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Milford KiwiSaver Plan Monthly Review
September 2019

Market and Economic Review

August was another hectic month in financial markets. Investors were presented with a deluge of information, from trade war tweets to local company earnings updates. Milford funds navigated the volatility well, generally outperforming their underlying markets and ending the month in positive territory.

Risks from the escalating trade war, coupled with a softening global growth outlook has seen bond investments continue to deliver strong returns as investors retreat to these perceived safe havens. Central banks have been quick to try and get ahead of the global economic slowdown by lowering interest rates. This includes the Reserve Bank of New Zealand which delivered a surprise 0.5% rate cut during the month to encourage spending by businesses and consumers.

With declining returns available from holding cash, investors continue to hunt down better return opportunities elsewhere. This includes bonds with longer maturities - demand for higher yielding 10-year US bonds has caused an 'inversion' in the US yield curve (where longer dated bonds offer lower interest rates than shorter dated bonds) – something that previously has been a signal of impending US recession. Company bonds also benefit from the search for yield - they have outperformed shares over the past month and year.

August saw Australian and NZ companies report their results. As usual there were some surprises, both positive and negative, but overall the outlook from Australian companies has improved in the last six months, whilst in NZ the outlook felt a bit more subdued.

Looking ahead, we remain cautious as global growth continues to slow, particularly with trade war tensions escalating. Low interest rates help, but we may have already seen the benefits of lower interest rates via strength in global consumer spending recently. Nonetheless, a slowing but still positive global growth picture, coupled with low interest rates, remains a reasonable environment in which to invest. We continue to look for attractive companies that can deliver strong returns, either from dividend income or earnings growth, or in some cases a bit of both.

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Milford KiwiSaver Plan Monthly Review as at 31 August 2019

KiwiSaver Conservative Fund

Portfolio Manager: Paul Morris

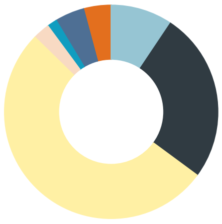
The Fund returned 1.0% in August, contributing to a strong 1-year return of 7.6%. Global and Australasian market interest rates (represented by bond yields) fell further in August on increased concern that geopolitical risks (most notably the US-China tariff war) will weigh on global growth and inflation.

This supported a strong return from the Fund's corporate bond holdings (bond prices rise when yields fall), albeit they underperformed government bonds. It also underpinned much of the Fund's Australasian share exposure which is oriented towards income shares and generally benefits from lower interest rates. Global share performance was more mixed but offset by the Fund's foreign currency exposure which benefited from a lower NZ dollar.

Given an ongoing uncertain economic backdrop and multiple known risks we believe it is prudent to retain slightly cautious positioning. We acknowledge likely supportive monetary policy but think this approach is consistent with the Fund's conservative risk profile. We believe through active management the Fund can still deliver reasonable returns, albeit with lower risk.

Near term, we also reiterate that after yet another month of strong gains (especially in bonds) returns should moderate.

Actual investment mix [1]



- Cash and Cash Equivalents 9.38%
- New Zealand Fixed Interest 25.72%
- International Fixed Interest 52.21%
- New Zealand Equities 2.57%
- Australian Equities 1.49%
- International Equities 4.58%
- Listed Property 4.05%
- Other* 0%

KiwiSaver Balanced Fund

Portfolio Manager: Mark Riggall

The Fund returned 1.0% in August, bringing the 1-year return to 8.1%. Fund returns continue to be boosted by the performance of bonds. Global economic growth is slowing and risks to the outlook are increasing via the escalating trade war and impending Brexit deadlines.

To combat this, central banks the world over have moved to cut interest rates. This is a significant shift in tone over the past nine months and investors have ratcheted up expectations of further rate cuts ahead. The impact has been twofold, firstly, bond prices move up when interest rates fall. Secondly, falling interest rates mean investors have rushed to buy higher yielding bonds, or assets such as company bonds and high dividend yielding shares to generate returns.

Within the Fund, this has been very beneficial for the income portfolio which remains heavily invested in company bonds. It has also benefited the share portfolio which is tilted towards higher dividend paying shares such as Contact Energy or Real Estate Investment Trusts. Although interest rates are unlikely to fall significantly further, the valuations of higher dividend shares remain attractive and so the Fund remains invested.

The outlook is uncertain, so we will continue to invest cautiously as the backdrop of low growth, but supportive interest rates provides a reasonable investment backdrop.

