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# Snapshot

## Market insights for investment professionals from Fisher Institutional — September 2018

**David McLeish**
Senior Portfolio Manager — Fixed Interest

## Chinese credit rating woes

News last month that the Chinese credit rating agency, Dagong Global Credit Rating, had its licence suspended is yet another chapter in the less-than-illustrious history of the credit rating industry.

Irregularities that include giving companies higher credit ratings than their financial standing would otherwise have deserved, in return for cash, are just part of a laundry list of activities Chinese authorities claim to have exposed at the company.

I'm not suggesting for one minute that fraudulent practices such as these are anything other than an isolated incident. But the fact remains, this is an industry which has struggled with credibility even well before it's more pervasive practices of assigning triple-A ratings to toxic structured products that contributed to the Global Financial Crisis a decade ago.

### The importance of research

There is an exhaustive and compelling body of research that documents the many failures of credit rating agencies to fulfil their primary role. That is, to warn investors of the true risks entailed in the financial assets they rate.

This, in my opinion, is far less about errors in judgement by the men and women conducting the research at these agencies though. Instead it is far more about the perverse incentive structure inherent in the industry's issuer-pays business model. That is to say, when the company you are meant to be critically analysing is the same one paying you for this service, a very clear conflict of interest exists.

When combined with rigid, backward-looking, and often unnecessarily complex rating models it is a constant source of wonder to me how anyone would knowingly rely on credit ratings as a guide to the perceived safety of a fixed income investment.

Despite these obvious deficiencies, the investment industry remains wedded to these agencies and their less-than-sufficient ratings. Be it passive funds that use these ratings to scale portfolio exposures or do-it-yourself investors who don't have the expertise to assess credit risks themselves, the implications are significant and wide-ranging.

### Trust matters

This is yet another strong reminder that there are no short cuts in investing. Ensuring your money is managed by trusted, experienced professionals who conduct thorough, transparent, and independent research is the least you can do to protect your money.

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**Frank Jasper**
Chief Investment Officer

## Robust trumps resilience

The theme for this year's Sorted money week is building financial resilience. Resilience is defined by the ability and speed taken to recover from a shock. This is a laudable goal.

Our job as active investment managers is to go one step beyond resilience. It's to build portfolios that are robust in periods of market turmoil. If we do this well we can reduce losses, reducing the shock to your finances and hopefully calling for a little less resilience. The ability to recover is important but I would rather lose less in the first place.

As active investment manager we have a raft of tools at our disposal to build robust portfolios that help protect your wealth. These include:

Building robust multi-asset strategies – the building blocks of our multi-asset portfolios like KiwiSaver and the recently launched multi-asset class managed funds are a range of different types of assets, shares, property and fixed interest, based in New Zealand and around the World. This multi-asset approach puts robustness at the front and centre of portfolios. Each asset type, and often assets in different parts of the World, perform differently at different times. Very importantly some investments like fixed income tend to perform well when shares are performing badly. Having fixed income acts as an important protection in times of share market stress.

Changing asset mix as conditions change – not only does the mix of multi asset portfolios help protect your investments in but we can change this mix responding to shorter term market conditions. This can be an important source of extra returns as well as managing risk. At present we are worried about rising interest rates outside of New Zealand. As a consequence, right now, we own a lot less in international fixed income than usual preferring to invest your money at the higher interest rates we expect will be coming. Similarly we think that inflation in New Zealand will rise and have invested in inflation indexed bonds. These bonds benefit from increases in the consumer price index. These shorter term portfolio tilts are an important tool in building more robust portfolios.

A quality approach does better in tough markets – the STEEPP investment process that we use for selecting hand-picked portfolios of shares in New Zealand and Australian markets emphasises quality, growing companies. Quality companies typically perform better than the average company in challenging markets. The reasons for this make sense. Quality businesses typically have less debt, tend to have profits less tied to the direction of the economy, are growing and have business models that are protected from competition. All of these attributes protect profits and are increasingly valuable in difficult times.

Using falling prices wisely – falling share prices get a lot of headlines but it is not all bad news. Periods of market stress often enable us to buy shares in high quality, growing companies at very attractive prices. It's like your favourite restaurant is on special – you should be dining out every night and enjoying the best steak in town. The great news from buying shares rather than steak on special is that it's even good for your health, in this case the long term health of your wallet.

Sorted is right. Building your financial resilience is important. We work hard to do our part by delivering robust portfolios designed to protect your wealth should, as will inevitability happen, we face more difficult market environments.

