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

Market Commentary

Equity markets enjoyed a ‘Santa Claus rally’ in December, wrapping up 2021 on a positive note. Although markets got off to a volatile start at the beginning of the month, given worries around the new highly transmissible Omicron. Those concerns later dissipated as optimism grew due to the less severe nature of the variant. The focus remains on central banks as they begin to accelerate the pace of tightening and withdrawal of stimulus to combat record levels of inflation.

This amounted to a lot of moving pieces in December for fixed income, traditionally a quiet month for the asset class. November US consumer price inflation continued unabated at 6.8%, a multi-decade high. Even excluding volatile food and energy prices, the “core” rate was still a chunky 4.9%. Indeed, the US Federal Reserve solidified its view that the word “transitory” should be put to bed when considering recent inflation, increasing its taper such that its $120 billion per month bond-buying program will now end in March. This sets the scene for up to three interest rate hikes through the end of 2022. Usually, that would result in higher interest rates in order to compensate bond investors for the purchasing power of their principal being eroded in the future. However, the sudden unwelcome arrival of the Omicron variant stymied this sentiment (albeit a weak unemployment report didn’t help either). Rather, interest rates declined, with the rate on the US 10-year government bond dropping to a low of 1.34% from 1.44% at the start of the month. Inflation expectations and, therefore, interest rate expectations did come down with the oil price, which sold off on the expectations of lower demand. However, most of the rate decline appeared to be a knee-jerk reaction to yet another twist and turn in the Covid story. Interest rates began to climb again towards the end of the month as it became clearer that this most contagious variant was less virulent. The US 10-year treasury rate ended about unchanged at 1.51%.

Longer-term interest rates in NZ took the US lead and declined as well. However, longer interest rates did not bounce as much in New Zealand with the better Omicron news. The mid-month publication of the treasury’s HYEFU (Half Year Economic and Fiscal Update) illustrated a resilient economic outlook and an improved trajectory for the public finances despite various Covid disruptions (lower government borrowing, the eventual return to OBEGAL surpluses in 2023/24 was flagged, and lower Crown borrowing). A major factor behind a big reduction to further debt issuance were forecasts for the NZ debt management (NZDM) to start running down its big cash buffer, which it has built up at the Reserve Bank. This major reduction in issuance overshadowed a stronger-than-expected Q3 GDP report which showed a better-than-expected decline of -3.7% in a lockdown hit quarter. This interest rate on a 10-year New Zealand government bond declined ten basis points bps to 2.38% over the month.

Roger Browne
M: +64 021 211 0552; E: roger.browne@kiwiinvest.co.nz

Kiwi Investment Management Wholesale Funds

Portfolio Commentary

Lifetime Fixed Interest Trust

	Units	Unit Price*	Market Value	%
Cash Fund	139,236.27	1.0604	147,646.14	100.00
Total			147,646.14	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 December, beating its benchmark, the S&P/NZX Bank Bill 90-Day Index, which returned 0.06%. The Reserve Bank is on hold over the summer but has made it crystal clear that it expects a series of 25 basis point hikes into 2023 with a terminal rate just above 2.5% in 2023.

Lifetime VIP Balanced Fund

	Units	Unit Price	Market Value	%
Fixed Interest Fund	2,568,612.98	1.3108	3,366,937.89	43.78
Growth Fund	2,128,234.94	2.0315	4,323,509.27	56.22
Total			7,690,447.16	100.00

Fixed Interest Fund

The Fixed Interest Fund returned 0.53% before fees and taxes in December, underperforming its benchmark, the S&P/NZX NZ Government Index, which returned 0.54%. Underperformance was due to having a lower average maturity than that of our benchmark as global investors sought the safe havens in longer government bonds, and lower expected government bond issuance pushed rates up. All things being equal, bond prices go down when interest rates go up and usually more so if the bond's maturity is higher. While interest rates did bounce towards the end of the month as the market absorbed the enormously higher contagiousness but lower virulence of the virus, the effect of lower future NZ bond issuance predominated.

December was a quiet month for the portfolio. We did add some **Goodman Property** (BBB+) bonds in a new issue but were essentially in a holding pattern. We continue to believe that longer rates do not compensate investors against the risk of higher inflation. Both the Reserve Bank and the Treasury expect rates to decline from recent highs but for their level to remain higher than the lows of the 2010s. As a result, we think there is some value at the shorter end of the curve, which have already efficiently priced in future OCR (Official Cash Rate) hikes.

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Growth Fund

The Kiwi Wealth Growth Fund returned 3.24% on a gross of tax and fees basis for the month ended December, outperforming its benchmark, which returned 2.75%. The underlying Global Quantitative and Core Global strategies both added positive alpha for the month. Portfolio wise, we're overweight US momentum and underweight Asia & Japan. There were no significant changes to the fund during December, and the effective equity exposure sits at ~96.4%

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Lifetime International Companies Fund

	Units	Unit Price*	Market Value	%
Global Quantitative Fund – Hedged	1,495,333.30	1.5271	2,283,523.49	68.99
Global Quantitative Fund – Unhedged	685,388.08	1.4973	1,026,231.57	31.01
Total			3,309,755.06	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 strategy returned 4.03% in December, a solid 1.05% ahead of the Solactive Kiwi Global benchmark. Ending the year strongly, December was an excellent month for equity returns. A relative strengthening of the NZD resulted in returns 0.68% higher for the hedged class. Investors initial fears of Omicron being more virulent than existing COVID variants in November were shown not to be correct, although its transmissibility is much higher. Oil reversed much of its losses the month prior, ending up 14%.

Winners included the United States and the United Kingdom, Value (underpriced companies relative to their fundamentals), and the Health Care sector. Laggards included China and Russia, Momentum (i.e. stocks with the highest returns over the past year) and the Consumer Discretionary sector.

The majority of the positive performance came from stock picking within the IT Sector, where overweight Broadcom rallied 19% after announcing a bullish quarterly forecast on strong chip demand. Within Consumer Discretionary, retailer Autozone rose by 15% after beating quarterly earnings and sales expectations. The worst detractor to relative returns was overweight software developer Adobe, which fell 15% after lowering FY22 revenue estimates. Overweight Bath & Body Works also detracted from performance as the stock ended 8% lower after revising its future earnings estimate lower.

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