Pendal Australian Share Fund

ARSN: 089 935 964

Factsheet

Equity Strategies

June 2020

About the Fund

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

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 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 Australian companies and industries 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. Derivative can also be used to gain exposure to assets and markets.

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 28 years' industry experience. Crispin is also Head of Equity.

Investment Guidelines

Ex-ante (forward looking) tracking error	2.0% - 6.0%
Min/max stock position	+/-4%
Min/max sector position	+/-8%

Other Information

Fund size (as at 30 Jun 2020)	$995 million
Date of inception	September 1992
Minimum investment	$25,000
Buy-sell spread[1] For the Fund's current buy-sell spread information, visit www.pendalgroup.com	
Distribution frequency	Quarterly
APIR code	RFA0818AU

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

Management Costs[2]

Issuer fee[3]	0.79% pa

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

[3] 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.

Performance

(%)	Total Returns (post-fee)	Total Returns (pre-fee)	Benchmark Return
1 month	1.41	1.48	2.43
3 months	16.41	16.64	16.79
FYTD	-6.21	-5.46	-7.61
6 months	-10.19	-9.84	-10.55
1 year (pa)	-6.21	-5.46	-7.61
2 years (pa)	0.59	1.39	1.46
3 years (pa)	5.13	5.97	5.24
5 years (pa)	5.64	6.49	6.00

Sector Allocation (as at 30 June 2020)

Energy	6.0%
Materials	22.8%
Industrials	10.6%
Consumer Discretionary	7.0%
Consumer Staples	4.4%
Health Care	11.3%
Information Technology	3.6%
Telecommunication Services	6.0%
Financials ex Property Trusts	22.8%
Property Trusts	2.2%
Cash & other	3.3%

Top 10 Holdings (as at 30 June 2020)

CSL Limited	8.5%
BHP Billiton Limited	7.1%
Commonwealth Bank of Australia Ltd	5.8%
Westpac Banking Corporation	4.6%
Telstra Corporation Limited	4.4%
ANZ Banking Group Limited	4.1%
Atlas Arteria	3.0%
Amcor Limited	2.6%
Santos Limited	2.6%
Qantas Airways Limited	2.6%

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.

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

Market review

The S&P/ASX 300 continued to benefit from positive sentiment around the pace of the economic rebound and the degree of fiscal and monetary policy support. It gained +2.4% in June, to cap a very strong +16.8% return for the quarter. The index is now down -10.6% for the calendar year to date.

This came despite some wobbles late in June as the market expressed some concern over the rise in cases in the US as it rolled back restrictions.

There was strong rotation from growth and defensives to value and more cyclical stocks during the quarter as confidence around the economy improved – although this rotation stalled late in the period.

Economic data continued to reflect the material blows inflicted by the shutdown. However in most respects it is not as bad as many as expected – while the rebound in activity and confidence indicators has also been sharp.

Real Estate (-1.5%) was the weakest sector over the month. In particular, rising concerns over the implications of a second wave weighed on the retail malls in the latter part of June.

The outcome for Energy was mixed. It was the third best sector in the quarter (+28.4%) but the worst performer in June (-2.0%). Supply discipline form OPEC and Russia and capacity closure in US shale have helped a recovery in the oil price – as has improved expectations around demand. This has driven outperformance from the oil/LNG names over several months, however sentiment was tempered in the final weeks of June.

Consumer Discretionary (+5.4%) was the best performing sector over June; and the second best performing over the quarter (+30.8%). The suppression of the virus in Australia has raised expectations that restrictions could be rolled back further and faster than many expected. At the same time, recent retail sales data is signalling a strong rebound. This has helped retail names such as Wesfarmers (WES, +11.0%), JB Hi-Fi (JBH, +15.9%) and Harvey Norman (HVN, +10.5%). The uptick in Victorian cases late in June bears watching in this regard. However at this point a return to broad-based nation-wide lockdowns looks unlikely.

Consumer Staples (+4.8%) also outperformed in June. Woolworths (WOW, +5.5%) and Coles (COL, +11.8%) did relatively well in the back end of the month as risk aversion rose, having lagged the index for a couple of months.

Health care was the worst performer over the quarter (+2.3%) although it fared relatively well in June (+3.5%). Trends have diverged within the sector. Some companies are benefiting from Covid-related demand, while the restrictions on elective surgeries have had a negative impact on others.

Technology was the best performing sector over the quarter (+48.7%), and outperformed in June alone (+3.7%). This is due in large part to the unrelenting surge from Afterpay (APT) which gained another +224% over the quarter. However the backdrop of low bond yields – and little expectation of a material increase in interest rates any times soon – is providing a tailwind to the broader growth sector.

Fund performance

The Fund performed broadly in line with its benchmark over the June quarter.

Contributors

Overweight Santos

Despite losing some momentum in June, Energy was among the best performing sectors over the quarter, as the oil price rebounded strongly. It wasn't a smooth ride without turbulence – price for the WTI futures contract turned negative for the first time in late April; although it was believed to be largely attributed to the contract rollover of a specific tenue. Underlying demand for oil has recovered somewhat over the course, however we believe there is risk to the downside should new Covid cases continue to rise in the US. More specifically on Santos, its quarterly report was well received, confirming that it had more hedging in place than people had expected, which can help support near term cash flow. We believe it remains the best exposure to the oil/LNG complex, given its low cost base and strong management.

