PENGANA CAPITAL

MONTHLY REPORT
SEPTEMBER 2021

PENGANA HARDING LOEVNER INTERNATIONAL FUND

DESCRIPTION

An International Fund targeting superior risk-adjusted returns through investing in high-quality and durable growing companies at reasonable prices.

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The **Pengana Harding Loevner International Fund** invests in high-quality, growing companies identified through fundamental research with a long-term, global perspective.

Pengana has appointed Harding Loevner to managed the Fund. Harding Loevner is a New Jersey-based global equity fund manager formed in 1989 with over US$84billion in Assets under Management.

Harding Loevner' analysts search the world for companies that meet their high quality and durable growth criteria, conduct fundamental research, then value and rate their stocks to make them available to PMs for investment.

STATISTICAL DATA

VOLATILITY[8]	NUMBER OF STOCKS	BETA (USING DAILY RETURNS)[9]
9.5%	73	0.76

PERFORMANCE TABLE

NET PERFORMANCE FOR PERIODS ENDING 30 Sep 2021[1]

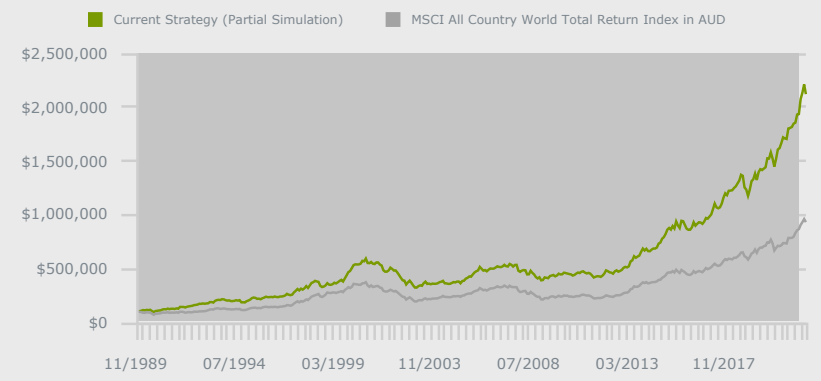
Pengana Harding Loevner International Fund Class B

The Class was established in 1 July 2015. From June 2021 Harding Loevner was appointed as the investment manager for the Fund.

	1M	Since Harding Loevner Appointed June 2021[1]	1Y	3Y	5Y	Since Fund Inception July 2015[2]	Since Strategy Inception November 1989[3]
Fund (APIR PCL0026AU)[1,2] Managed by Harding Loevner from June 2021	-4.1%	9.6%	22.8%	16.6%	16.1%	13.0%	
Current Strategy (Partial Simulation)[4] Harding Loevner Global Equity Strategy			24.1%	15.9%	18.0%	15.2%	10.1%
Index[5]	-3.0%	7.4%	26.4%	12.6%	14.5%	11.8%	7.3%

PERFORMANCE CHART

NET PERFORMANCE SINCE INCEPTION[2]



TOP HOLDINGS (ALPHABETICALLY)

Alphabet Inc	Communication Services
Amazon	Consumer Discretionary
Deere & Co	Industrials
Facebook Inc	Communication Services
First Republic Bank	Financials
Illumina	Health Care
Microsoft	Information Technology
PayPal	Information Technology
SVB Financial Group	Financials
Wuxi Biologics Cayman Inc	Health Care

SECTOR BREAKDOWN

Consumer Discretionary	7.8%
Consumer Staples	1%
Energy	2.1%
Financials	13.3%
Health Care	22.9%
Industrials	11%
Information Technology	22.9%
Real Estate	1.9%
Communication Services	12.8%
Utilities	0.5%
Cash	3.8%

CAPITALISATION BREAKDOWN

Under 5bn USD	2.2%
In between 5bn - 10bn USD	0.8%
In between 10bn - 50bn USD	33.1%
In between 50bn - 150bn USD	24.6%
In between 150bn - 500bn USD	20.4%
Above 500bn USD	15.1%
Cash	3.8%

REGION BREAKDOWN

North America	63.5%
Europe ex-UK	12.2%
Emerging Markets	13.5%
Japan	2.7%
UK	1.8%
Asia Pacific ex-Japan	2%
Australia/New Zealand	0.5%
Cash	3.8%

THE LONG-TERM HEALTH OF CHINA'S SOCIETY AND ECONOMY

COMMENTARY

In September 2021, the portfolio retracted -4.1% compared to a market decline of -3.0% for the same period.

