IWI investor
Pou Tiaki i Ngā Rawa
New Zealand's wealth advisers

Economic & Market Commentary, Quarter End – March 2023

Overview

6.0% p.a.	+1.7%	-1.2%	8.9%	0.6%	21	3
Balanced Portfolio 5-year return	Balanced Portfolio 5-year performance versus peers (per annum)	Balanced portfolio return over year	Best Performing asset class: quarter (Global Equities)	Worst quarterly performing asset class: quarter (Global Listed Property NZDH)	No. of funds on APL	Funds on watch (+2)

Key discussion points

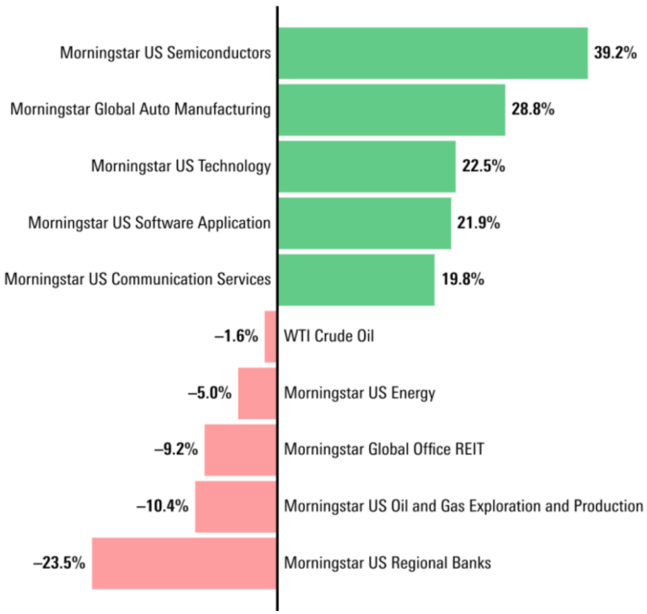
- Market returns were positive over the quarter. International shares posted strong returns, with NZ and Australian equity markets lagging in comparison.
- All model portfolio returns were positive this quarter, with all models also outperforming their respective peer group averages over the quarter and year to March. This has mainly reflected the asset allocation decisions to reduce bond exposures in favour of short duration and alternatives. The longer-term horizons show strong returns and outperformances.
- The majority of funds on the APL continue to perform well, with Dimensional Emerging Markets Sustainability remaining on Watch due to its short history. Dimensional 2-year Fixed Income and Simplicity NZ Shares have entered the Watch zone due largely to poor-peer relative performance.
- As part of our ongoing commitment to assessing the impact of climate risk in your portfolio we have provided a summary of the funds with a low-carbon focus in your portfolio and extended our greenhouse gas emissions analysis across the total growth exposure (shares, property and infrastructure). This analysis shows a material reduction in the greenhouse gas emissions of your portfolio versus a benchmark.

Market Commentary March Quarter 2023

Overview

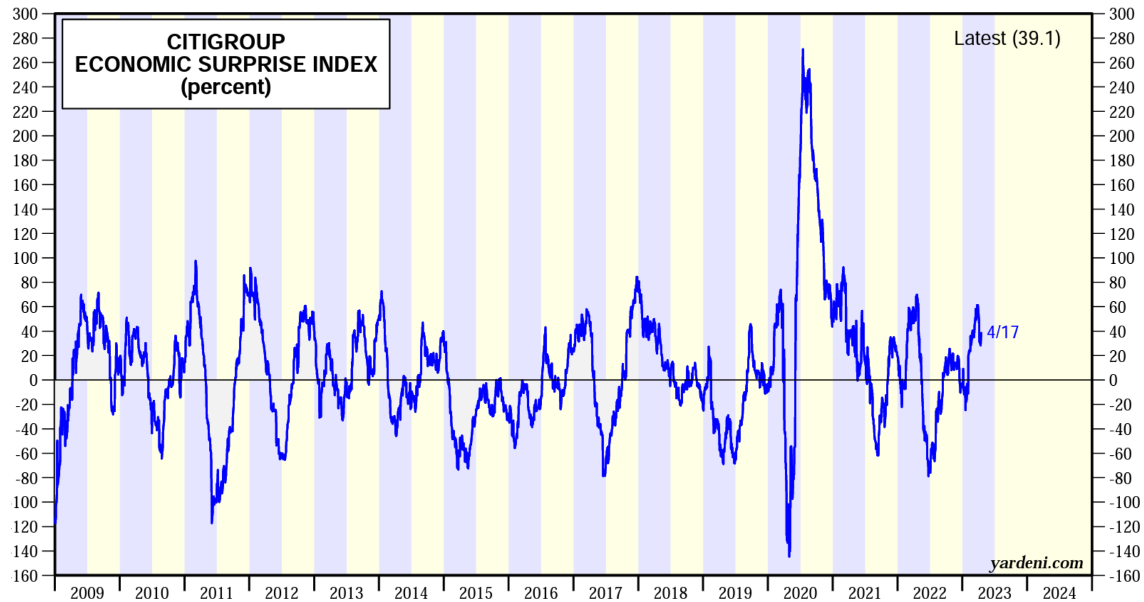
Both equity and bond markets bounced higher in the March quarter, following increasing signs that central banks are getting on top of inflationary pressures. However, the pattern of returns was volatile as shown in figure 1. Equity markets surged in January on the back of reducing interest rate expectations, only to give back most of this gain in February and early March as the banking sector particularly came under pressure with the failure of Silicon Valley Bank. Later in March markets rose again as banking contagion risks receded, and macroeconomic data, in general, reported better than expected (see Figure 2 for the US economy).

