Pendal Australian Equities

The consequences of COVID and the next game in equity investment

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Same sport different games …

Post-GFC the investment game changed

Behaviour of key agents shifted as a result of debt overhang

	Pre-GFC	Post-GFC
Households	• Rising Debt • Fallings savings	• Debt reduction • Stable savings
Banks	• Strong credit growth • Increased leverage	• Subdued credit • Re-capitalisation
Central Banks	• Traditional monetary policy	• Unconventional policy
Government	• Balanced budgets	• Balanced budgets
Geopolitics	• China economic integration	• Growing reliance on China
Technology	• Emerging digital model	• Disruption accelerates

Structural and cyclical deflationary forces built

Debt

- Banks and households need to de-gear subdued credit growth and spending

Policy maker caution

- Governments still sought to balance budgets
- Central banks continued to fight the inflation battle

Globalisation

- Optimised supply chains leveraged Chinese labour supply

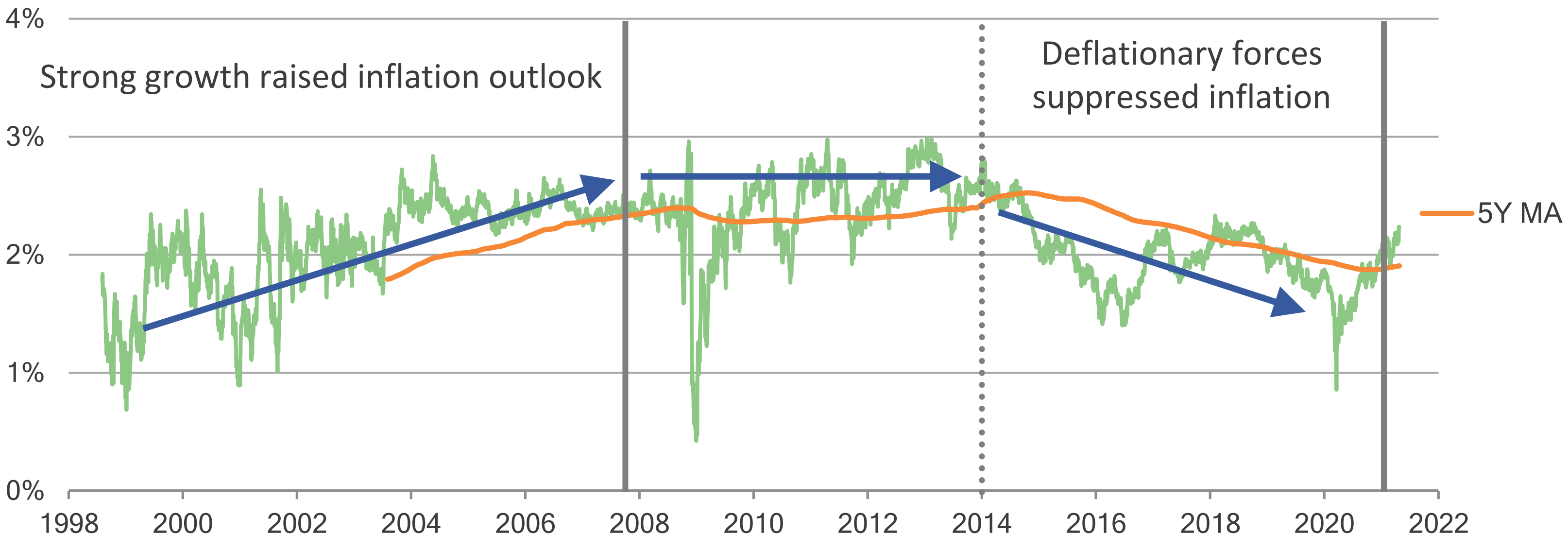
Technology

- Reduced distribution costs and increased pricing transparency

Inflation expectations fell on subdued recovery

Post-GFC the traditional recovery did not eventuate

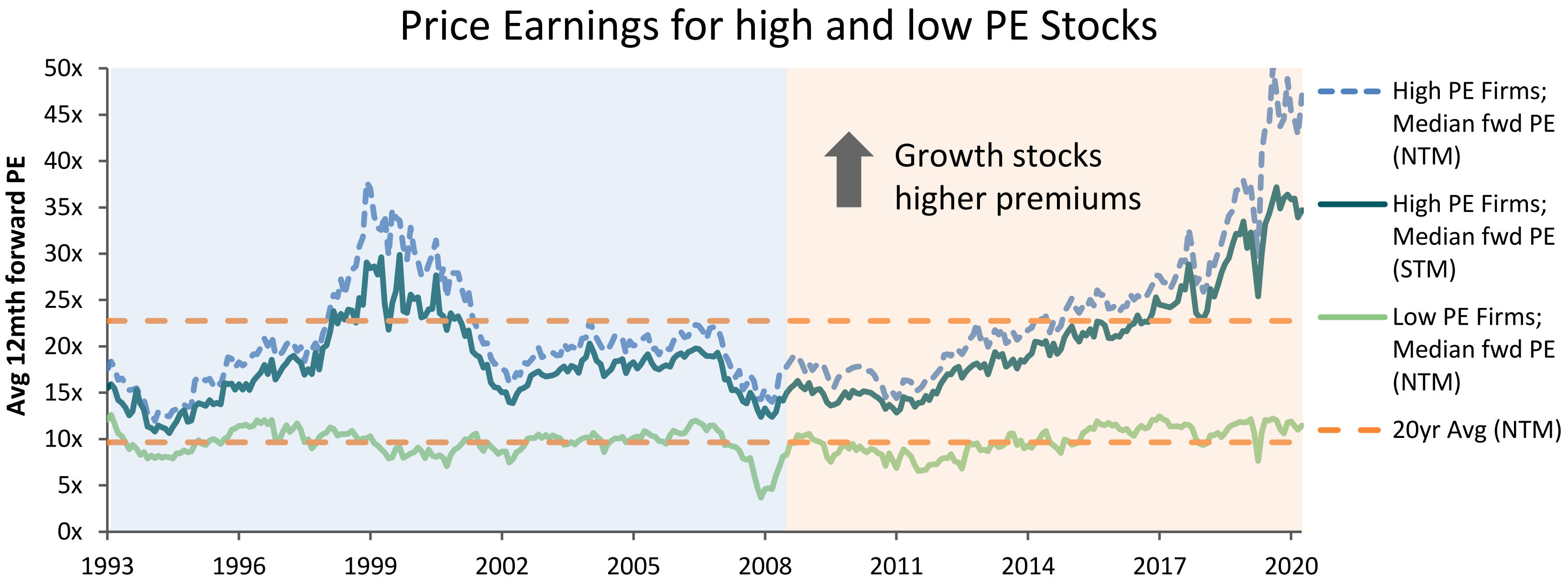
US 5-year inflation expectations 5 years forward



Source: Bloomberg; Credit Suisse; as at 23/04/2021.