The Global Equity Fund lagged the benchmark, the MSCI All Country World Index, primarily due to weak holdings in Information Technology (IT) and Consumer Discretionary. Strong stock selection in Health Care proved helpful during the month.

In IT, Dutch payment-processing business **Adyen** declined to absent any specific news, apparently caught in a shift from more expensive, long-duration growth companies in response to expectations of higher interest rates. Another case was US software developer **Adobe**, whose shares declined after recently reporting another quarter of strong earnings growth that nevertheless did not satisfy investors' elevated expectations. In Discretionary, US sportswear manufacturer **Nike** cut its sales guidance due to supply-chain challenges, specifically the closure of factories in Vietnam due to COVID-19 outbreaks.

In Health Care, Chinese pharmaceutical contract development and manufacturing company **Wuxi Biologics** reported strong results for the first half of the year, with revenues up 127% and net profits up 163%, both year-over-year. The company is running at full capacity with a strong backlog of projects. Japan's **Sysmex**, a manufacturer of blood-testing instruments has also recently reported good results, with rising revenues and margins.

By region, stock selection in the US weighed on relative returns. Key detractors included **Adobe** and **Nike**, as well as life science products and services company **Illumina**. The company's shares continued to decline after it announced last month it had completed its acquisition of GRAIL (leader in the new field of liquid biopsies) without EU regulatory approval. This action may subject Illumina to future regulatory action. The portfolio's underweight in Japan also hurt performance versus the benchmark.

In the spring of 2020 – in the early stages of the global pandemic – we marveled at the resiliency of the Chinese stock market, which we ascribed to the country's success in containing the domestic spread of the coronavirus through draconian lockdowns, whose efficacy was made possible by its authoritarian political system. Eighteen months later, a similarly authoritarian intervention has this time left investors reeling. While government intervention is not uncommon in China, the scale and pace of this latest crop of reforms are unprecedented. Is Xi, China's most powerful leader since Chairman Mao, revealing his allegiance to a collectivist ideology long thought to be discredited? Or is he boldly grasping the nettle of reform to redress economic imbalances and social ills before they become more entrenched and undermine the Chinese Communist Party's legitimacy?

Despite hyperventilating headlines conjuring memories of the CCP's gruesome past, we accept that on balance the policy changes are intended to benefit the long-term health of Chinese society and economy, especially its middle class. The message the Party is sending to business leaders across China is clear: compete on a level playing field and pay a fair wage. For instance, much of the coverage of Ant Group's cancelled IPO focused on the ostensible desire of the CCP to clip the wings of its tech oligarchs.

More persuasive in our view is that having observed and learned from the West's subprime debacle a decade prior, Chinese financial regulators are not keen to allow loan origination to be divorced from the underlying credit risks of the loans—a source of moral hazard that would potentially destabilize a financial system still dominated by lumbering state-owned banks with weak credit cultures and poor management systems. Antitrust interventions targeting the largest e-commerce platforms echo the statements (if not yet the achievements) of many Western policymakers to improve competition by increasing the bargaining power of smaller businesses versus the giants.

Meanwhile, although the gutting of the private educational tutoring sector may seem disproportionate, it has with the stroke of a pen stigmatized one of the educational advantages of affluence while inhibiting the exam preparation arms race that many middle-class families feel has spiralled out of control. Actions taken to strengthen the data privacy protections of social media companies, tighten local ownership of Macau casinos, and rein in speculation in the high-end liquor market would not be out of place in Europe or the US. Not to minimize the serious consequences of these abrupt and radical reforms for private businesses; as investors, we are viewing these actions mainly as problems requiring further analysis rather than as an indication that China has become too unpredictable to be investable.

More troubling for China's long-term prospects, although less of an immediate danger to our portfolio, is the looming default of Evergrande. For years, the Chinese government has promised to wean the economy from fixed asset investments in favour of consumption, with little to show for the rhetoric. Regional governments have continued to rely on a red-hot property sector to provide their funding and achieve their mandated growth targets. Alarmed by the outsized role of property development in the economy, and the associated risks to the financial system of too much property speculation, the central government pushed through a series of policies last year to force the property sector to deleverage. Evergrande's plight looks like the direct consequence of those blunt top-down mandates as the heavily indebted company started to find itself cut off from its usual credit lines. While the CCP may be happy to make an example of the company, the probable spill-over effects to the rest of the economy will be hard to contain and likely to require yet more interventions.