- Cash and Cash Equivalents 12.04%
- New Zealand Fixed Interest 6.71%
- International Fixed Interest 24.49%
- New Zealand Equities† 13.15%
- Australian Equities 8.55%
- International Equities 26.10%
- Listed Property 8.96%
- Other* 0%

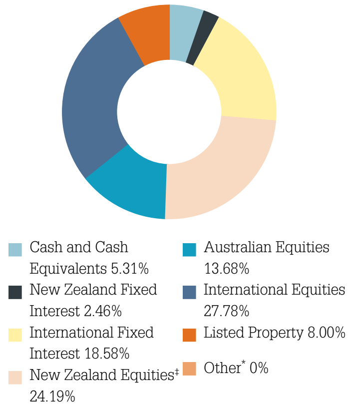
†Includes unlisted equity holdings of 0.25% *Other includes currency derivatives used to manage foreign exchange risk.

[1] The actual investment mix incorporates the notional exposure value of equity derivatives and credit default swaps, where applicable.

KiwiSaver Active Growth Fund

Portfolio Manager: Jonathan Windust

Actual investment mix [1]



The Fund rose 0.9% in August which was a good result given falls in Australian (-2.4%), New Zealand (-0.9%) and global (-1.9%) share market indices. Shares fell in response to escalating trade tensions and softening global growth. Falls were cushioned by strong returns from bond markets, the fall in the NZ dollar, good company selection and cautious positioning.

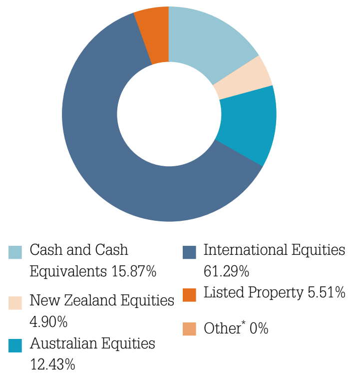
The performance of the Fund's investment in the Dynamic Fund was particularly strong rising 3.0%, compared to a 3.1% fall for the Australian Small Industrials Index. Key company performers during the month included Contact Energy (+11.3%) and Spark (+11.1%), which benefited from good results announcements and the low interest rate environment.

During the month, the Fund took advantage of market falls to increase exposure to Australian and global share markets. Looking forward we believe shares will be supported by low rates, reasonable dividends and positive economic growth (whilst we expect growth to slow, we do not forecast a recession). Key headwinds for shares are relatively high valuations, slowing company earnings growth and political uncertainty.

In this environment the strategy of the Fund is to remain active to take advantage of market volatility and opportunities. We remain focused on identifying those companies that offer strong risk adjusted returns.

KiwiSaver Aggressive Fund

Portfolio Manager: Stephen Johnston



The Fund is off to a positive start, gaining 1.5% in August, in what was a volatile month for global share markets. The weakness in the NZ dollar was a positive contributor to the Fund's performance in August.

In terms of the Fund's neutral asset allocation, international shares comprise 70%, 20% is allocated to Australian shares (mix of large and small cap), 5% in New Zealand shares and the balance in cash.

Our allocation to the Milford Global Select Fund contributed positively in August, with strong performance from derivative exchange CME (+11.8%) and pet favourite Zoetis (+10.0%). Other key outperformers were US mobile tower companies Crown Castle (+8.9%) and American Tower (+8.8%), beneficiaries of the boom in data use.

Stock selection was also strong in our Australian Funds, with notable outperformers including advertising company Wellcom (+29.3%), mortgage broker Australian Finance Group (+16.0%), building materials company James Hardie (+13.4%), and professional services company Smartgroup (+22.0%).

For now, the global backdrop remains somewhat challenging, with the ongoing trade war unresolved and the upcoming Brexit deadline both adding to the uncertainty. In this environment, volatility is likely to stay elevated. Reflecting this risk, the Fund has retained a higher allocation to cash that will be deployed as risks recede and we have more clarity on the outlook.

‡Includes unlisted equity holdings of 1.84% *Other includes currency derivatives used to manage foreign exchange risk.

[1]The actual investment mix incorporates the notional exposure value of equity derivatives and credit default swaps, where applicable.