Low growth and falling yields fueled growth stocks

Valuation premiums rose persistently post 2009

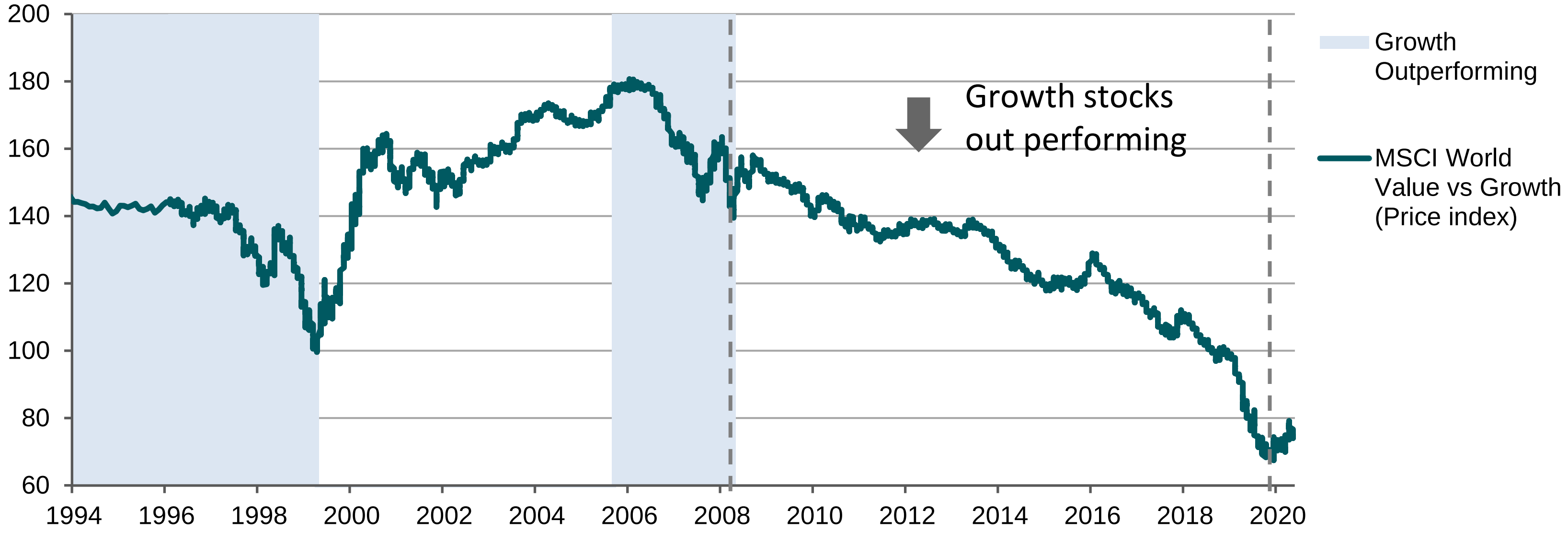


Source: Goldman Sachs as at 31/03/2021.

Growth stocks outperformed through whole period

Factor dominance a function of rates, low growth and disruption

Global Value vs Growth



Source: Bloomberg; Pendal; as at 23/04/2021.

Post-COVID the game is set to change again

Key agents and how their behaviour may now shift

	Pre-GFC	Post-GFC	Post-COVID
Households	• Rising Debt • Fallings savings	• Debt reduction • Stable savings	• Rising Debt • Fallings savings
Banks	• Strong credit growth • Increased leverage	• Subdued credit • Re-capitalisation	• Capacity to lend
Central Banks	• Traditional monetary policy	• Unconventional policy	• Unconventional plus
Government	• Balanced budgets	• Balanced budgets	• Pseudo MMT • Interventionism
Geopolitics	• China economic integration	• Growing reliance on China	• De-globalisation
Technology	• Emerging digital model	• Disruption accelerates	• Continued digitisation • Clean energy transition

Post-COVID era marks a major shift in the game

Policy-makers mindset

- Shift from balanced budgets and inflation to social & sustainability issues

Clean energy transition

- Providing a platform for a resurgence in infrastructure spending

Geopolitics

- Globalisation's deflationary forces may fade as supply chains are disconnected

Household & financial sector financial position

- Repaired balance sheets and higher savings rates gives capacity to lend & spend

