

### Pendal Sustainable Australian Fixed Interest Fund

Income & Fixed Interest

Class R

31 October 2023

ARSN: 612 664 730

#### About the Fund

The Pendal Sustainable Australian Fixed Interest Fund (**Fund**) is an actively managed portfolio of Australian fixed interest securities. Investments are selected based on a range of sustainable, ethical and financial criteria.

#### Investment Return Objective

The Fund aims to provide a return (before fees, costs and taxes) that exceeds the Bloomberg AusBond Composite 0+ Yr Index by 0.75% p.a. over rolling 3-year periods.

#### Description of Fund

This Fund is designed for investors who want income, diversification across a broad range of fixed interest securities and are prepared to accept some variability of returns. The Fund may also hold cash and may use derivatives.

Pendal's investment process for fixed interest aims to add value through multiple strategies and investment research. Pendal seeks to generate excess returns through strategies including active security (including green bonds, social bonds and sustainable bonds) and sector selection, duration, yield curve and credit management.

Our investment approach for credit management seeks to identify opportunities on a sector, issuer and security basis by incorporating top-down and bottom-up research. Top-down research includes analysis of economic and market data, along with macro credit fundamentals such as company earnings, balance sheet health, default rates and equity volatility. The bottom up research includes analysis of earnings and cashflow volatility, balance sheet, business diversity, industry and valuation.

The Fund applies a sustainable and ethical assessment process to fixed interest credit issuers, which includes such factors as:

- environmental issues,
- corporate governance, and
- social practices,
- ethical practices.

The Fund will not invest in issuers directly involved in either of the following activities:

- tobacco production (including e-cigarettes and inhalers); or
- controversial weapons manufacture (including cluster munitions, landmines, biological or chemical weapons, nuclear weapons, depleted uranium weapons, blinding laser weapons, incendiary weapons, and/or nondetectable fragments).

The Fund will also not invest in issuers directly involved in any of the following activities, where such activities account for 5% or more of an issuer's gross revenue:

- exploration, extraction or refinement of fossil fuels (specifically coal, oil and gas);
- the production of alcohol;
- manufacture or provision of gaming facilities;
- manufacture of non-controversial weapons or armaments;
- manufacture or distribution of pornography; or
- direct mining of uranium for the purpose of weapons manufacturing.

The Fund aims to meet its investment objectives by investing in government and credit securities that pass our sustainable and ethical screens. The Fund also seeks investments in securities (including green bonds, social bonds and sustainable bonds) that in addition to meeting our financial risk and return requirements also aim to generate positive and measurable social and/or environmental outcomes and where possible, contribute towards the advancement of the United Nations Sustainable Development Goals.

#### Performance

(%)	Total Returns		Benchmark
	(post-fee)	(pre-fee)	Return
1 month	-1.71	-1.67	-1.85
3 months	-2.51	-2.41	-2.63
6 months	-4.77	-4.57	-5.20
1 year	-0.66	-0.26	-1.18
2 years (p.a)	-4.39	-4.01	-4.26
3 years (p.a)	-4.36	-3.98	-4.61
5 years (p.a)	0.33	0.73	-0.13
Since Inception (p.a)	0.61	1.01	0.36

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: August 2016.

Past performance is not a reliable indicator of future performance.

#### Sector Allocation (as at 31 October 2023)

Government bonds <sup>^</sup>	25.4%
Semi-Government bonds <sup>^</sup>	4.3%
Sustainability Screened Corporate bonds	25.3%
ESG Thematic bonds - Climate	24.1%
- Social	8.9%
- Sustainable	7.5%
Cash & other	4.4%

<sup>^</sup> Ex Green, Social & Sustainable Bonds



CERTIFIED BY RIAA

The Pendal Sustainable Australian Fixed Interest Fund has been certified by the Responsible Investment Association Australasia according to the strict operational and disclosure practices required under the Responsible Investment Certification Program. See [www.responsibleinvestments.com.au](http://www.responsibleinvestments.com.au) for details.

