest a slow-down, which needs to be watched.

In Australia, we are watching to see whether previous rate hikes start to squeeze the economy enough to lower inflation and allow cuts, or if current growth momentum forces the RBA to hike further and run the risk of a more rapid slowdown. The most recent data supports the view that the economy is cooling and that rates have peaked.

In China there have been some positive surprises on the policy front in the last couple of weeks, but the economy remains challenged, which remains an issue for Australian resources.

More broadly, heading into February's reporting season, consensus expects aggregate index earnings to fall low single-digits in FY24. This is driven by falls in bank and resource earnings. Earnings in Industrials are expected to be positive, providing some offset. At this point, the market seems prepared to look through this earnings valley, helped by the potential for lower rates to support market valuations.

In the near term the Red Sea conflict presents a risk given it may have knock-on effects for inflation (via freight disruption and the oil price). These are not evident at the moment, but any escalation needs to be watched.

We are also mindful that market positioning is very positive given the current Goldilocks scenario. This does not mean that the market can't continue to rise if the current environment endures – there is still plenty of cash on the sidelines. But it does leave the market more vulnerable if there is a shift in the currently benign outlook.

For more information please call 1300 346 821,
contact your key account manager or visit [pendalgroup.com](https://www.pendalgroup.com)

PENDAL

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