There is a major shift in policy makers' goals

Covid crisis and fall-out from post-GFC era has shifted policy focus

1

Reducing Inequality

- Lower unemployment
- Higher real wages
- Improving the safety net

2

Economic resilience

- Resilient supply chains
- Local sourcing
- Protecting key industries

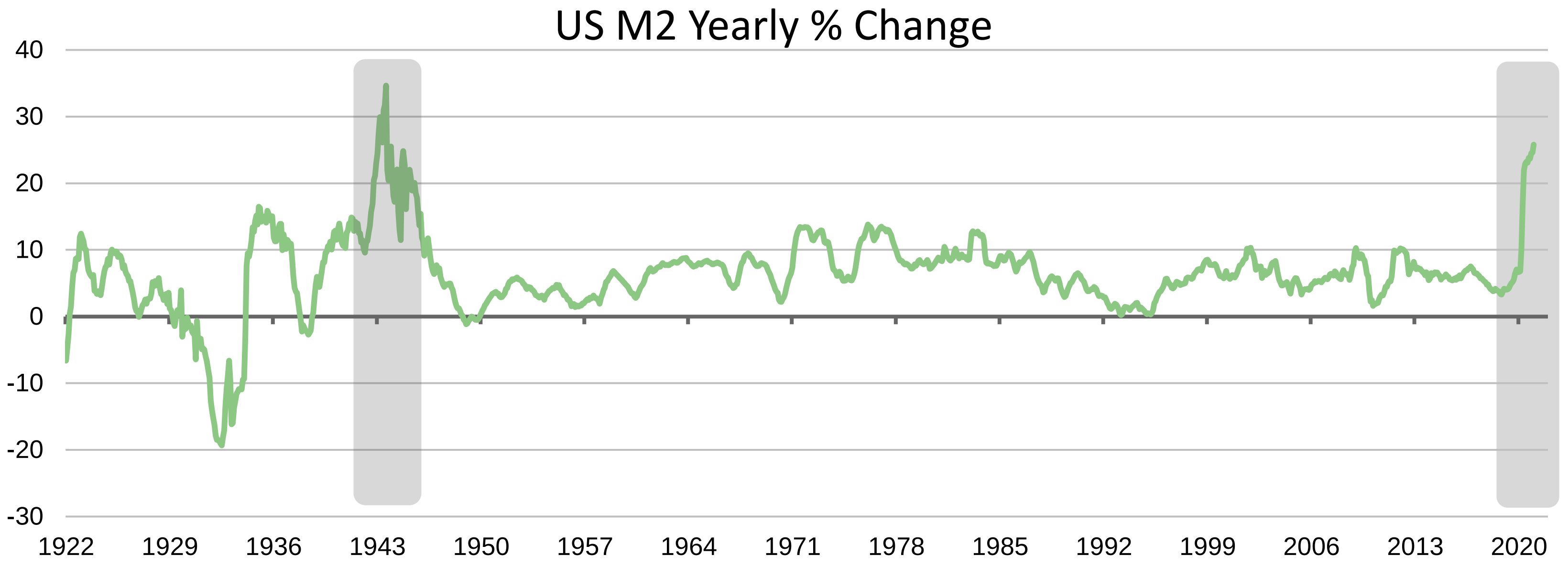
3

Investing in clean energy

- Accelerate renewable shift
- Upgrading power grid
- Promoting shift to EVs

Money supply seeing unprecedented growth

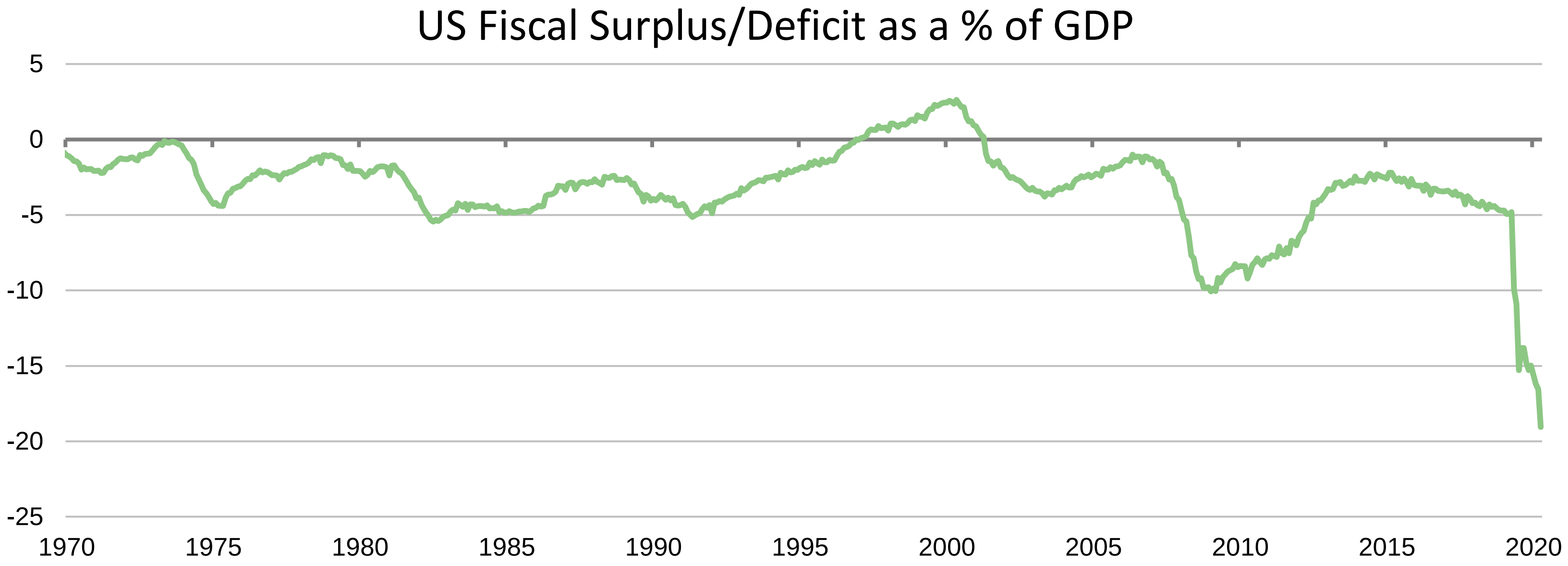
Growth on this scale has broad-based and long-term implications



