NEWTON ROSS
PRIVATE WEALTH MANAGEMENT

13 October 2020

September 2020 Quarterly Report

It has been another positive quarter for investment portfolios. Markets did give up some of their returns in September as a surge in global Covid-19 cases, concerns about forthcoming US elections and delays to additional US government spending weighed on investor sentiment.

International shares and listed property securities provided the bulk of returns for the quarter with lower contributions from NZ shares and fixed interest investments. Client portfolios are now up for the 2020 calendar year having recovered the ground that was lost during the March market falls.

Since the first lockdowns, global economic growth has recovered sharply and better than generally expected with the OECD now forecasting the world economy to shrink -4.5% this year and down from their -6% forecast in June. The recovery to date has just been a restart of activity following months of pandemic enforced hibernation. The real work now begins for governments to implement effective policies to keep the momentum for growth particularly, as there are new signs that growth is plateauing. In NZ, we are back to a nationwide Level 1 status which will help our embattled hospitality and entertainment industries as we move into the summer season while there is an increasing possibility of a more effective travel bubble being extended with Australia.

The final quarter of the year is likely to be mixed for markets as we face the uncertainty of US elections, final Brexit negotiations and as rising Covid infections lead to further lockdowns for some countries. We expect further large fiscal stimulus packages to be announced this quarter (US, Australia, UK and Europe) and further global central bank easing. We may also see the first very limited deployments of vaccines. A broader and fuller global economic recovery is not expected until late 2021 and the shape of that activity will be different to the pre-Covid 19 era.

Kind regards,

Ross

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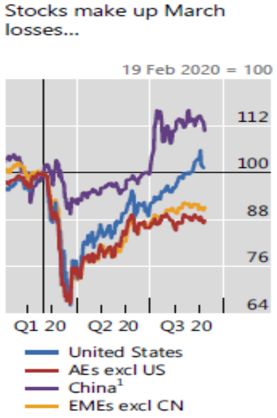
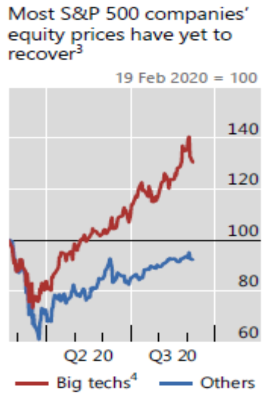
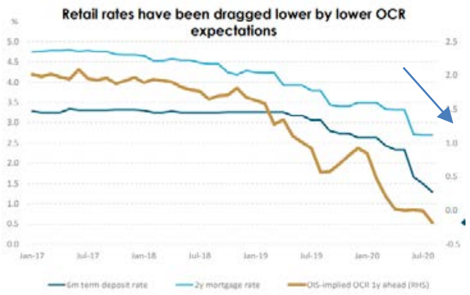
ECONOMIC AND MARKET SUMMARY

Client portfolios have recovered to be slightly positive for the year to date and over the 1-year period. After the worst drop in global economic output since The Great Depression, economies bounced strongly in the third quarter on pent up demand. However, this growth is showing signs of plateauing - particularly as Covid-19 cases surge and potentially push some countries back into more restrictive conditions. Investment markets are more recently cautious on the sharp lift in asset valuations since March. The rise has largely been driven by record central bank stimulus and government spending and is now showing signs of running out of puff. The recovery in investment markets has however not been equal. While Chinese and US share markets rose strongly over the last 2 quarters and are up year to date (+ 9.7% and +4.1%) other share markets are still well down including Australia -13%, UK-22.2%, Europe -13% and Japan -5.6% as are most emerging markets. The NZ share market has performed well being up +1.7% year to date. The recovery within markets has also been uneven with technology, healthcare and consumer staples sectors outperforming and energy, banking, insurance and utilities underperforming. The later sectors are more closely linked to the actual performance of the economy (nominal economic growth). This divergence in performance is slowing as valuations for outperforming sectors become stretched beyond expectations of reasonable earnings growth. Investors will focus back on those cheaper sectors as broader economic activity improves over the next 1 to 2 years. There are also encouraging signs investors are coming back into the worst affected industries (including travel) on rising confidence for near term vaccine solutions.
The charts below from the Bank of International Settlements show most share markets are still below their pre-Covid levels and the significant divergence of returns from the US share market where technology stocks have dominated the market return. The top 5 US technology stocks now account for more than 25% of the US share market by value.