The Responsible Investment Certification Program does not constitute financial product advice. Neither the Certification Symbol nor RIAA recommends to any person that any financial product is a suitable investment or that returns are guaranteed. Appropriate professional advice should be sought prior to making an investment decision. RIAA does not hold an Australian Financial Services Licence.

For more information on how these exclusions are applied, refer to section 5 'How we invest your money' of the Fund's Product Disclosure Statement at [www.pendalgroup.com/PendalSustainableAustralianFixedInterestFundClassR-PDS](http://www.pendalgroup.com/PendalSustainableAustralianFixedInterestFundClassR-PDS).

### 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 George Bishay, who has more than 29 years industry experience.

### Portfolio Statistics (as at 31 October 2023)

Yield to Maturity <sup>#</sup>	5.21%
Running Yield <sup>†</sup>	3.60%
Modified duration	4.85 years
Credit spread duration	1.55 years
Weighted Average Maturity	6.62 years
Average Credit Rating	AA

<sup>#</sup> 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.

<sup>†</sup> 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)	\$733 million
Date of inception	August 2016
Minimum investment	\$25,000
Buy-sell spread <sup>1</sup>	
For the Fund's current buy-sell spread information, visit <a href="http://www.pendalgroup.com">www.pendalgroup.com</a>	
Distribution frequency	Quarterly
APIR Code	BTA0507AU

<sup>1</sup> 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 <sup>2</sup>	0.40% pa
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<sup>2</sup> 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.

### Market review

October was a poor month for bond markets. In almost a carbon copy of September, markets were largely unchanged for the first half of the month but collapsed in the second half. Unlike September though, the reasons for the selloff were less clear and numerous explanations were given for what was a surprise to most. In Australia three year bonds sold off 0.32% to 4.40%. 10 year bonds sold off more, moving up 0.43% to 4.92%, the highest level since early 2011. A decade long rally of over 4% in 10 year bonds has now been unwound in two years.

The key data release in Australia over October was the Q3 inflation numbers late in the month. The RBA has been on hold recently but expressing a low tolerance for inflation surprises. Unfortunately for the RBA their inflation forecasting has yet again been poor, changing their year end 2023 forecast down to an optimistic 3.9% in August. The Q3 number ended up coming in slightly higher at 1.2%, leaving the likely year end inflation rate closer to 4.2%. Whilst these are small differences in the scheme of things it will pressure the RBA into hiking, otherwise their rhetoric starts to look hollow.

The higher rates also put pressure on spreads in general. Semi government spreads were hit quite hard, out around 10 basis points on the month. This wiped out the positive performance through August and September. Swap spreads and credit markets also drifted wider but found some receiving and buying at the higher yields, limiting the spread movements.

### Credit review

In October, credit spreads widened as investor sentiment weakened. The primary catalyst for this downturn in risk appetite can be attributed to the continued rise in global bond yields, and the events in the middle east with the conflict between Israel and Hamas driving wider geopolitical fears. On the flip side, dovish Central Bank rhetoric and a positive US earnings season supported markets.

The surprise Hamas attack on Israel drove market weakness. The prevailing concern lies in the potential for regional escalation from Iran or other influential actors such as Saudi Arabia and Qatar. A wider military conflict in the Middle East could lead to a reduction in oil supply, provoking a surge in crude oil prices.

Compounding this negative sentiment was the persistent increase in U.S. interest rates. The driver of rising yields has been the resilience of the U.S. economy, higher oil prices and the anticipation of substantial Treasury supply to fund the significant US fiscal spending. Key US economic indicators such as payrolls, producer price and GDP all exceeded expectations during the month.

Federal Reserve and ECB officials spoke to monetary policy being restrictive enough to lower inflation to their goals and risks now more evenly balanced relative to the past. This was viewed favourably by markets as it indicates Central Banks may be close to the end of their hiking cycle.