Source: Bloomberg, JP Morgan; as at 28/02/2021

The tolerance of running fiscal deficits has risen

Ability to fund deficit at low cost opens door to new policy goals

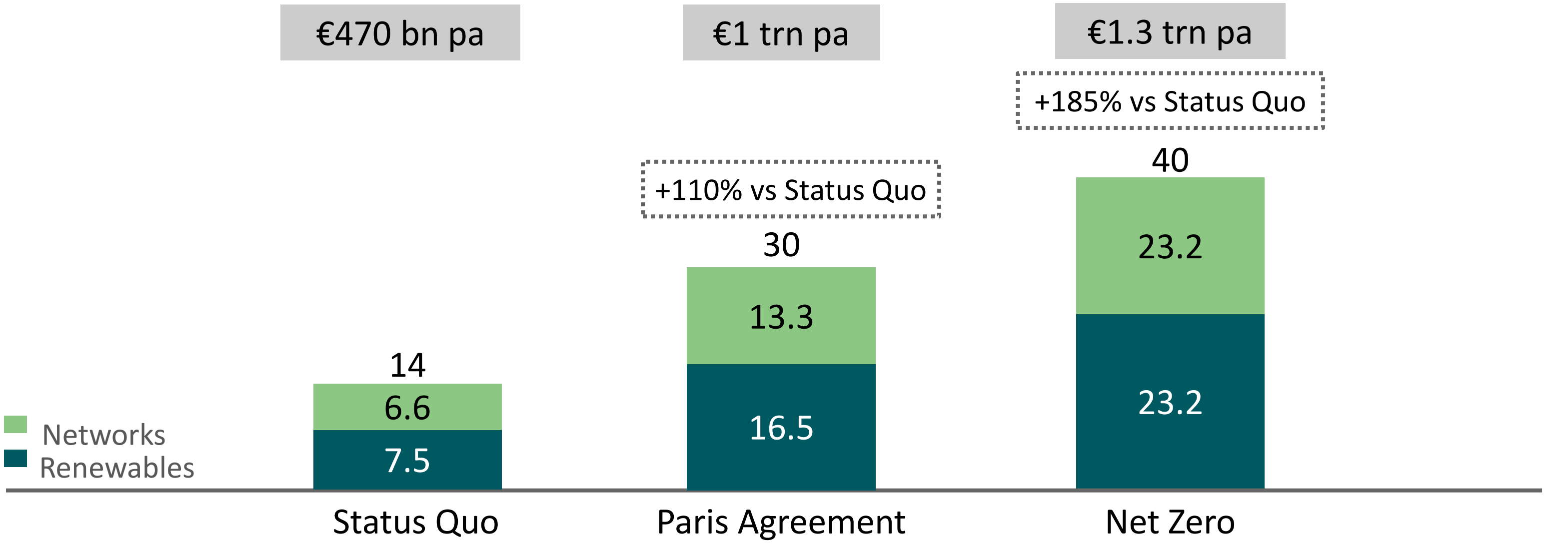


Source: Bloomberg; as at 31/03/2021

Clean energy to boost investment spend

The need to act and ability to fund will drive higher investment

Cumulative investment in clean energy transition over next 30 years (US$tn)

