Lifetime Income Limited Monthly Portfolio Report as at 31 May 2021 Wholesale Investor

Market Commentary

Global equity markets stood resilient in May, recording a 1.1% return as measured by the NZD-Hedged MSCI ACWI index. The S&P 500 finished the month just below its all-time high as recorded earlier in the month. Closer to home, the NZX 50 saw disappointing returns, falling as much as 3.2%, weighed down by heavyweight names such as Fisher & Paykel Healthcare which saw disappointing earnings. Sector wise, Energy, Finance and Materials led the pack while Tech and Consumer Discretionary had a lackluster month.

The trend of a global economic recovery continued in May, with the pace of vaccinations continuing to gain traction across developed countries. Domestic consumption of goods and services picked up amidst the growing list of economies that have begun to reopen. It is becoming more evident that there is a sizable mismatch between supply and demand. On the one hand, the unprecedented amount of fiscal support has provided a significant tailwind for demand. While on the other hand, the supply side continues to be constrained by labour shortages, shipping, and material bottlenecks.

This supply and demand mismatch has meant that inflationary pressures are pretty much a given, the only questions that remain are for how long and how aggressive. As such, market watchers have spent much of May keeping close tabs on economic data backing the inflation debate. US employment data stole the spotlight earlier on in the month, surprising the market to the downside. In total, about a quarter of a million new jobs were reportedly added in April, significantly below the expectation of close to a million. While the most pandemic-affected sectors such as travel, and hospitality added the most jobs, manufacturing and retail on the other hand actually recorded declines. Labour supply shortages have so far been floated as the culprit.

The next key piece of economic data released during the month was the US inflation gauge as measured by the Consumer Price Index (CPI). In contrary to the earlier jobs data, it painted an economy with signs of potential overheating. Year on year inflation rose 4.2% vs the expected 3.6%, surprising the market to the upside. Core inflation (excluding food and energy) also rose 0.9% month on month, above the expectation of 0.3%. Some of the biggest drivers include used cars, travel, and accommodation. It's worth noting that the US Federal Reserve continues to maintain that any inflation spikes would be 'transitory', a buzzword that has been used too often recently.

Not helping the whole inflation story, one of the largest US pipeline operators covering the east-coast was subject to a massive cyberattack, forcing the shutdown of its operations for almost a week. Fuel shortages sent thousands on a panic-buying spree, driving Gasoline prices above $3/gallon for the first time since 2014. In fact, crude oil along with other commodity prices have climbed considerably, stoked by the pent-up demand of reopening economies. All being said, the economic outlook for the remainder of the year certainly looks promising, but it's important to avoid being blindsided by the prospect of an overheated economy, or a recovery story that doesn't fully pan out.

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Kiwi Investment Management Wholesale Funds

Portfolio Commentary

Lifetime Fixed Interest Trust

	Units	Unit Price*	Market Value	%
Cash Fund	189,149.77	1.0558	199,704.33	100.00
Total			**199,704.33**	**100.00**

**Applications are valued using the buy price, redemptions are valued using the sell price and market values are calculated using the mid-price.*

The Cash Fund returned 0.10% before fees and taxes in May outperforming its benchmark, the S&P/NZX Bank Bill 90-Day Index, which returned 0.04%.

New Zealand rates moved higher in May in a month with a lot of moving parts. First of all, the annual budget pulled off a few surprises. It lifted payments to beneficiaries (who tend to spend rather than be able to save thus stimulating the economy) by $3.3billion over three years. It also raised infrastructure spending by $4.4 billion (assuming we can find the people to build it out).

Despite a far better than hoped response to COVID-19, we are keeping more cash on hand on the country's balance sheet – just in case. That means more government bond issuance than expected including an upcoming 11-year maturity bond as well as a new 30-year bond later on this year. While described as being "in the shadow of COVID", the Treasury's economic outlook was quite rosy reflecting high global commodity prices for milk, logs and many other of our exports as well as strong employment. In fact, there are multiple sources suggesting that there is widespread lack of labour in many industries. Now, the Reserve Bank (RBNZ) has been moving in lockstep with global central banks for some time not really talking much about interest rates rises - albeit we are a few quarters ahead of the rest of the world in coming out of Covid and we have already begun our tapering. Nevertheless, the RBNZ surprised the market towards the end of the month. It gave an equally positive economic outlook and, crucially, added in a clear and aggressive track towards higher rates with up to 6 OCR hikes from mid-2022 through mid-2024 (from 0.25% to 1.78%).