Closer to home, our small NZ share market is dominated by two companies, Fisher and Paykel Healthcare and A2 Milk which account for around 30% of the total market value. Both these companies have performed strongly since March returning our overall market index back to pre-Covid levels. The Australian share market continues to underperform the NZ market given the prominent role underperforming energy, mining, banking, and insurance sectors have on their market. Their valuations also remain more attractive.
Fixed interest (bond) markets also performed well in the quarter as central banks continued to aggressively purchase bonds across the globe in a policy to drive down interest rates and funding costs for borrowers while inflation remains stubbornly absent. These purchasing programs (funded by debt themselves) have also substantially reduced the interest rate difference between riskier junk bonds and much safer investment grade bonds and down to record low levels. This means investors holding higher risk bonds have generally done better and been rewarded for taking on the additional credit risk (chance of the failure of the underlying borrower to pay interest or repay capital). Borrowers, especially higher risk companies have been taking advantage of these conditions to raise historically cheap money. This trend will continue and we witness the rise of finance companies and higher risk issuers in the market which are being funded by investors desperate to get better yields as term deposit rates plummet. The Auckland Council (investment grade issuer) released a 30-year bond in the quarter that pays a 2.95% interest rate. The Reserve Bank keeps signaling a move of the official cash rate into negative territory with many commentators now expecting a cash rate of -0.25% to -0.5% in March 2021. This chart from Harbour Asset Management shows how term deposit (blue line) rates are being dragged down by these lower official cash rate expectations.



There is much debate that negative rates will actually reduce spending while simply boosting asset prices even further. In the absence of inflation and sub-optimal economic growth, central banks and governments will keep the stimulus going and growth assets in particular will continue to do well in such an environment.

The table below shows the gross returns (before tax) from the benchmark index for each asset class.

Market Returns	Sep. Qtr.	1yr p.a.	3yr p.a.	5yr p.a.
$NZ v TWI	**0.3%**	1.9%	-2.1%	0.6%
$NZ v $US	**2.4%**	5.6%	-2.8%	0.7%
$NZ v $AUD	**-1.2%**	-0.4%	0.2%	0.3%
NZ Cash	**0.1%**	0.6%	1.3%	1.6%
NZ Fixed Interest	**2.6%**	5.4%	6.6%	5.3%
Intl Fixed Interest 100% hedged to $NZ	**0.7%**	4.2%	5.5%	5.0%
Australasian Equities 50/50 Indexes	**1.7%**	-1.3%	9.4%	11.6%
NZ Listed Property	**13.3%**	-4.3%	13.9%	11.9%
Intl Equities 50% hedged to $NZ	**6.2%**	6.0%	8.3%	9.7%
Commodities $NZ	**6.2%**	-12.9%	-1.3%	-3.7%

SECURITIES RETURNS FOR THE QUARTER

During the quarter we purchased Spark New Zealand for the Australasian portfolio and made minor adjustments to the target weights across the 20 companies we hold in the sector for direct portfolios. Spark NZ was recommended by Devon for inclusion as an opportunity to participate in the accelerated (post Covid-19) shift in modern life to online socialising, working, and learning. Spark is split into four business lines; Spark Home, Mobile and Business provides fixed line, mobile and internet services; Spark Digital provides information and communications technology; Spark Connect & Platform provides network and shares business operation and Spark Ventures and Wholesale looks to target new business opportunities. In broad terms the company's broadband business is lower margin and more competitive than the mobile business which remains essentially a strong duopoly in NZ with Infratil owning Vodafone - the other major player. At the time of purchase the stock offered a 5% dividend yield which is attractive given the low level of interest rates and given the connected world we live in is considered relatively defensive during periods of slower economic growth.

In order to fund the Spark NZ purchase we have sold Vista Group (VGL). The cinema software company has been dramatically impacted by Covid-19 with the enforced closure of cinemas worldwide. When the extent of the disruption became apparent management acted quickly, raising additional capital (we participated in this for client's buying more shares at $1.05) and making changes across the business to reduce costs. This was reflected in solid operating cashflows for the first half of 2020 and a strong balance sheet. Despite revenue being down 33% the company share price jumped (reaching a high of $1.94) on the better than expected result and we took the opportunity to sell at a price more than double the low reached in March. While VGL is expected to continue to improve over time as restrictions are lifted, the timing around this remains uncertain and subject to changing consumer preferences. Consequently, it was felt that Spark offered a better long-term opportunity moving forward.

The following tables show the returns from the securities recommended by NZ DIMS. Depending on your investment strategy you may hold all or only a portion of these securities and the returns for the securities held may also differ slightly depending upon cash flows and transactions in your portfolio over the quarter.