Equally disturbing to us are the rolling power outages afflicting as many as 20 provinces. Duelling top-down mandates with competing objectives seems to be playing a role here. Earlier in the year, the central government renewed its commitment to "dual control," a mandate to curb carbon emissions by limiting both energy usage and intensity (i.e., the amount of energy used per unit of GDP). That directive was issued, however, without anticipating this year's spike in industrial output, whose emissions far exceed those from less energy-intensive sectors. Now that they have met their local growth targets, regional administrators are rushing to institute power shutdowns to avoid breaching stipulated emission ceilings. Woe be to the regional leaders who fail to shrink their carbon footprint before President Xi goes before the UN Climate Change Conference in early November determined to show that China is no climate backslider.

To be sure, there are other factors contributing to the power crisis—not least, skyrocketing coal prices resulting in part from both extreme weather as well as China's boycott of Australian coal imports in retaliation for that country's insistence on reopening the inquiry into the origins of the COVID-19 virus.

Nobel Prize-winning economist Friedrich Hayek would have predicted that the Chinese government would ultimately fail to manage its economy by mandate because officials can't foresee and prevent every unintended consequence of their own actions. If China's growth slows further, more such shortcomings are likely to surface. The Chinese authorities exhibited competence at virus management but, even when their intentions are good, leaders inevitably miscalculate. When the views of authoritarians are subjected to little debate and their mandates are implemented without checks and balances, miscalculations can have outsized consequences. It's unclear to us when a greater trust in the spontaneous order spawned by private actors and market forces, however, well-mitigated by regulation and taxation, will take hold in China.

FEATURES

APIR CODE	PCL0026AU
REDEMPTION PRICE	A$ 0.986
FEES *	Management Fee: 0.974% Performance Fee: Nil
MINIMUM INITIAL INVESTMENT	$10,000
FUM AT MONTH END	A$ 68.14m
STRATEGY INCEPTION DATE	1 December 1989
BENCHMARK	MSCI All Country World Total Return Index (net) in $A

FUND MANAGERS

Peter Baughan
Portfolio Manager

Jingyi Li
Portfolio Manager

1. Harding Loevner was appointed fund manager as of 10 May 2021. June 2021 represents the first full month of Harding Loevner managing the Fund.
2. Class B Inception date 1 July 2015. Figures shown are calculated from the continuous performance of both the current and previous strategies. For performance see row labelled Fund (APIR PCL0026AU) in the table above which is the continuous performance of both the current and previous (shaded) strategies.
3. Harding Loevner Global Equity Strategy inception 1 Dec 1989
4. Prior to June 2021, the Harding Loevner Global Equity Strategy performance (labelled 'Current Strategy (Partial Simulation)' and shown in the shaded area) includes the strategy performance simulated by Pengana from the monthly gross returns of the Harding Loevner Global Equity strategy. This simulation was done by: 1) the conversion of US-denominated gross returns to AUD, 2) applying the fee structure of Class B. From June 2021 the strategy performance is the performance of the Pengana Harding Loevner International Fund Class B.
5. MSCI All Country World Total Return Index in AUD.
6. Performance for periods greater than 12 months are annualised. Net performance figures are shown after all fees and expenses and assume reinvestment of distributions. No allowance has been made for buy/sell spreads. Past performance is not a reliable indicator of future performance, the value of investments can go up and down.
7. The Harding Loevner Global Equity Strategy performance (shown in the shaded area in the chart, and in the performance table as row labeled 'Harding Loevner Global Equity Strategy) has been simulated by Pengana from the monthly gross returns of the Harding Loevner Global Equity strategy. This simulation was done by: 1) the conversion of US-denominated gross returns to AUD, 2) applying the fee structure of the stated class. Strategy Inception 30 November 1989.
8. Annualised standard deviation since inception.
9. Relative to MSCI All Country World Total Return Index in AUD

* For further information regarding fees please see the PDS available on our website.

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