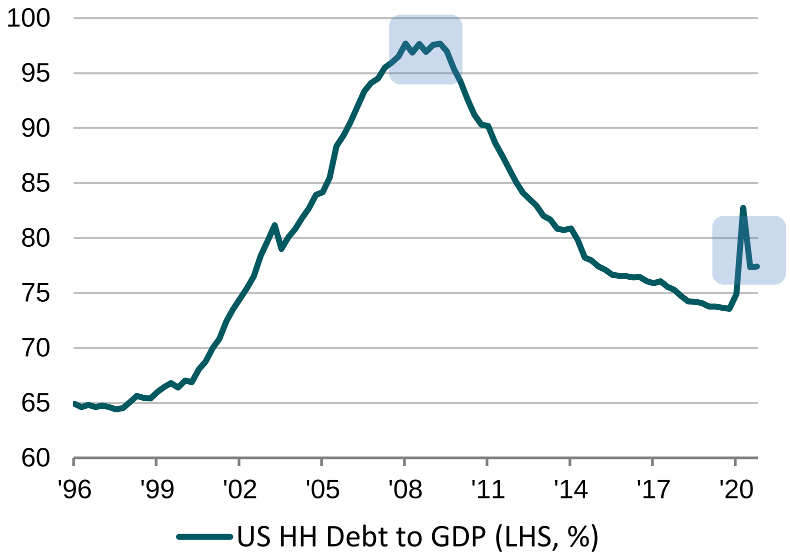


Source: IEA, Goldman Sachs

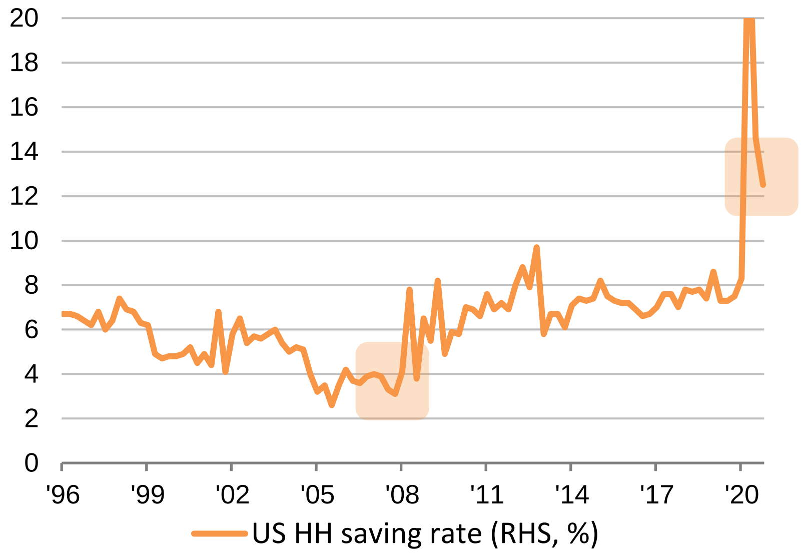
US household financial position in far better shape

Capacity for savings rates to fall can support consumption

US household debt to GDP



US household savings rate



Source: Saving ratio is household net saving to household net disposable income; Bloomberg; data as at 31 Mar. 2021.

The next game – themes and consequences

Stronger economic growth
- Cyclicals as an alternative to growth stocks

Higher bond yields
- Equities benefiting from rising yields

Inflation risks building
- Stocks with pricing power to provide inflation hedge

Higher investment spend
- Companies benefiting from government incentives & resource constraints

Digital disruption
- Growth stocks that can scale with low incremental investment

Sustainability differentiation
- Companies rewarded with lower cost of capital and higher ratings

Building a portfolio for the current environment

Protection against change in policy direction

- Structural growth, low gearing, predictable and strong, free cash flow

Pricing power plays as hedge on inflation risks

- Companies where supply constraints and market position enable price pass through

Franchise leaders

- Companies in good industry structures, strong market positions, high incremental returns

Cyclical winners

- Stocks benefiting from stronger consumption, higher investment avoiding cost pressures