PENDAL

Factsheet

Income & Fixed Interest

31 October 2023

Pendal Government Bond Fund

ARSN: 098 011 048

About the Fund

The Pendal Government Bond Fund (**Fund**) is an actively managed portfolio of predominantly government bond securities which aims to take advantage of investment opportunities within bond markets.

Fund Objective

The Fund aims to provide a return (before fees and expenses) that exceeds the Bloomberg AusBond Govt 0+ Yr Index over a rolling 3-year period. The suggested investment timeframe is three years or more.

Description of Fund

This Fund is designed for investors who want to take advantage of opportunities within the government bond markets and are prepared to accept some variability of returns. The Fund offers income and a diversified portfolio of government bonds and cash securities. The Fund invests primarily in the Australian government bond market across a combination of Commonwealth government bonds, semi government bonds (State issued bonds), corporate bonds (which are Government guaranteed), foreign sovereign and supranational bonds. The Fund may also invest tactically in international government bonds, which are in developed markets.

The Fund can use derivatives to achieve its investment objective and to gain exposure to assets and markets. Derivatives may also be used to reduce risk and can act as a hedge against adverse movements in a particular market and/or in the underlying assets.

Pendal's investment process for government bonds aims to add value through multiple strategies and investment research. Pendal seeks to generate excess returns through strategies including active security and sector selection, duration and yield curve management.

Investment Team

Pendal's Income & Fixed Interest team is a large team of dedicated investment professionals. 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 Tim Hext who has more than 34 years industry experience.

Other Information

Fund size (as at 31 October 2023)	$294 million
Date of inception	July 1992
Minimum investment	$500,000
Buy-sell spread[1] For the Fund's current buy-sell spread information, visit www.pendalgroup.com	
Distribution frequency	Quarterly
APIR code	BTA0111AU

[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]	0.32% pa

[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.

Performance

(%)	Total Returns (post-fee)	Total Returns (pre-fee)	Benchmark Return
1 month	-2.04	-2.02	-2.09
3 months	-3.05	-2.97	-3.13
6 months	-5.83	-5.68	-6.04
1 year	-1.53	-1.22	-2.10
2 years (p.a)	-4.57	-4.26	-4.86
3 years (p.a)	-5.03	-4.72	-5.20
5 years (p.a)	-0.14	0.18	-0.36
Since Inception (p.a)	5.50	5.85	5.52

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: July 1992.

Past performance is not a reliable indicator of future performance.

The benchmark for this Fund has changed over time. The benchmark performance shown is that of the combined benchmarks that the fund has aimed to exceed over time.

Sector Allocation (as at 31 October 2023)

Government bonds	49.8%
Semi-Government bonds	40.6%
Cash & other	9.6%

Portfolio Statistics (as at 31 October 2023)

Yield to maturity[#]	4.94%
Running yield[*]	3.40%
Modified duration	5.48 years
Credit spread duration	0.22 years
Weighted average maturity	7.29 years

[#] 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.

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.
- **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.
- **Inflation risk -** The risk that the rate of return of inflation may exceed the net after-tax return from your investment. Thus, the purchasing power of an investment may not keep pace with inflation.
- **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.
- **Currency risk -** Currency exchange rate fluctuation risk arising from investing across multiple countries.
- **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.
- **Regulatory risk -** The risk that a change in laws and regulations governing an investment or financial markets could have an adverse impact on an investment.

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

Market review

The Reserve Bank of Australia (RBA) left the cash rate unchanged in October at 4.10%. In their October meeting minutes the RBA Board expressed "a low tolerance for a slower return of inflation to target than currently expected". That is highly likely to have occurred following the release of the 3rd quarter inflation data late in the month. 3rd quarter inflation was higher than expected with headline and trimmed mean rising by 1.2% and resulting in annual increases of 5.4% and 5.2% and saw the market move to price further policy tightening as more than likely in November. Other data released included the employment data which saw the unemployment rate fall from 3.7% to 3.6% due to a 0.3% decline in the participation rate. Employment grew by 6,700 jobs in September with part time employment growth of 46,500 offsetting the decline of 39,900 full time jobs.

