

Snapshot

Market insights for investment professionals from
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An impact of earthquake proportions



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Chief Executive Officer

Thomas Richter invented the Richter scale. This is a logarithmic scale based on the factor of 10, for example, an earthquake of 6 has 10 times the energy of an earthquake of 5. The impact of earthquakes is something very close to the hearts of New Zealanders as we are more than familiar with the colossal impacts they can have on people's lives, communities and the economy at large. The 2011 Christchurch earthquake materially affected the lives of 350,000 people, and will cost circa \$50b and take around 15 years to rebuild the city. The real impacts will be far greater and longer than this.

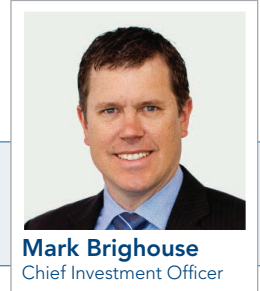
Four years before the Christchurch earthquake, the Clark/Cullen Labour government launched KiwiSaver. The 10th birthday of this event has just passed and is a great time to reflect on the wider impacts on New Zealand, investment markets and individuals. With total savings nearing \$41b and 2.7m KiwiSaver members, it is fair to say that today KiwiSaver has changed New Zealand for good. However, these numbers are only part of the story.

The really interesting numbers are not where KiwiSaver balances are today after ten years, but the scale at which they are increasing. Treasury's latest estimates have KiwiSaver balances doubling every three to four years, meaning the impacts over time are on a logarithmic basis, although not quite at the Richter scale level. Even then, New Zealand trails many other nations in preparing for retirement.

Many countries who have had a long term commitment to retirement savings (e.g. Australia, UK, USA, Canada, Switzerland and The Netherlands) have pension assets of over 100% of their national GDP. New Zealand's current GDP is \$265b, which dwarfs the current \$41b saved in KiwiSaver. So while KiwiSaver has been a success so far, we've only just begun. When New Zealand matches the maturity of these other western nations, the average KiwiSaver balance will be more like \$100,000 per member, rather than the existing \$15,000.

This month's newsletter is unashamedly about the last ten years in investment markets and the impact of KiwiSaver. Sometimes it is important to reflect. While people will contemplate major events like the GFC or the Christchurch earthquakes, ongoing everyday game changers like KiwiSaver can be forgotten.

As an aside, it was interesting witnessing Wellingtonians guessing the magnitude of aftershocks following the 7.8 Kaikoura earthquake of 2016. People get pretty good at this and our Christchurch citizens are expert at it. It's time to get New Zealanders similarly engaged in estimating their KiwiSaver balances. This really can have an impact of earthquake proportions.



KiwiSaver investors rewarded for going the distance

Warren Buffett often says that we should only buy shares that we would be happy to hold if the market were to shut for the next ten years. This has always been a useful test when choosing an investment. Am I confident enough in the investment to not look at it again for ten years and to not care what the price does in the meantime?

Well, people who signed up to KiwiSaver in 2007 have now had a ten year timeframe. If they hadn't opened a newspaper or turned on the TV over the past decade, they would have avoided an enormous amount of angst about market turmoil. Not only that, they could now be looking at their balances, feeling good about their progress and mistakenly concluding that it must have been a pretty dull old time in the markets for the past ten years.

What they would have missed is the Global Financial Crisis, or GFC, which caused sharemarkets to halve in value, numerous housing markets around the world to collapse and left many people financially ruined. The first events of the GFC were actually unfolding only a month after KiwiSaver launched in July 2007. French bank BNP Paribas froze three of their funds that held sub-prime loan exposure in what was the first move by a major bank to acknowledge the rising risk of such investments.

That led to much debate in the early years of KiwiSaver about whether growth-oriented funds were a good idea. Everyone knew that a long term investment plan should include a considerable weighting toward shares, but as prices fell more conservative funds were doing so much better. An investor who ignored all this short term turmoil and focused on their long term goals would have enjoyed the stronger returns from share markets that followed from 2009 as you can see in the following table.



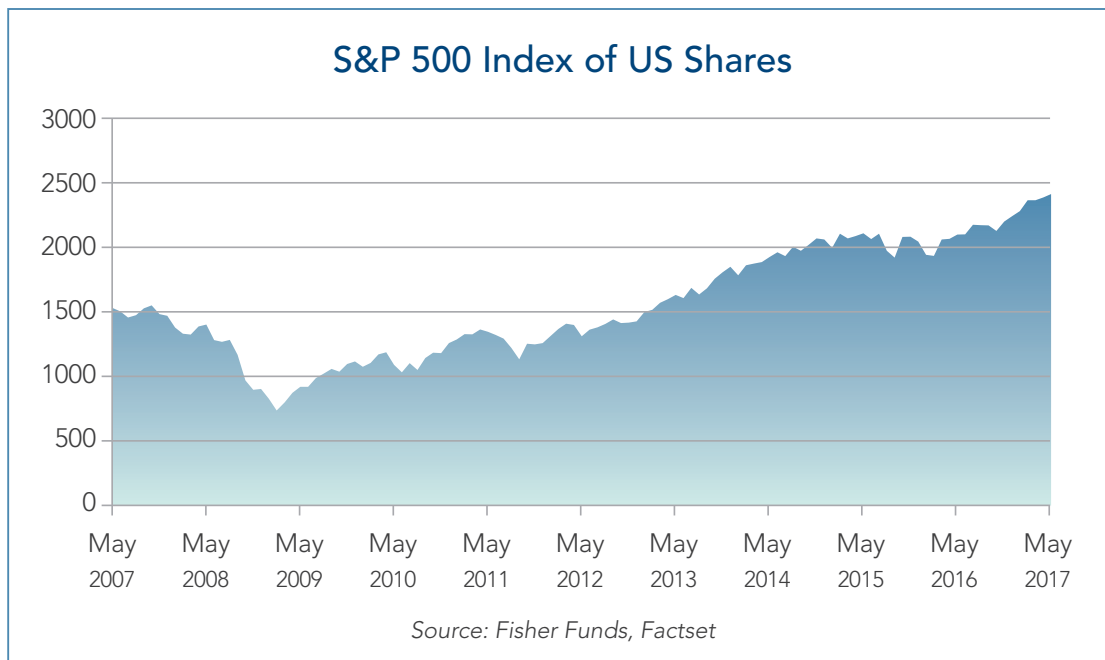
Share market index	Total returns 30/06/07 to 09/03/09	Total returns 10/03/09 to 30/06/17
NZX50 Index of NZ Shares	-41.7%	+208.3%
S&P 500 Index of US Shares	-53.1%	+326.5%

