

Pendal Dynamic Income Fund

Class R

ARSN: 622 750 734

Income & Fixed Interest

31 October 2023

About the Fund

The Pendal Dynamic Income Fund (**Fund**) is an actively managed portfolio of fixed income securities, Australian and global credit indices and emerging market sovereign issuers.

Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes) that exceeds the RBA Cash Rate by 2-3% p.a. over the medium term. The suggested investment timeframe is three years or more.

Description of Fund

The Fund is designed for investors who seek income from a portfolio of fixed income securities across a range of market conditions and are prepared to accept some variability of returns.

The Fund is an actively managed portfolio that invests primarily in Australian issued investment grade corporate bonds[^]. The Fund may also invest in Australian and global credit indices and emerging market sovereign issuers to provide portfolio diversification and enhance returns when we believe market conditions are supportive. The Fund also has the ability to decrease its allocation to credit and invest in cash and interest rate duration strategies when we expect volatility to increase.

Pendal uses a combination of quantitative modelling and qualitative research to construct the Fund's portfolio.

The Fund's portfolio is constructed using the following three step approach:

1. Generate investment themes through quantitative models
2. Reaffirm investment themes with qualitative research
3. Asset Allocation

Investment Team

Pendal's Income & Fixed Interest team is a large team of dedicated investment professionals with both global and domestic experience, invested across Income, Composite, Pure Alpha, Global and Australian Government strategies. The team also draws on a wide range of knowledge resources including Pendal's other specialist investment teams: Equity and Multi-Asset. The portfolio manager of the Fund is Amy Xie Patrick who has more than 19 years industry experience.

Portfolio Characteristics

Benchmark	RBA Cash rate
Liquidity	Daily

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 ¹	0.55% pa
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¹ 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.

Performance

(%)	Total Returns (post-fee)	Total Returns (pre-fee)	Benchmark Return
1 month	-0.10	-0.05	0.35
3 months	0.49	0.63	1.04
6 months	-0.82	-0.54	2.06
1 year	3.18	3.75	3.71
2 years (p.a)	-0.84	-0.30	2.25
3 years (p.a)	-0.05	0.50	1.53
5 years (p.a)	1.21	1.73	1.26
Since Inception (p.a)	1.35	1.84	1.30

Source: Pendal as at 31 October 2023

"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 2017.

Past performance is not a reliable indicator of future performance.

Asset Allocation (as at 31 October 2023)

Australian Credit	82.3%
Emerging Market Credit	15.5%
Other	11.9%
Cash	6.7%

Allocations may not add to 100% due to the use of derivatives to obtain credit exposure.

Top 10 Issuer Exposure (as at 31 October 2023)

NBN CO LTD	6.4%
COMMONWEALTH BANK OF AUSTRALIA	5.6%
NATIONAL AUSTRALIA BANK LTD	5.1%
AUSTRALIA & NEW ZEALAND BANKING GROUP LTD	4.0%
COLES GROUP TREASURY PTY LTD	3.9%
LONSDALE FINANCE PTY LTD	3.7%
MACQUARIE BANK LTD	3.4%
WESFARMERS LTD	3.4%
MCDONALD'S CORP	3.2%
DBNGP FINANCE CO PTY LIMITED	3.0%

[^]Corporate bonds held within the Fund are required to be rated investment grade at the time of investment. Downgraded securities can continue to be held up to 15% of the Fund (in aggregate). Investment grade bonds refer to securities that are expected to have a high probability of payment of interest and repayment of principal.

Portfolio Statistics (as at 31 October 2023)

Yield to Maturity [#]	5.27%
Running Yield [*]	3.46%
Modified duration	1.68 years
Credit spread duration	2.98 years
Weighted Average Maturity	2.80 years
Average Australian Credit Rating	A+

[#] The portfolio yield to maturity is an estimate of the fund's internal rate of return. It is calculated as the yield to maturity of all securities comprised in the benchmark at the relevant time (sourced from Bloomberg), plus our estimate of the weighted average traded margin over the swap rate for each of those securities based on observed market prices. The portfolio yield to maturity does not represent the actual return of the fund over any period.