Lifetime VIP Balanced Fund

	Units	Unit Price	Market Value	%
Fixed Interest Fund	2,196,764.73	1.3509	2,967,609.48	38.86
Growth Fund	2,536,918.62	1.8403	4,668,691.33	61.14
Total			7,636,300.81	**100.00**

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Kiwi Investment Management Wholesale Funds

Fixed Interest Fund

The Fixed Interest Fund returned -0.44% before fees and taxes in May, outperforming its benchmark which returned -0.66%.

Interest rates rose in New Zealand following an unexpectedly aggressive move towards Official Cash Rate (OCR) hikes and a lower average maturity protected the portfolio from this move. Offsetting this, short term interest rates (which we are overweight) rose fast on the back of the Reserve Bank's aggressive change in the OCR stance). Bond markets typically trade lower when interest rates rise.

We continue to remain leery of the idea that reopening will only have a "transitory" effect on inflation amidst higher oil and commodity prices, higher shipping costs and an enormous FOMO (fear of missing out) consumer pulse. We are therefore continuing to take a wait-and-see approach and remain positioned towards shorter average maturities. That view led us to sell 2037 maturity Australian Government (AAA) bonds. Conversely, we used interest rate swaps to take a view on the 5-year interest rates where we thought that the market had over-priced in the number of OCR hikes that might happen. Should NZ end up raising interest rates too fast, it would likely push up the Kiwi dollar too far for comfort, hurting our exports.

Credit spreads (the extra interest rate you receive to buy a risker company bond vs a government bond) remain at near 2007 pre-Global Financial Crisis level lows, so we have been equally leery on adding too much credit risk. We did, however, purchase new names such as SkyCity Entertainment (BBB-).

Growth Fund

The Growth Fund returned 0.35% before fees and taxes in May, underperforming the MSCI ACWI benchmark by -0.29% as US stocks trailed the rest of the world and our technology holdings were generally weaker.

Two of the three underlying equity strategies contributed positively to relative performance while the third resulted in a drag. The alternative assets on the other hand outperformed both equities and cash.

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Lifetime International Companies Fund

	Units	Unit Price*	Market Value	%
Global Quantitative Fund – Hedged	1,599,271.82	1.4577	2,331,258.52	71.59
Global Quantitative Fund – Unhedged	674,422.41	1.3556	914,247.02	28.41
Total			3,245,505.54	**100.00**

**Applications are valued using the buy price, redemptions are valued using the sell price and market values are calculated using the mid-price.*

The Global Quantitative Fund returned 1.64% before fees and taxes in May, 0.50% ahead of the MSCI ACWI benchmark, as economic data continues to be robust and policy continues to be supportive.

Inflation fears are bubbling with US CPI printing 4.2% YoY albeit real time data suggests this is peaking but is tightly linked to oil which rallied up 4% for the month. This pushed Value stocks into the driver's seat again, with Energy, Materials and Financials leading the market higher. Crypto volatility was high as Musk backtracked on accepting bitcoin as payment for Tesla cars, citing emissions concerns, and China indicated lower tolerance for tokens. Our top sectors were Industrials (Deutsche Post, Expeditors International) as global freight transport continued to be in strong demand and Consumer Discretionary led by autos (Ford, Yamaha) particularly as the market took a liking to Ford's EV plans. Our worst sector was Materials (Corteva). HP Inc was our worst position overall, falling on fears of peaking PC demand.

Our top-down positioning targets higher quality companies and sectors seen as more suited to the current environment. Stock selection favors companies with attractive metrics across earnings quality, capital efficiency, valuations, sentiment, and sustainability. Over the month, we increased allocation to Financials (SEB, CaixaBank) and Industrials (Waste Management, Hitachi), and reduced allocation to Technology (Intel, Fortinet) and Discretionary (Tractor Supply, Alibaba). Technology and Industrials are our favoured sectors while Energy and Utilities are our largest underweights.

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