Fund Performance

	Past month	1 year	3 years (p.a.)	5 years (p.a.)	Since Fund inception (p.a.)	Unit price $	Fund size $
KiwiSaver Conservative Fund	0.96%	7.65%	6.41%	7.54%	9.39%	1.8324	120.3 M
KiwiSaver Balanced Fund	0.96%	8.09%	9.33%	10.01%	10.38%	2.4422	347.8 M
KiwiSaver Active Growth Fund	0.88%	7.68%	10.74%	11.60%	12.83%	3.9388	1,456.1 M
KiwiSaver Aggressive Fund	1.48%	—	—	—	—	1.0147	18.8 M

For details of how investment performance is calculated, and returns at each PIR please see www.milfordasset.com/funds-performance/view-performance#tab-performance.
Performance figures are after total Fund charges* have been deducted and at 0% PIR.
Please note past performance is not a guarantee of future returns.
*Total Fund charges do not include the $36 p.a. Administration and Registry fee.
Inception dates for the Funds: KiwiSaver Active Growth Fund: 1 October 2007^, KiwiSaver Balanced Fund: 1 April 2010, KiwiSaver Conservative Fund: 1 October 2012, KiwiSaver Aggressive Fund: 1 August 2019.

^This is based on the performance of the 'AonSaver AMT Milford Aggressive Fund' until 31 March 2010 and the 'Milford KiwiSaver Active Growth Fund' from 1 April 2010.

Key Market Indices

	Past month	1 year	3 years (p.a.)	5 years (p.a.)	7 years (p.a.)
S&P/NZX 50 Gross Index (with imputation credits)	-0.85%	16.66%	14.62%	16.98%	18.07%
S&P/ASX 200 Accumulation Index (AUD)	-2.36%	9.04%	11.38%	7.90%	11.02%
S&P/ASX 200 Accumulation Index (NZD)	-0.17%	6.82%	12.51%	6.92%	8.11%
MSCI World Index (local currency)*	-1.95%	1.28%	10.08%	7.64%	11.21%
MSCI World Index (NZD)*	2.51%	5.48%	14.87%	12.33%	13.62%
S&P/NZX 90-Day Bank Bill Rate	0.15%	1.94%	2.01%	2.48%	2.58%
Bloomberg Barclays Global Aggregate Bond (USD-Hedged)	2.27%	10.74%	3.81%	4.16%	3.92%
S&P/NZX NZ Government Bond Index	2.22%	9.53%	4.82%	6.06%	4.77%

*With net dividends reinvested

Milford KiwiSaver plan is the proud winner of multiple awards:

2018|2019 consumer. PEOPLE'S CHOICE Milford KiwiSaver Plan

Consumer NZ People's Choice Award – KiwiSaver

MORNINGSTAR Awards 2019

Morningstar Fund Manager of the Year - KiwiSaver Category, NZ

FundSource Awards 2018

FundSource 2018 KiwiSaver Manager of the Year

Top Security Holdings (as a percentage of the Fund's Net Asset Value)

KiwiSaver Conservative Fund	KiwiSaver Balanced Fund
Westpac 2.22% 2024 1.54%	Contact Energy 2.10%
NZ Govt. Inflation Indexed 2% 2025 1.46%	Spark New Zealand 1.90%
Bank Of China 3% 2020 1.44%	a2 Milk Company 1.64%
QBE 6.75% 2044 1.41%	Meridian Energy 1.19%
Vector 3.45% 2025 1.34%	Financial Select SPDR 0.92%
ING Group 1.45% 2024 1.33%	Wellington Strategic Euro 0.88%
ANZ Bank 3.03% 2024 1.30%	Vontobel Sust. EM Leaders 0.87%
JPMorgan 5% 2024 1.23%	Wellington Global Health Care 0.86%
Westpac Float 2029 1.20%	Transurban Group 0.83%
ANZ Bank Float 2024 1.19%	QBE 6.75% 2044 0.83%

Note: Fixed interest securities are reported in the following format: Issuer name, interest (coupon) rate, maturity year, size of fund holding (as % of total portfolio).

KiwiSaver Active Growth Fund	KiwiSaver Aggressive Fund
Contact Energy 4.32%	Alphabet 2.35%
Spark New Zealand 3.45%	Microsoft Corp 2.34%
iShares MSCI EAFE Min Vol ETF 3.13%	CME Group 2.28%
a2 Milk Company 3.09%	Amazon 2.17%
Alphabet 1.56%	Crown Castle 2.12%
Visa 1.45%	Visa 2.11%
CYBG 8% 2049 1.39%	Mastercard 2.08%
Transurban Group 1.36%	Starbucks 1.78%
HCA Holdings 1.27%	S&P Global 1.77%
Westpac 5% 2027 1.21%	Financial Select SPDR 1.75%

Note: Fixed interest securities are reported in the following format: Issuer name, interest (coupon) rate, maturity year, size of fund holding (as % of total portfolio).

Milford staff have approximately $10.5 million invested in the Milford KiwiSaver Plan as at the end of August 2019.