Who would have thought that a retirement saving scheme that kicked off just ahead of the GFC would end up delivering success for so many people ten years later? Much of this is due to a triumph of the long term over the short term. The chart below of the S&P 500 Index clearly illustrates the journey KiwiSaver investors have been on and ultimately profited from.

Any KiwiSaver members who heeded Buffett's advice and were able to pretend the market was closed for the decade and ignored any short term news would have stuck with their strategy and kept on contributing; this is what would have led to the balances they are seeing now.

This type of investor would also have missed a host of other distractions in addition to the GFC including: a plunge in commodity prices, deflation in China, tension in the Eurozone, negative interest rates, the UK's Brexit vote and, of course, the US election of Donald Trump.

Every single one of these events came with dire predictions about the end of the world as we know it and could easily have prompted a KiwiSaver investor to abandon their saving plan. But as we stated earlier, sticking with a strategy you will be happy to hold for ten years, regardless of what the price of the investment does during that time, is a good way to ensure that you don't get distracted by the news.



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Market Movements

As at 30 June 2017

Stock Markets*	Closing Values	Changes over:			
		1 Mth %	3 Mths %	6 Mths %	12 Mths %
S&P Developed LargeMidCap — (Local Curr)	676	0.1	3.1	8.9	19.9
S&P Developed LargeMidCap (\$NZ)	N/A	0.1	1.6	6.9	20.3
S&P Global LargeMidCap (\$NZ)	N/A	-2.6	-0.2	6.6	16.3
USA — S & P 500	4678	0.6	3.1	9.3	17.9
USA — Nasdaq	7022	-0.9	4.2	14.7	28.3
Japan — Topix	2324	3.0	6.8	7.4	32.2
UK — FTSE100	6097	-2.4	1.0	4.7	16.9
Germany — DAX	12325	-2.3	0.1	7.4	27.3
France — CAC40	12979	-2.7	2.4	8.1	24.8
HK — Hang Seng	68302	1.4	8.5	19.5	27.8
Australia — S & P 300	54993	0.2	-1.6	3.1	13.8
NZ-S&P/NZX 50 Gross Index (inc imp credits)	9018	2.7	5.9	11.3	11.7
NZ-S&P/NZX 50 Gross Index (excl imp credits)	7611	2.6	5.8	10.6	10.4
Market Volatility — VIX	11.2	7.4	-9.6	-20.4	-28.5

New Zealand Property		%	%	%	%
S&P/NZX All Real Estate (inc imp credits)	1202.2	1.5	4.4	6.1	1.8
S&P/NZX All Real Estate (exc imp credits)	1176.6	1.3	4.1	5.5	0.6

Ten Year Bonds	%	Yield Changes			
USA	2.19	-0.11	-0.29	-0.30	0.55
Japan	0.08	0.04	0.02	0.05	0.32
United Kingdom	1.26	0.21	0.12	0.16	0.39
Australia	2.60	0.21	-0.09	-0.16	0.61
New Zealand	2.98	0.20	-0.21	-0.29	0.74

90 Day Interest Rates	%	Yield Changes			
USA	1.00	0.10	0.25	0.49	0.73
Japan	0.06	0.00	0.00	0.00	0.00
United Kingdom	0.00	-0.29	-0.34	-0.37	-0.56
Australia	1.71	-0.02	-0.08	-0.10	-0.25
New Zealand	1.98	0.01	-0.02	-0.02	-0.43

	Closing Values	Changes over:			
		1 Mth %	3 Mths %	6 Mths %	12 Mths %
Bond Indices					
S&P/NZX Bank Bills 90-Day	696.67	0.16	0.51	1.02	2.21
S&P/NZX NZ Government Bond Index	1628	-0.74	1.36	2.77	0.19
Barclays Capital Global Aggregate Index (Hedged NZD)	N/A	-0.20	1.22	2.00	0.91

		%	%	%	%
Hedge Funds & Commodities					
HFRX Global Hedge Fund Index (USD)	1236	0.3	1.0	2.7	6.1
DJ-UBS Commodity Index Total Return	168	-0.2	-3.0	-5.3	-6.5
Gold (US\$/ounce)	1240.70	-2.5	-0.5	7.9	-5.9
Oil (US\$/barrel)	48.74	-1.3	-6.6	-11.3	1.4

		%	%	%	%
Currencies					
NZD / USD	0.7322	3.2	4.7	5.0	2.8
NZD / EUR	0.6420	1.7	-1.8	-2.9	0.1
NZD / GBP	0.5637	2.5	0.8	-0.1	5.8
NZD / AUD	0.9546	0.1	4.2	-0.9	-0.2
NZD / YEN	82.27	4.8	5.6	1.2	12.6
Trade Weighted Index	77.92	3.2	1.8	-0.3	3.6

*Total Return Indices. Indices are net of offshore tax.

Source: Thomson Reuters Datastream

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