Figure 1: Q1 2023 Top & Bottom Performing Sectors



Source: Morningstar Direct, Morningstar Indexes as of 31 March 2023

Figure 2: US data has been positive relative to expectations so far this year



Source: Citigroup, Yardeni Research Inc.

Market Commentary March Quarter 2023

Market roundup

Market performances are reported on the following page. International shares rallied strongly over the quarter, by around 9% in NZD terms and 7.2% in NZD hedged terms. Within global equities, value stocks took a breather and returned only 2% over the quarter, but they still outperformed over 12-months, returning 5.6% in NZD terms. Small caps have fared worse, returning around 5.5% in the quarter, but only 0.7% in the year to March 2023.

Emerging markets returned around 5% over the quarter, slightly stronger than the 3.9% and 3.3% returns posted by the NZ and Australian markets respectively. Over the year to March, however, all performed quite similarly returning around -1%.

NZ and international investment grade (IG) bonds returned around 2.5% in the quarter with some of this gain reflecting a paring back of future rate rise expectations. Over the year to March NZ IG bonds fell around 1%, while international IG bonds fell around 5%.   This difference in performance largely reflects that the RBNZ was generally quicker than offshore central banks to raise rates, and hence the marked-to-market capital losses were incurred earlier in our bond market than most offshore markets.

International property stocks again struggled in the quarter, increasing only 0.6% in NZD hedged terms.   In contrast, global infrastructure performed well once again, returning a handy 2.6% for the quarter and 3% for the year to March 2023. Finally, gold performed well in response to the banking sector stress and increasing efforts being made by Petroleum States and China to reduce their reliance on US dollars for trade settlements.

Bonds and their role in your portfolio.

Bonds play an important role in all but the highest risk portfolios. They provide a predictable income stream, and typically rally in times of stress, providing a portfolio diversification benefit. We assess these benefits to be more certain and material today than they were a year or so ago now that both short term interest rates and bond yields have risen to more normal levels.

We can expect returns of 5% p.a. or more from most NZ and offshore bond funds, whether they are of short or longer-term duration, given their current yields. Most of the bond funds in your portfolio comprise highly rated investment grade (IG) bonds. While issuers of IG bonds very rarely default on their debt obligations, this does not mean that they are risk-free.