A decent US Q3 earning reporting season was also supportive. With just over half of the S&P500 having reported by the end of October, 79% had beaten earnings expectations by 8% on average. Actual sales growth was 2% with profit growth of 3% vs pcp.

### Fund performance and activity

The Fund outperformed the Bloomberg AusBond Composite Bond index over the month.

The duration component of the fund had a positive month. The fund had some short duration positions in the front end on the view that the market was underpricing the risk of a rate hike. This position was largely covered post the CPI selloff. We kept out of duration further out the curve over the month. Outright levels in the

longer end now look attractive to go long duration on a fundamental view. We are waiting for momentum and model indicators to turn positive before risk is taken.

The physical portfolio performed well outperforming the benchmark. Both the government sector positioning and the non-government portion of the portfolio added to performance. Industrials, infrastructure and financials sector positioning added to performance whilst supra-nationals detracted.

Activity during the month included increasing exposure to industrials, infrastructure, and financials funded out of shorter dated banks and utilities. We also completed a Commonwealth government bond switch into the new 2054 bond funded out of mid curve bonds.

### Market outlook

Bond markets should find some support after the dramatic move higher in late October. Real yields and nominal yields are at levels last seen in 2011 and offering investors very attractive returns over inflation. The big question is how much is structural and how much is cyclical. We expect the answer is a bit of both and we see levels as now being cheap.

The inflation outlook over the next year will be more market friendly, although levels will remain above the RBA target band. Similar to the second half of the last decade though the RBA will look through inflation outcomes in the 3-4% band. Wages will be slower to moderate but they will as the cycle moves on.

We expect a rate hike in November, but for that to be the end of the cycle. The inflation profile for the next year will see quarterly outcomes slightly below 1% and for inflation to end 2024 nearer 3.5%. This will allow the RBA to spend most of 2024 with tight but

stable rates holding back the economy. Potential US rate cuts in the second half of 2024 may see some speculation of lower rates in Australia but we see actual cuts as more an early 2025 event.

### Credit outlook

We remain tactically positive on credit spreads given the continued fall in US core inflation and the resilience of the consumer. This easing of inflation concerns should see central banks ultimately reduce cash rates which should see soft economic landing as opposed to a harder landing, and in turn would be positive for risk assets.

We are still cautious medium term as tight labour markets globally could see services inflation remain sticky and would see Central Banks maintain cash rates higher for longer, which would translate into a deeper global economic growth slowdown and potential recession.

Tightening of credit lending globally is also a risk to growth.

Higher oil prices and geopolitical concerns remain a risk for inflation.

### 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.
- **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.
- **Liquidity risk:** The risk that an asset may not be converted to cash in a timely manner.
- **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.

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

**PENDAL**

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PFSL is the responsible entity and issuer of units in the Pental Sustainable Australian Fixed Interest Fund (Fund) ARSN: 612 664 730. A product disclosure statement (PDS) is available for the Fund and can be obtained by calling 1300 346 821 or visiting [www.pentalgroup.com](http://www.pentalgroup.com). The Target Market Determination (TMD) for the Fund is available at [www.pentalgroup.com/ddo](http://www.pentalgroup.com/ddo). You should obtain and consider the PDS and TMD before deciding whether to acquire, continue to hold or dispose of units in the Fund. An investment in the Fund is subject to investment risk, including possible delays in repayment of withdrawal proceeds and loss of income and principal invested.

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If market movements, cash flows or changes in the nature of an investment (e.g. a change in credit rating) cause the Fund to exceed any of the investment ranges or limits specified, this will be rectified by PFSL as soon as reasonably practicable after becoming aware of it. If PFSL does so, it will have no other obligations in relation to these circumstances. The procedures, investment ranges, benchmarks and limits specified are accurate as at the date of this factsheet and PFSL reserves the right to vary these from time to time.

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