^{*} The portfolio running yield is calculated as the weighted average coupon rate of the physical portfolio assuming all securities are held at par or face value. Carry/interest income from synthetic positions are excluded from this calculation. Running yield does not reflect the actual income return of the portfolio.

Other Information

Fund size (as at 31 October 2023)	\$231 million
Date of inception	December 2017
Minimum investment	\$25,000
Buy-sell spread ²	
For the Fund's current buy-sell spread information, visit www.pendalgroup.com	
Distribution frequency	Quarterly
APIR code	BTA8657AU

² 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.

Risks

An investment in the Fund involves risk, including:

- **Market risk** – The risk associated with factors that can influence the direction and volatility of an overall market, as opposed to security-specific risks. These factors can affect one country or a number of countries.
- **Security specific risk** – The risk associated with an individual security.
- **International investments risk** – The risk arising from political and economic uncertainties, interest rate movements and differences in regulatory supervision associated with international investments.
- **Interest rate risk** – The risk associated with adverse changes in asset prices as a result of interest rate movements.
- **Credit risk** - The risk of an issuing entity defaulting on its obligation to pay interest/principal when due.
- **Emerging markets risk** – The risk of asset price volatility and higher currency, default and liquidity risk from investments in emerging markets.
- **Liquidity risk** - The risk that an asset may not be converted to cash in a timely manner.
- **Derivatives risk** – The risks arising from use of derivatives to manage exposures to investment markets.
- **Counterparty risk** – The risk of another party to a transaction failing to meet its obligations.
- **Class risk** - The Fund has been established as a separate class of units in the Scheme. As the assets are held on trust for all investors, there is a risk that investors of one class may be exposed to liabilities of another class of units and they could lose some or all of their investment in the Fund. There is also a risk that in the event of an insolvency, the assets of the Fund could be made available to creditors of another class of units of the Scheme

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

Market review

The past month in global markets was marked by significant movements, influenced by a myriad of factors. In the US, the spotlight was on mixed corporate earnings, geopolitical turmoil in the Middle East and concerns about rising interest rates, with the 10-year US treasury yield breaching 5% mark for the first time in over a decade.

The recent surge in longer-dated treasury yields has led to a significant tightening of financial conditions, providing the Fed with an opportunity to pause and evaluate if its current policy stance is sufficiently restrictive to steer inflation back to its target. Of comfort to the Fed will be that the bulk of the rise in nominal rates has been propelled by real yields rather than inflation expectations, alleviating pressure off the central bank to persist with more hikes. Given more breathing space, consensus among economists is that the Fed will maintain the Fed funds target range at 5.25-5.50%. This viewpoint comes in light of robust 3Q GDP growth, a resilient job market, and persistent inflation rates that exceed the 2% target.

At the Fed, Chair Powell has continued to highlight the "long and variable lags" associated with policy rate adjustments and their subsequent impact on the real economy. His recent address to the Economic Club of New York reiterated the theme that prior monetary decisions carried delayed impacts. Given the rapid pace of recent adjustments as well as the banking sector's increased selectiveness in lending decisions, investors have increasingly braced for a potential downturn in bank lending by year-end. Historically, in a credit-driven economy like the US, such trends have been precursors to recessions.

From a macro front, the US reported 4.9% annualised growth in the for third quarter. This marks a significant jump from the 2.1% in Q2 and is the most robust growth seen in almost two years. The US consumer remains a primary growth engine driven by robust demand for both goods (4.8%) and services (3.6%). Elsewhere elevated interest rates appear to have impacted investments, which saw the slowest growth since Q4 2022. Business capital expenditure dipped slightly due to a decline in equipment investment and subdued growth in intellectual property products. In contrast, residential investment witnessed a 3.9% rise, its first in ten quarters.