AUSTRALASIAN EQUITIES

Company	Sector	Quarterly Performance In NZ$ terms
New Zealand Equities		
Auckland Airport	Ports	10.9%
Contact Energy	Energy	11.1%
F&P Healthcare	Healthcare	-5.9%
Fletcher Building	Building	4.1%
Freightways	Transportation	7.8%

- The sharp drop in interest rates has positively impacted the yield-based valuation for listed property companies with both Stride Property and Goodman Property rising over 20% during the quarter. Stride recently purchased a Shortland Street office building as they focus more on this sector having spun out their industrial assets into a separate fund. While risks remain in the office and retail space due to the soft economic environment, the company is looking to add value to the purchase through improving services and more active management. The purchase is expected to help Stride retain or even increase their current 5.1% dividend.
- IAG was sold down after reporting a A$435m profit, 70% lower than 2019 but in line with guidance. Key drivers for the lower result were reduced investment income (on a A$10b portfolio); a A$138m class action settlement related to

Meridian Energy	Energy	6.0%
Port of Tauranga	Ports	-3.4%
Spark NZ	Telecommunications	1.5%
Stride Property	Property	20.5%
Australian Equities		
BHP Group	Resources & Energy	2.8%
Brambles	Professional Services	-1.0%
CSL	Healthcare	1.8%
IAG	Financials	-23.2%
Macquarie Group	Financials	1.8%
Goodman Group	Property	22.1%
Ramsay Healthcare	Healthcare	0.6%
Sonic Healthcare	Healthcare	12.0%
Westpac	Financials	-5.0%
Woodside Petroleum	Energy	-16.3%
Woolworths	Consumer Staples	0.8%

- CSL has confirmed it is talking with partner organisations to roll out University of Queensland's Covid-19 vaccine if it proves to be successful. This follows a giant deal signed with the federal government to produce Australia's leading vaccine option. CSL's agreement would involve producing 51 million doses of the UQ's vaccine V451, with the first participants in the final stage trials to be enrolled in December providing progress remains on track.

insurance add-ons; provisions for claims related to Covid-19, bushfires and floods as well as higher reinsurance costs. The company has acted ahead of its competitors and significantly lowered the assumed margins on parts of its product portfolio to position it for the challenging economic environment ahead. The company is the Australasian market leader in general insurance and owns many well-known retail brands such as NZI, AMI and Lumley.

- Electricity companies Contact Energy and Meridian Energy benefited from the upcoming election as both major political parties got involved in the horse trading around the Rio Tinto exit from the Tiwai aluminium smelter. The potential loss of 2600 jobs in Southland was enough incentive for both Labour and National to try and influence a 3-5-year extension to the recently announced 2021 exit.
- Housing and construction activity in both NZ and Australia have held up better than expected and point to a smoother path in the short to medium term for Fletcher Building than previously indicated by management in August. Residential consents are holding up well, a key competitor in the cement industry went into receivership, company restructuring cost-outs are beginning to flow through and Fletcher Living cannot build residential houses quick enough for sale in the Auckland market.
- F&P Healthcare upgraded profit guidance following a strong start to the financial year. Global hospitalisations requiring respiratory support are now expected to remain elevated for longer due to Covid-19. Hospital hardware sales were up 390%, hospital consumables revenue is up 48% and production output has been rebuilt despite both IV and Optiflow sales at similar levels to the peak in April. This reflects more hardware in hospitals, a change in clinical practice to favour high nasal flow therapy for Covid-19 patients and some stock rebuilding. Outside hospitals there has also been strong revenue growth of in-home respirators.

AUSTRALASIAN EQUITIES

The Australian market fell sharply (-4.5%) in September but ended the quarter up 0.8% in NZ dollar terms. This month the Reserve bank of Australia kept cash rates unchanged at 0.25% and reiterated that they see little benefit in further cuts unless they are convinced this will lead to better job creation. They believe the heavy lifting needs to be done through fiscal policy from here (in contrast to the RBNZ view) and to that end the Australian Federal Government delivered a budget which has been favourably received. They have looked to reinvigorate economic growth through a wide ranging mix of immediate personal tax cuts, targeted income support, payments to businesses to hire more staff, improved company depreciation rates for new asset purchases and increased national infrastructure spending.

The NZ market peaked in mid-August at a 6% gain for the quarter before being negatively impacted by election uncertainty (US and NZ), profit taking on tech companies and mixed news on Covid-19 vaccine trials. The market still posted a solid 2.6% gain over the quarter and continues its remarkable run since the March selloff - although the easiest part of the recovery phase may well have passed. There remains significant return dispersion between individual stocks and this quarter was no different with F&P Healthcare -6%, a2Milk -24%, Mainfreight +18%, Chorus +18% and Goodman Property +16%. This was partly due to profit taking and late quarter rotation into higher yielding stocks, and partly due to continued uncertainty for near term growth with economists widely dispersed views for 2020 NZ GDP growth ranging between -2.1% and -7.9%.