Overweight James Hardie

James Hardie delivered a positive update and an upgrade for expected quarterly earnings, which reflects the fact that US housing is doing better than many thought. This is flowing through to higher margins for JHX, which is also gaining market share. We are mindful that JHX has benefited from a geographic advantage in terms of its key US exposures – there is some risk here in the next few months given their exposure in the southern US. We continue to keep a close eye here. However at this point we continue to like JHX as one of our recovery plays and policy beneficiaries.

Overweight Oil Search

Despite losing some momentum in June, Energy was among the best performing sectors over the quarter, as the oil price rebounded strongly. This benefited the likes of Oil Search. It wasn't a smooth ride without turbulence – price for the WTI futures contract turned negative for the first time in late April; although it was believed to be largely attributed to the contract rollover of a specific tenue. Underlying demand for oil has recovered somewhat over the course, however we believe there is risk to the downside should new Covid cases continue to rise in the US.

Detractors

Overweight Metcash

Metcash delivered its FY20 results in June. The key factor, in terms of their underlying position, was that there are continued signs that IGA's loss of share in recent years has stabilised and is turning. While there were indications of this pre-Covid, the trend has been helped by a return to more localised shopping in recent months. This comes soon after MTS had revamped formats in many IFAs and reduced prices, with the result that people returning to IGAs during March and April have liked the experience. MTS saw a bump in revenues during Covid, however this did not feed through to earnings, which was disappointing but consistent with a recent update from Woolworths. Supermarkets were forced to take on additional costs – such as extra shifts - to meet the surge in demand, offsetting revenue gains. However IGA sales growth remains strong and we believe that they should be able to contain costs. Management also announced some small bolt-on acquisitions, using some of the capital they raised and helping calm fears that there would be no return on it. MTS's liquor and hardware businesses remain well positioned. If the food segment can continue to perform it will no longer be seen as an offset to the other parts of the business and should help support a better rating.

Does not hold Afterpay

Buy-now-pay-later companies enjoyed a strong rally over the quarter, as investors expect them to benefit from the surge in online shopping following the Covid outbreak. In particular, Afterpay reached record high price following the announcement that Tencent bought a 5% stake in the company.

Overweight IAG

GI insurers, including IAG, QBE and SUN generally underperformed over the June quarter. IAG in May stated that the hit to their investment book had been larger than consensus expectations and this has been the market's focus at the moment. We remain mindful that unlike some peers, they have not had to sell these assets. As a result, we may see this revert given the rebound in credit markets.

Strategy and outlook

The economic rebound as restrictions roll off has generally beaten expectations. Coupled with supportive data and strong policy support, it has driven a rapid bounce in equity markets.

While second wave clusters in China and Germany appear to have been contained, cases continue to rise in the US. This in itself is not causing economic issues at this point. However the fear is that we will see a re-run of March/April, with cases leading to stress on hospitals and ICUs and a surge in mortality. This would likely be a material setback for market sentiment and confidence.

As China and Germany have demonstrated, a replay of April - in terms of case-loads, hospitalisations and mortality – is not a foregone conclusion. Today's situation is different from then in several important ways.

1. The outbreaks are in less densely populated areas than New York.
2. The age profile of new cases is a lot lower this time – an average of 20 years younger.
3. There is substantially more testing. This may result in worse-looking numbers but does mean that the problem is being identified earlier than in April.
4. There is more physical distancing and use of face masks – despite well-publicised incidents to the contrary.
5. Knowledge of how to treat the virus is far better now. Previously, treatment had focused on the lungs, which are now believed to be more symptomatic in nature. Instead, treatment is now focused more on anti-inflammatories, with better outcomes as a result.

If the US is able to successfully deal with this wave without reimposing broad-based restriction or a severe spike in mortality, then it should bolster market confidence. Nevertheless, this issue comes with material risk for sentiment and potential consequences for markets in the near term.

While we remain watchful on this issue, at this point we do not expect that recent weakness will morph into a second sharp drop in markets. We are mindful that:

1. We believe that sufficient measures are being - or will be taken - to avoid the resurgence in US cases from triggering material new shutdowns, which would see a large hit to confidence. However, this remains a key risk.
2. The Victorian outbreak should be containable and - while delaying border re-opening - does not represent a significant deterioration in the economic outlook.
3. The current case rise will likely cement the need for more policy stimulus in US and Australia.
4. Economic momentum is still positive.
5. Significant liquidity remains on the sidelines in cash, which can support equity markets.

That said, we do expect the current period of consolidation to continue as the rate of improvement in economic data is likely to slow down, the market's short term positioning remains bullish, and policy news flow is in a lull to the end of July.

At this point it appears the worst case scenario has been avoided and that Australia has been reasonably successful in suppressing Covid-19, paving the way to a resumption in domestic economic activity.

However there will be divergences between industries in terms of the degree to which they recover. Some will only partially recover, while others may get back to previous capacity – or more – in relatively quick time. The uncertainty here – and mis-pricing that results – coupled with the divergence in responses to the crisis at a company level, is driving material opportunity for active management.