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Snapshot

Market insights for investment professionals from Fisher Institutional — December 2017

Bruce McLachlan
Chief Executive

A time to reflect

We are oh so lucky to live in New Zealand. Investors have never had it so good. Not only do we live in this amazing progressive country with a lifestyle to match, we are free to live our lives as we want and also get to spend our hard earned income as we see fit. And this year has offered opportunities such that 2017 has felt like an investment year like no other. Is it the New Zealand share-market being up 19% or the US share-market being up 18%? Or could it be interest rates staying at their lifetime lows? Is it A2 Milk going up nearly 400%? You could be excused for thinking any of these could be the standout event in investing in 2017, but in reality all of these are indicative of the investing party that we have seen in 2017. In addition, there has been the crypto currency bubble taking Bitcoin from $1500 at the start of the year to $16,000USD now. Bring out the champagne if you speculated on Bitcoin!

Of great note has also been the recent release of the Legatum Prosperity ranking of 148 countries (see prosperity.com). This ranks New Zealand as the second most prosperous country in the world in 2017, behind Norway. In 2016 New Zealand was number 1 so our privileged position is not new. What this study does though, is rank prosperity across 9 broad based measures including business environment, governance, health, education, freedom and safety amongst others.

We all know New Zealand is far from perfect, however sometimes we have to be reminded by others just how good we have it here.

Despite the very good times, 2017 has also been a year when the public have said they want changes. There have been concerns regarding those being left behind, housing affordability and the environment. That is the challenge for the new government, while not damaging the already high relative prosperity New Zealand enjoys.

So as we wrap up 2017, has Fisher Funds committed enough to the wishes of you, our clients? Investment returns have overall been very strong, and I have had only very favourable feedback from investors in that regard. 2017 has been a gem. We have had mostly favourable feedback (but not from all of you) to our new commitments on responsible investing and especially the ban on investing in thermal coal extraction. Overall, the Fisher Funds active management philosophy only investing in quality (and responsible) companies enables us to stay current with investor expectations, in a way that passive index tracking funds will never be able to do.

As we look forward to 2018 most investors understand many asset markets are at very high valuations. That does not mean in itself that the party ends with a crash, but does mean markets are unlikely to replicate the performance of 2017. The Fisher Funds investment team may have their work cut out to navigate through any uncertainty, but are up to the challenge.

Thank you for your custom in 2017. We are aware that our clients have many many choices of where they can invest their money, and we are very proud that you continue to support Fisher Funds. I know some of you were a little concerned with Carmel stepping down as Managing Director, and hopefully you can see we are continuing to build on the fantastic legacy Carmel and her husband Hugh created. Carmel is also keeping a watchful eye as she has continued as a Director!

From all of the team at Fisher Funds we wish you a fantastic holiday season, and look forward to continuing our association in 2018 and hopefully beyond.

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Green light for 2018 share market

Frank Jasper
Chief Investment Officer

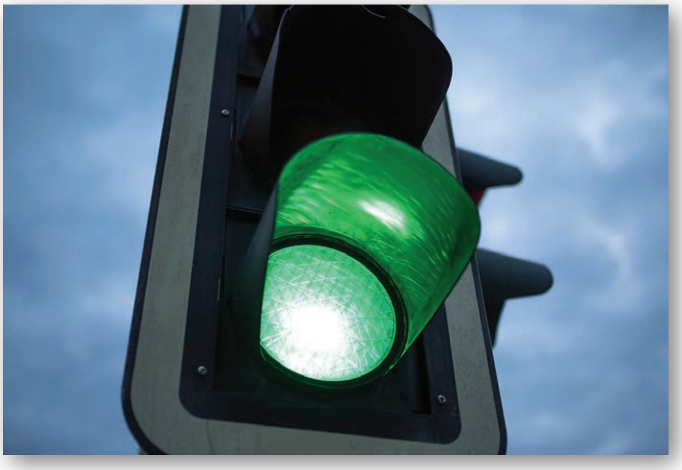
It has been a wonderful year for markets and most investors will enjoy looking at their KiwiSaver balance or investment portfolios, which will look a lot healthier than they did at the start of 2017. Markets have been carried higher on the back of rosy economic growth, which for the first time since the Global Financial Crisis is showing coordinated strength all around the world.