Risk aversion continued in October with equity markets recording their 3rd consecutive decline. In the United States the S&P and Nasdaq fell by 2.2% and 2.8% over the month and by 8.6% and 10.4% over the past quarter. In Australia the S&P/ASX200 fell 3.8% for the month and 8.5% over the quarter. The recent rise in bond yields continued in October and weighed on equity valuations. The worsening budget situation and the increasing debt funding required continues to exert upward pressure on yields in the United States. Risk sentiment was also negatively affected by Hamas' attack on Israel early in the month and Israel's subsequent response. The risk of a wider conflict drawing in other countries escalated over the course of the month.

In the United States no Central Bank meeting was held during the month. Meeting minutes from the September meeting provided no new information with Fed members agreeing policy should remain restrictive for some time and incoming data would determine if further policy tightening was required.

Economic data included the JOLTS report which showed job openings unexpectedly rising in August, indicating further strength in an already tight labour market. Non-farm payrolls data for September also exceeded expectations when adding 336,000 jobs (consensus was 170,000) and prior month revisions added a further 119,000 jobs. Allaying some fears was the weaker average hourly earnings which rose 0.2% in September and 4.2% over the past year and the unemployment rate that was unchanged at 3.8%.

September inflation data provided little comfort with headline inflation rising 0.4% in the month resulting in annual headline inflation of 3.7%. Core inflation of 0.3% and 4.1% was in line with market expectations. Underlying details would not have provided comfort for the Federal Reserve with services inflation remaining elevated. Offsetting this was weaker goods inflation driven by the fall in used car prices. The producer price index also came in higher than expected.

September retail sales rose 0.7% and the control group, which feeds into economic growth calculations rose 0.6% easily surpassing the market forecast of a rise of 0.1%. Economic growth for the 3rd quarter showed an annualised growth rate of 4.9% although the core personal consumption expenditure (PCE) deflator falling to 2.4% did provide some cause for optimism about the inflationary environment.

The Bank of Canada left their policy settings unchanged at their October meeting. Inflation is not forecast to return to target until mid 2025 and Governor Mackem stated that they are prepared to hike further if inflationary pressures persist.

The European Central Bank (ECB) left their policy settings unchanged as expected. As per their statement the ECB sees interest rates at levels that if maintained for a sufficiently long duration will bring inflation back to its target. In the press conference ECB President Lagarde reinforced this view noting that the transmission mechanism is increasingly dampening demand and in turn pushing inflation down.

The Reserve Bank of New Zealand also left their cash rate unchanged at 5.5% as expected. 3rd quarter inflation rose by 1.8% resulting in an annual headline inflation rate of 5.6%. The result was weaker than the RBNZ's inflation forecast and likely sees monetary policy remaining unchanged in the near term.

Fund performance and activity

Bonds again performed poorly in the late part of October, meaning negative returns in the fund. The fund outperformed the benchmark, with a number of strategies providing good results.

The fund entered the month short front end duration on the view that a November rate hike was a close call, and the markets had little priced in. The higher than expected Q3 CPI saw us cover this as markets were largely priced for a hike after. Long end duration was kept small and the fund has a number of very short term tactical positions that netted out for performance.

The fund also did well from a new 2054 bond issued by the AOFM (federal government issuer). The bond came cheaper than our analysis and ended the month at fair value. The fund also did well from some pre-hedging of the duration risk.

The fund entered October with a neutral position in semi government bonds. As we expected they did underperform and we took advantage of new issuance from QTC and the ACT to again go overweight at wider levels later in the month. Semi governments still have large borrowing programs to execute but bank balance sheets and new demand at these high yields are seeing decent support.

Finally, the fund exited a position in short dated inflation bonds post the high Q3 CPI. We have held these for a number of years as the high inflation results have helped strong performance. Although they may still provide some performance we are concerned that oil prices will push lower and the inflation narrative will become less favourable.

Outlook

The Reserve Bank of Australia (RBA) is likely to raise the cash rate to 4.35% at its November meeting. To not do so would risk the credibility of the new governor given the stated low tolerance the RBA has for a slower return of inflation to the target and the higher than expected 3rd quarter inflation subsequently released.

With the cash rate having already increased 4% since May last year and economic growth forecast to be sub-trend for 2024 and 2025 the RBA had viewed it as prudent to adopt a wait and see approach. The RBA remains cognizant of the uncertainties around the outlook for the Australian economy including the lagged effect from past tightening. Higher inflation and particularly services inflation however means that the RBA has little choice other than to tighten. We do not expect a follow up hike in December with 4th quarter inflation released in late January 2024 the likely catalyst should further policy action be required.

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

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