One sector to gain strongly this quarter was property. Globally, property prices have fared better under Covid than expected as wage subsidy programs and ultra-low rates assisted mortgage servicing. As subsidies start to cease and more long-term unemployment becomes known, rent pressures may become apparent in some markets - particularly if boarder restrictions take longer to lift. The NZ housing market surprised everyone with strong price rises following the first lock-down and may end 2020 up more than +6%. Barfoot and Thompson had a 41% increase in sales over the last 12 months to August. Chronic house shortages (circa 50,000) continue to constrain supply, while cheaper financing and lower deposits rates have seen home buyers and property investors return to the market with gusto. National building consent issuance has been very high (+37,000 last 12mths) and at levels not seen in the last 30 years. Additionally, there has been a focus on medium density dwellings for Auckland and Hamilton which may alleviate supply constraints. Net migration has been running at 0% since April although anecdotal evidence suggests offshore kiwis are wading into the higher end of the market. The non-residential market is not so rosy with consents down from this time last year (-8.8%). Commercial office and retail remain under pressure - particularly in Auckland where new supply is coming on stream.

Fund	Quarterly Performance In NZ$ terms	Commentary
Devon Trans-Tasman Fund	1.0%	The fund slightly underperformed the market benchmark over the quarter but benefited from sector rotation from tech to value and yield stocks during September. Positive contributions were made by Sky City, oOh!Media, Fletcher Building, Aristocrat Leisure and Contract Energy. Freightways also delivered a positive return with its courier business improving both its pricing and volume, particularly in the Business to Consumer division with industry wide price increases providing a platform for increased margins. The portfolio also benefited from the sharp rebound in Vista after the company reported

		better than expected cash positions and the first major blockbuster films since the pandemic started were released. During the quarter, the manager took profits in a2 Milk and Rio Tinto after periods of strong share price growth.
Harbour Australasian Equity Focus Fund	10.8%	The fund strongly outperformed the market benchmark over the quarter. Key contributors were growth positions in Pacific Edge (+129% after a capital injection and US progress on their bladder cancer test), Serko (+37%), Summerset (+40% as aged care village sales jumped 50% post lockdown) and Afterpay (+31%). The largest detractor for the quarter was a2 Milk which fell -24% after downgrading revenue forecasts to $1.8-1.9bn. This reflects the impact of the lockdown in Victoria, Australia where the Daigou channel has been severely interrupted. More positively, a2Milk has increased sales by 77% over last year via 20,000 retail outlets across China. The manager took some profits in a2Milk earlier in the period and subsequently added to their holdings post the share price dip. Ebos and CSL have been added to the portfolio bringing the healthcare sector allocation to 37% of the total portfolio. Small positions were also added in bio-tech companies 4D Medical and Aroa Biosurgery. In the technology sector an initial investment in Afterpay was made and the existing holding in Pushpay was increased, while profits were taken in Vista Group and Xero.

INTERNATIONAL EQUITIES

Global share markets have surged since March when valuations reached deep recessionary levels. With economies restarting, massive fiscal spending and effectively unlimited central bank support, markets have rallied hard with the US market up over 50% and NZ market up 40%. A significant portion of the recovery in markets has been concentrated in sectors less affected by GDP performance including technology and healthcare industries. Investor exuberance for some tech companies has been self-fulfilling with a wave of new direct retail platform investing frothing prices. More recently, the prices for these sectors have pulled back but still remain excessively high. Their high valuations have driven market PEs up also which look far less extended when these companies are excluded. Apple, Microsoft, Amazon, Google and Facebook make up 25% of the S&P500 index and their earnings per share in the 2nd quarter grew by 19% (versus -40% for the rest of the market). In New Zealand, Fisher & Paykel Healthcare and a2Milk account for 30% of our index. As broader economic conditions improve and vaccine candidates come to market, we expect to see a greater rotation towards cyclical sectors, some previously ignored value stocks and Covid-19 hit industries. The outlook for earnings should get better as conditions improve but it will be record money supply levels, low interest rates and investors desperate for yield that continue to drive equity markets higher.