For those of us who have been around for a few years while we enjoy strong markets there is always the question about whether they can continue and for how long. One of the frameworks we take into consideration in order to answer that question is our "traffic light indicator", an assessment of the risks that typically point to market downturns.

The good news is that right now most potential risks that typically point to corrections are not that evident in markets. In fact we see plenty of green lights supporting continued healthy returns. There is only one key red light on the horizon, which while this is something we are monitoring, in our opinion it is unlikely to be enough to derail the strong run of markets into 2018.

The only red light we see is the level of debt that companies have right now. This is very high by historical standards. While this is of some concern, it is a logical outcome of the very low interest rates experienced since the Global Financial Crisis. Companies have taken advantage of this by borrowing money at low interest rates and buying back their own shares. This has been good for shareholders but could go awry if for some reason company earnings come under pressure or interest rates rise dramatically.

There are some things that are flashing amber. We are monitoring these closely to see if conditions deteriorate further but for now they would not stop us being



comfortable owning shares. Top of the list of these concerns are equity valuations which are stretched, the fact that interest rates look to have bottomed and that investors on the whole seem too complacent. Complacency manifests itself in many ways including the lack of market volatility, which could signal investors increased willingness to take on more risk.

The reason we remain comfortable with the outlook for shares is many of the typical indicators of market stress are just not flashing any warnings whatsoever. There are plenty of green lights. Inflation is well and truly under control, economic momentum is strong, company profits are growing and wage demands are modest and not impacting profit margins. These measures all suggest a healthy outlook for 2018.

While our traffic light risk indicator system is no guarantee that markets will behave next year they certainly give me the confidence to face Xmas dinner without worrying about a financial market hangover from 2017. Now just need to avoid eating too much!

Responsible Investing: it's more than ruling out industries

Mark Brighouse
Chief Investment Strategist

Responsible investing has become an increasingly important part of the investment landscape in New Zealand in the last 18 months. This has seen the majority of KiwiSaver providers introduce this in some form or another. With everyone having their own different approaches you may be wondering what exactly constitutes responsible investing? Like many things in life it is up to interpretation. For some investors it is merely ruling out the worst industries and not investing in them. This exclusion approach may involve, for instance not investing in some armaments companies. For us an active manager on your wealth this broad brush exclusion approach is simply the start to truly investing in a responsible way.

We have ingrained responsible investing as a fundamental part of our investment framework. As an active fund manager we believe that it is more than just the right thing to do, it also helps us identify the best companies and the worst companies in the world. In our view managing a business to be truly sustainable is one of the many indicators that points to a company's long term success. We apply our responsible investing overlay in two distinct ways.

The first of these is the more typical broad brush industry exclusions on manufacturers of tobacco, weapons that cause indiscriminate/ disproportionate harm and, somewhat unusually in New Zealand, thermal coal producers. Our process doesn't stop there. Our second pillar of responsible investing is to evaluate the corporate conduct of companies. This means looking at a company's behaviour from an environmental, social and governance perspective. We use this information in both a positive way, to identify companies with sound records of sustainability but also to exclude companies with poor sustainability track records.

To do this we partner with research agencies who help us collate a wide range of information and data from sources that provide deeper insight into the culture and operating principles of companies. One such source is people on the ground from Non Government Organisations. A great example of this is feedback that is gathered from Amnesty International staff and volunteers who deal with workers first hand and observe the day to day conditions of that they face. This type of feedback can help identify those companies who have a sustainable long term approach to labour relations and those who don't.

This information, combined with our own observations and research, helps us form a picture of a company's conduct. This is taken into consideration when forming our exclusion list of the companies that we will not invest in on the basis of the way they operate. Altruistic and environmental purposes aside, there is sound economic reasoning why companies with a poor record of corporate misconduct should be avoided. Recently published research by MSCI, a well-respected research house for institutional investors found that exclusions of the worst types of corporate wrongdoing had a "mildly positive effect on returns." The way I look at these results is that while making decisions on this basis of corporate conduct alone is not a silver bullet to guarantee good returns, it definitely helps and we are always looking for every edge we can identify. We continue to believe investing responsibly is investing wisely.