Frances Sweetman
Senior Analyst

Investment Highlight - Spark NZ

One of our top performers on the NZX over reporting season has been Spark. It is one of our largest New Zealand holdings, although the stable nature of its earnings means it doesn't feature in our monthly updates very frequently.

Globally, telecommunications companies (telcos) have been less popular investments in recent years than other companies with stable cashflows and attractive dividends.

Telecommunications markets are often highly competitive with low barriers to entry, and the investment required to upgrade mobile networks to 5G could be substantial. The ability of telcos to monetise 5G investment via higher prices or new revenue streams is uncertain. This means investors have less confidence in the long-term earnings and dividend outlook.

Spark is a highlight among global telcos. The company faced significant disruption a number of years ago with the arrival of a new mobile competitor, 2Degrees, in 2009 and the separation from its fixed line infrastructure with the creation of Chorus in 2011.

The company's navigation of these challenges has been impressive. Under former CEO Simon Moutter, the company re-branded from Telecom to Spark, launched a new mobile brand 'Skinny' to compete with 2Degrees, grown a corporate digital business, and has undertaken an internal transformation from a traditional bureaucratic structure to a lower cost, agile, retail business. This has allowed it to maintain stable earnings and, utilising its strong balance sheet, pay out an attractive dividend of 25c per share for the last four years.

The investment case for Spark this year has hinged on its ability to maintain its 25c dividend into the future without using debt to top it up, as it approaches its self-imposed gearing limit. Other factors for investors to consider have been the change in ownership of Vodafone New Zealand, its largest competitor, which was bought by the NZX listed company Infratil and Brookfield earlier this year. CEO Simon Moutter has also been replaced by Jolie Hudson, an executive that has been with Spark since 2013. This has seen the share price underperform its NZX peers. However, confirmation at its recent earnings update it can continue to support a 25c dividend saw its share price increase 10% in the week following.

Spark is a good example of how a high calibre management team can drive performance. We continue to hold the stock as we expect this to continue, despite ongoing challenges in its operating environment. Importantly, debt levels remain conservative, reducing risk and providing the ability to diversify into new technology and grow earnings in the future.

Meet your Investment Team - Stephen Johnston

Stephen Johnston
Portfolio Manager

Stephen Johnston is Portfolio Manager of the newly launched Milford KiwiSaver Aggressive Fund, he joined Milford in 2013 and has over 20 years' experience in the investment industry across global financial markets and asset classes. Stephen is also Co-Manager of the Milford Global Equity Fund.

As Portfolio Manager for the Milford KiwiSaver Aggressive Fund, what does your average day look like?

I am an early bird, getting up at 5am. The first thing I do is check to see how the northern hemisphere share markets have performed and any market related news that may impact the companies in our portfolios. I have found exercising first thing clears my mind and most mornings I exercise while listening to Bloomberg or CNBC and sometimes company earnings calls.

Before I rush to catch my bus, I make it a priority to have breakfast with my wife and kids if they are up. Once at the office, I catch up with the global team and other investment team members. We have a very collaborative working environment and there is a constant exchange of information across the team. My day tends to involve company calls, speaking with investment bank analysts, modelling company financials and discussing with our team where the best opportunities are.

What's your favourite thing about your job?

While investment management is my job, it is also my passion. Quite conceivably, I could see myself like Warren Buffett, 88 and still investing! I really enjoy the variety of work; no two days are the same. I love the mental challenge of the job, there is nothing better than discovering new and exciting businesses. I find it very satisfying when our hard work pays off and we achieve good outcomes for our clients.

With so many companies globally, how do you decide which companies to invest in?

We focus on the long term and identify investment themes and trends that will stand the test of time and pick companies which will benefit from these trends. We look for exceptional businesses that have key attributes we believe leads to long term outperformance. Given this quality focus, 99% of listed companies globally will not be of interest to us.

What are some of the key themes the Aggressive Fund will invest into?

We want to expose our investors to some of the most exciting long-term themes globally. Examples include, the "rise of the middle class" in emerging markets which we believe is a multi-decade theme, the move to a "cashless society" as we all transition from paying with cash to credit cards and mobile payments. The "hunt for yield" is becoming more important as bank deposit rates and bond yields fall. Let me finish on a favourite of mine, pet humanisation. Globally we are increasingly treating our pets like members of the family, driving a spending boom.

Which KiwiSaver Fund/s are you in and why?

What matters most when looking at long term returns, is time in the market, you need patience. At Milford we have a range of KiwiSaver funds you can choose depending on your risk profile and time till retirement. I have more than 15 years to retirement, so I have 100% of my KiwiSaver in the Aggressive Fund but it really depends on your individual circumstances. I would love investors to come on the journey with me.