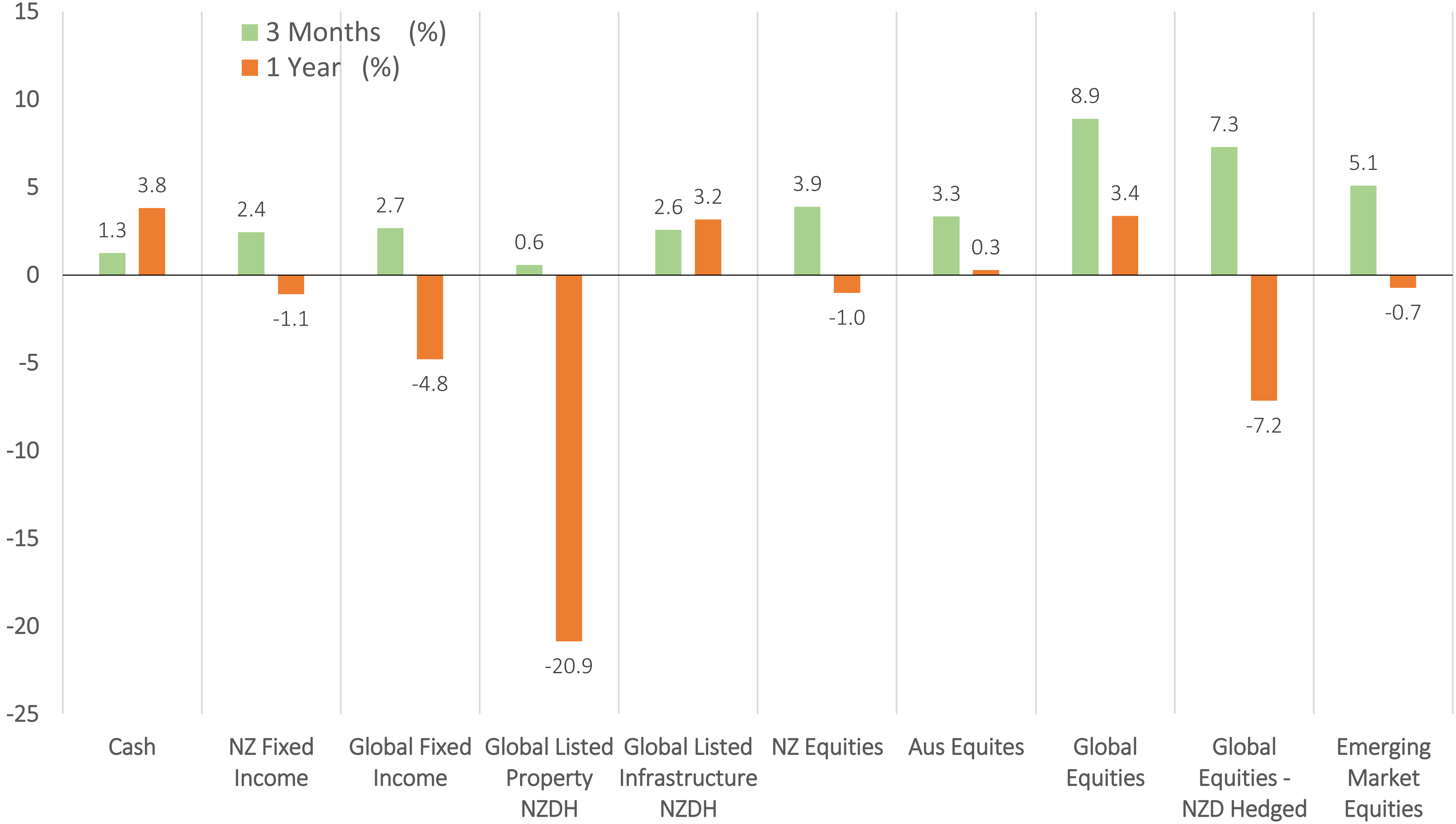
Bonds can still suffer negative returns even when there is no default, for several reasons:

- The assessed creditworthiness of the issuer deteriorates, causing the value of the bond to decrease.
- Interest rates rise by more than is factored into bond prices when they are bought. This is the main reason why bonds suffered a large decline in 2022, and why we advocated for “short duration” bonds earlier to reduce this risk.
- Some bonds may be difficult to sell during times of market stress. In these circumstances the investor may have to sell them at a lower price.
- Finally, most bonds pay a coupon that is fixed and does not adjust for inflation. As such real returns will fall when inflation rises, as it has over the past year.

Your exposure to bonds is in the form of well-diversified bond funds that have been selected in part to mitigate the risks above, and in part because of the strong conviction we have in the selected fund managers due to their track record, SRI credentials, business stability, and operational risk control.

Financial market update

Markets were positive over the quarter, although many markets remain negative over the year



The chart shows asset class returns in New Zealand dollars. The underlying indices are shown in the appendix.
Source: Morningstar Direct, MyFiduciary

Important information

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