## Contact us


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# Market Movements

## As at 31 August 2018

| Stock Markets* | Closing Values | Changes over: 1 Mth % | 3 Mths % | 6 Mths % | 12 Mths % |
|---|---|---|---|---|---|
| S&P Developed LargeMidCap - (Local Curr) | 784 | 1.3 | 4.7 | 5.7 | 14.3 |
| S&P Developed LargeMidCap ($NZ) | N/A | 1.3 | 7.9 | 12.2 | 20.2 |
| S&P Global LargeMidCap ($NZ) | N/A | 3.3 | 9.2 | 11.3 | 20.7 |
| USA - S & P 500 | 5731 | 3.3 | 7.8 | 8.0 | 19.7 |
| USA - Nasdaq | 9388 | 5.9 | 9.2 | 12.1 | 27.5 |
| Japan - Topix | 2556 | -1.0 | -0.5 | -0.7 | 9.6 |
| UK - FTSE100 | 6508 | -3.3 | -2.0 | 5.4 | 4.1 |
| Germany - DAX | 12364 | -3.4 | -1.9 | -0.6 | 2.6 |
| France - CAC40 | 14157 | -1.9 | 0.6 | 4.4 | 9.8 |
| HK - Hang Seng | 77410 | -2.1 | -6.9 | -7.2 | 3.1 |
| Australia - S & P 300 | 63973 | 1.4 | 6.0 | 7.2 | 15.4 |
| NZ-S&P/NZX 50 Gross Index (inc imp credits) | 11174 | 4.5 | 7.8 | 11.9 | 20.5 |
| NZ-S&P/NZX 50 Gross Index (excl imp credits) | 9313 | 4.4 | 7.6 | 11.2 | 19.1 |
| Market Volatility - VIX | 12.9 | 0.2 | -16.7 | -35.2 | 21.4 |

| New Zealand Property | | % | % | % | % |
|---|---|---|---|---|---|
| S&P/NZX All Real Estate (inc imp credits) | 1364.1 | 1.6 | 5.0 | 10.9 | 13.6 |
| S&P/NZX All Real Estate (exc imp credits) | 1322.6 | 1.6 | 4.7 | 10.4 | 12.5 |

| Ten Year Bonds | % | Yield Changes | | | |
|---|---|---|---|---|---|
| USA | 2.86 | -0.10 | 0.03 | -0.01 | 0.65 |
| Japan | 0.10 | 0.03 | 0.06 | 0.05 | 0.10 |
| United Kingdom | 1.43 | 0.09 | 0.20 | -0.07 | 0.40 |
| Australia | 2.52 | -0.14 | -0.13 | -0.27 | -0.19 |
| New Zealand | 2.53 | -0.23 | -0.36 | -0.42 | -0.37 |

| 90 Day Interest Rates | % | Yield Changes | | | |
|---|---|---|---|---|---|
| USA | 2.11 | 0.08 | 0.18 | 0.46 | 1.08 |
| Japan | 0.09 | 0.00 | -0.01 | 0.02 | 0.03 |
| United Kingdom | 0.80 | 0.00 | 0.19 | 0.22 | 0.52 |
| Australia | 1.95 | -0.03 | -0.03 | 0.15 | 0.24 |
| New Zealand | 1.91 | 0.00 | -0.11 | -0.01 | -0.05 |

| Bond Indices | Closing Values | Changes over: 1 Mth % | 3 Mths % | 6 Mths % | 12 Mths % |
|---|---|---|---|---|---|
| S&P/NZX Bank Bills 90-Day | 712.73 | 0.16 | 0.50 | 0.99 | 1.96 |
| S&P/NZX NZ Government Bond Index | 1726 | 1.29 | 2.32 | 3.72 | 5.08 |
| Barclays Capital Global Aggregate Index (Hedged NZD) | N/A | 0.31 | 0.53 | 1.40 | 1.14 |

| Hedge Funds & Commodities | | % | % | % | % |
|---|---|---|---|---|---|
| HFRX Global Hedge Fund Index (USD) | 1269 | 0.5 | 0.1 | -0.5 | 1.5 |
| DJ-UBS Commodity Index Total Return | 173 | -1.8 | -7.2 | -4.1 | 0.5 |
| Gold (US$/ounce) | 1200.30 | -1.9 | -7.7 | -8.8 | -8.8 |
| Oil (US$/barrel) | 77.72 | 4.8 | 1.7 | 17.6 | 47.5 |

| Currencies | | % | % | % | % |
|---|---|---|---|---|---|
| NZD / USD | 0.6635 | -2.5 | -5.4 | -8.1 | -7.4 |
| NZD / EUR | 0.5703 | -2.0 | -5.1 | -3.7 | -5.3 |
| NZD / GBP | 0.5105 | -1.6 | -3.2 | -2.6 | -8.2 |
| NZD / AUD | 0.9175 | 0.2 | -1.1 | -1.0 | 1.6 |
| NZD / YEN | 73.57 | -3.5 | -3.5 | -4.5 | -6.7 |
| Trade Weighted Index | 72.32 | -0.9 | -0.9 | -3.7 | -6.2 |

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



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