Over the month, corporate credit spreads have seen a slight expansion, yet they remain generally narrow. Such tight spreads indicate that the market remains optimistic about borrowers' creditworthiness and views the broader economic landscape positively. Despite global monetary policy shifts towards tightening, there's a prevailing sentiment for a potential "soft landing." This confidence is bolstered by robust corporate financials, sustained consumer expenditure, and a notably low corporate default rate this year.

Domestically, Australia's inflation dynamics took a notable turn in the September quarter, primarily propelled by surging petrol prices. This has intensified expectations surrounding the RBA's potential move towards another interest rate adjustment. The RBA's preferred inflation measure, trimmed mean CPI, grew by 1.2% for the third calendar quarter, marking a reacceleration from the 1.0% observed in the prior period. In a subsequent press conference, RBA governor, Michele Bullock, remained tight-lipped around a possible rate hike in November, citing that her team were "still analysing the numbers at the moment".

China, on the other hand, saw a glimmer of hope with rising industrial profits hinting at potential economic stabilisation. Furthermore, the Chinese government greenlit the release of an additional RMB 1 trillion in sovereign bonds, earmarked specifically for infrastructure development. This decision was accompanied by an upward revision of the fiscal deficit ratio for 2023, now projected at approximately 3.8% of the GDP, a notable increase from the 3% threshold established earlier in March. These budgetary amendments highlight Beijing's ongoing support for the nation's

financial and economic system. However, the (official) default of Country Garden Holdings on its offshore debt payments underscored the persistent challenges in the nation's housing sector. Overall, as a primary contributor to global growth, stability in China anchors its region neighbours as well as broader emerging markets.

Fund performance

In October, the Dynamic Income Fund underperformed the benchmark. Physical credit contributed to performance while duration and emerging markets detracted.

Within the credit portfolio we continue to favour a basket of higher-quality liquid securities, particularly infrastructure and utilities which rallied as the synthetic credit market sold off. While current default rates remains relatively low, they are anticipated to increase in 2024. The blend of persistent inflation, tighter lending norms and economic pressure sets a challenging backdrop for the lower-tier names. The financial cushion for capital-intensive cyclical is thinning, hinting at potential refinancing challenges in 2024, especially for sectors like real estate. We believe a US recession in 2024 alongside a eurozone locked in stagnation is plausible. Our spread duration sits around a relatively conservative 2.6 years with sufficient cash on hand to deploy should opportunities arise amid market weakness. Over the month we selectively added a new issue of Woolworths and Transurban to the book while rotating out of shorter dated banks.

In the interim however, credit markets have been sustained by extensive private sector resilience, a theme that is unlikely to reverse over the next couple of months. Issuance too has been stronger at the margin with most deals being oversubscribed. We believe there will be a last hurrah in risk assets before recession sets in. As such we see value in employing our emerging market (EM) lever to access alpha opportunistically. Tactical positioning in this space helped preserve some capital though a natural beta exposure to a softening market did detract from performance. Longer term, we believe there's substantial value in EM sovereign spreads particularly as constituent nations e.g. Turkey rotate further towards fiscal and monetary prudence.

The portfolio's duration book detracted from performance as mounting "soft-landing" headlines weighed on our rates positions. Backed by a resilient consumer, the US economy continued to showcase robustness, triggering a re-pricing of long-end yields everywhere. In addition, a surprise reacceleration of Australian core CPI prompted a reassessment of RBA intentions and whether there would be more hikes in the pipeline. Driven by our near-term bearish (quantitative and qualitative) views we have purposely held duration below our neutral range of 2-3 years. Currently we hold

1.7 years of duration, an appropriate balance between allowing a meaningful degree of insurance against left tail risks and ensuring the portfolio won't be compromised should positive correlations between bonds and equities persist.

The PAFI allocation was down, detracting from total performance. The predominant driver was a long CDX high yield position. The trade, predicated on the theme of goldilocks, struggled as risk names sank into the red. Elsewhere, gains Australia and Korea steepeners offset losses in our long US 2-year and US 10-year futures positions.

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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