Market Commentary

The heat wave that swept across the North Hemisphere seemed to flare the tempers of world leaders in August. Escalating bilateral trade disputes and political unrest in regions such as China/Hong Kong weighed on investor sentiment, and we saw the Volatility Index (VIX) shoot up towards 25, the highest level since the sharp correction at the end of last year.

Stock markets took a leg down in August, and the S&P 500 was particularly volatile, experiencing three trading days of significant drawdowns (-2.5% or more). The last time this occurred in a single month was September 2011, during the European sovereign debt crisis.

Bond markets echoed the growing concerns of a global slowdown, and US Treasury yields fell to a record low as demand for safe assets spiked. Commodities like gold, platinum and silver also surged as day traders rushed to increase portfolio diversifiers.

Over in Europe, the determination to deliver Brexit with or without a deal by the new Boris Johnson administration caused a panic in the continent's two largest economies, Germany and the UK. While stock markets have reacted swiftly to price-in the pessimism, economists are fearful that a no-deal Brexit will push the already contracting German economy further into a protracted recession.

Nevertheless, there were bright spots in the market and equities recovered from the worst of the mid-month losses. The two major positives for equities currently are lower interest rates and (still) robust corporate earnings, and while these factors are in play, the backdrop for equities remains broadly supportive.

Looking ahead, September will see important central bank meetings from the European Central Bank (Sept 12th) and Federal Reserve (Sept 18th). With monetary easing on the cards and plenty more ammunitions in the central banks' arsenal, there are good reasons to look through any short-term political turmoil.

Portfolio Commentary

The Cash Fund rose 0.23% before fees and taxes in August, above its benchmark the S&P/NZX Bank Bill 90-day total return index.

If July felt like a month where the finger in the dam of global rates was just holding the tide, the proverbial dam burst in August as yields on high grade government bonds collapsed amidst ever heightened trade tensions (and the potential for this to lead to a global recession) and a series of downward moves in interest rates by a number of central banks. As mentioned last month, the FOMC cut interest rates by 25 bps on July 31

Throughout August the yield on the US 10-year government bond declined from 2.01% on July 31st to 1.50% to close August. As well, the spread between the 2-year and 10-year US government bonds inverted (signalling the potential for recession) and remains inverted at the time of writing. In New Zealand, the Reserve Bank surprised the market by cutting the OCR by 50 bps and the market reacted accordingly. The 2-year NZ government bond yield fell 20 bps on the day and 19 bps for the week, while the 10-year government bond yield fell 20 bps on the day and 26 bps for the week, taking NZ interest rates to fresh all-time lows. At the end of the month the NZ 10-year government bond yield was 1.06% down 39 bps for the month.

Lifetime VIP Balanced Fund

The Kiwi Wealth Fixed Interest Fund (Fixed Income PIE) returned 1.23% in August underperforming its benchmark which returned 1.59%. This underperformance was primarily due to highly aggressive downward moves in long maturity government bond yields which dropped significantly over the course of the month. Throughout the year, the team has increased its holdings in longer dated bonds which has helped the FI PIE keep pace as best it can with the government bond index and has generated a 7.3% gross (pre taxes and fees) return calendar year to date.

The Kiwi Wealth Growth Fund (Growth PIE) rose 0.41% after tax and fees, 0.63% ahead of the benchmark which declined 0.22%. Global Thematic was the key driver of the outperformance, while Global Quantitative lagged the index. The alternatives assets made a strong positive contribution to returns, mainly due to a big month for the AHL Pure Momentum fund.

Lifetime International Companies Fund

Global Quantitative lagged the benchmark by about 100 basis points as cheaper and smaller stocks continued to lag those of larger growth companies. The lag was concentrated in the first half of the month when global bond yields sank as the US and China escalated their trade standoff. This kept the lid on companies preferring higher yields like Banks (Citizens Financial, Bank of New York Mellon). Our top performing sector was Consumer Staples (Unilever, Costco) which tends to do better when bond yields fall.