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Market Movements

As at 30 November 2017

Stock Markets*	Closing Values	Changes over: 1 Mth %	3 Mths %	6 Mths %	12 Mths %
S&P Developed LargeMidCap - (Local Curr)	733	1.5	6.7	8.6	21.4
S&P Developed LargeMidCap ($NZ)	N/A	1.5	11.6	12.5	25.6
S&P Global LargeMidCap ($NZ)	N/A	1.8	10.8	14.0	29.6
USA - S & P 500	5155	3.1	7.6	10.9	22.9
USA - Nasdaq	7897	2.3	7.2	11.5	30.5
Japan - Topix	2605	1.5	11.7	15.4	24.5
UK - FTSE100	6208	-1.8	-0.7	-0.7	12.3
Germany - DAX	13024	-1.6	8.0	3.2	22.4
France - CAC40	13658	-2.3	5.9	2.4	21.1
HK - Hang Seng	78732	3.4	4.9	16.9	33.0
Australia - S & P 300	58634	1.7	5.8	6.9	14.7
NZ-S&P/NZX 50 Gross Index (inc imp credits)	9757	0.6	5.3	11.1	20.2
NZ-S&P/NZX 50 Gross Index (excl imp credits)	8187	0.5	4.7	10.4	18.7
Market Volatility - VIX	11.3	10.8	6.5	8.4	-15.4

New Zealand Property		%	%	%	%
S&P/NZX All Real Estate (inc imp credits)	1249.9	3.6	4.0	5.6	9.2
S&P/NZX All Real Estate (exc imp credits)	1220.7	3.6	3.8	5.1	8.1

Ten Year Bonds	%	Yield Changes			
USA	2.35	-0.01	0.14	0.05	0.21
Japan	0.03	-0.03	0.03	-0.01	0.02
United Kingdom	1.33	0.00	0.29	0.28	0.05
Australia	2.50	-0.17	-0.21	0.11	-0.23
New Zealand	2.73	-0.19	-0.17	-0.05	-0.27

90 Day Interest Rates	%	Yield Changes			
USA	1.25	0.16	0.22	0.35	0.80
Japan	0.67	0.61	0.62	0.62	0.62
United Kingdom	0.52	0.08	0.24	0.23	0.14
Australia	1.74	0.05	0.03	0.01	-0.02
New Zealand	1.91	-0.03	-0.05	-0.06	-0.13

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Bond Indices	Closing Values	Changes over: 1 Mth %	3 Mths %	6 Mths %	12 Mths %
S&P/NZX Bank Bills 90-Day	702.41	0.17	0.49	0.99	2.03
S&P/NZX NZ Government Bond Index	1665	0.82	1.38	1.54	4.43
Barclays Capital Global Aggregate Index (Hedged NZD)	N/A	0.22	0.31	1.51	4.15

Hedge Funds & Commodities		%	%	%	%
HFRX Global Hedge Fund Index (USD)	1266	0.1	1.4	2.8	6.1
DJ-UBS Commodity Index Total Return	175	-0.5	1.5	4.0	0.5
Gold (US$/ounce)	1273.20	0.5	-3.3	0.1	8.7
Oil (US$/barrel)	62.65	2.1	18.9	26.8	30.7

Currencies		%	%	%	%
NZD / USD	0.6863	0.2	-4.2	-3.3	-3.2
NZD / EUR	0.5755	-2.1	-4.5	-8.8	-13.9
NZD / GBP	0.5070	-1.7	-8.8	-7.8	-10.6
NZD / AUD	0.9040	1.2	0.1	-5.2	-5.8
NZD / YEN	76.79	-1.3	-2.6	-2.2	-4.9
Trade Weighted Index	73.11	-2.2	-5.2	-3.2	-6.2

**Total Return Indices. Indices are net of offshore tax.*
Source: Thomson Reuters Datastream

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