Fund	Quarterly Performance In NZ$ terms	Commentary
Active Fund Managers		
Platinum International Fund	2.0%	The fund was up 0.7% in A$ terms for the quarter. The portfolio is invested in companies which in the manager's opinion offer exceptional value but which don't include the narrow range of companies which have dominated market returns this year. index returns this year have come from just three stocks (Amazon, Apple and Microsoft) while the average global stock has actually fallen in value. Positive contributors to performance came from investments in companies like LG Chem (Korean electric vehicle maker), logistics companies ZTO Express and Fed Ex, vaccine maker Moderna and platforms Facebook and Tencent. With the continued rise of tech market darlings, short positions (which make money if the share price drops and lose money if it rises) has cost the fund performance. The manager uses short positions and currency management to guard against steep losses in the event of a market downturn. This therefore provides risk mitigation for the overall international equity portfolio. No one is ever sure when the mood of the market may alter but in early September we saw the first signs of what might happen with the tech heavy Nasdaq falling sharply over a few days and Value style investing outperforming Growth style investing for the first time in 2020.
Monks Investment Trust	8.5%	The fund was up 9.0% in GBP terms for the quarter. The portfolio was positioned for a normal, generic economic slowdown prior to the pandemic and consequently had a significant allocation to economically insensitive growth companies which have performed well. This has allowed the manager to resist having to make sudden changes to the portfolio and they are now able to look for new opportunities. They perceive that new technology will open up geographic areas (South East Asia) and parts of the economy that have previously avoided major tech driven change such as healthcare, insurance, justice and education. There are also clear opportunities with growth cyclicals (e.g. travel companies), where the dominant players with strong balance sheets will be able to hoover up market share and position themselves for future demand.
Magellan High Conviction Fund	6.8%	The fund was up 5.7% in A$ terms despite starting the quarter holding 23% cash in response to the cautious economic outlook and given the risks equities are facing. Core investment themes in the portfolio include Chinese-consumer-related stocks including tech platform companies Alibaba and Tencent, Estee Lauder and Starbucks. Together they make up 35% of the portfolio. The Chinese middle class is forecast to double in size over the next 5-10 years and these companies are structural winners in the ecommerce, gaming, media, cloud computing and digital payments sectors and have strong brands. A further 20% of the portfolio is invested in enterprise software companies (Microsoft and SAP) which are integrated into their customer operations and at the forefront of the transformational growth in cloud computing. Global advertising spend has moved away

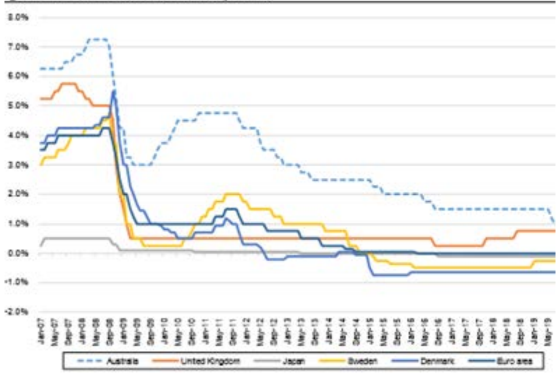
		from traditional outlets and onto digital platforms such as those owned by Google and Facebook (16% of the portfolio) which rely on payment platforms such as Visa (6%) to connect the millions of merchants with billions of customers.
Passive/Index Funds		
Vanguard Intl Shares Select Exclusions Index Fund Hedged to NZD	6.7%	This fund provides passive exposure to all major developed share markets and is hedged back to the NZ dollar which means values are not impacted by currency movements. Global share prices were underpinned by central banks' commitment to near zero interest rates for the next year or so, as well as economic data in several economies suggesting that a recovery is underway in many sectors as countries learn to live with and better manage the pandemic. During the quarter Asia was up 10%, the US +9% while the UK was down -3% (Brexit concerns) and Europe up 2% despite a resurgence in Covid-19 cases and being forced to reinstate lockdown protocols. Japan was one of the strongest markets as investors began to adjust to the new priorities of the Suga administration. Despite a wobble in September when utilities and industrials found some support, growth stocks remained in favour and value stocks continued to struggle. Within the sectors, Energy remains the weakest area having fallen more than -47% during 2020 on weak economic growth and the sector now represents less than 2.5% of the index.
iShares Russell 2000 Index Fund	2.5%	These funds provide passive exposure to smaller companies in the USA and around the world and are valued in USD. Over the quarter the 2.4% rise in the NZ dollar against the US$ reduced returns. Small capitalisation stocks have lagged behind their larger counterparts this year, but during September's selloff they held up better as investors sought value.
Vanguard FTSE All-World ex US Small Cap Index Fund	6.7%	
Vanguard Emerging Market Index Fund	7.6%	The fund provides passive exposure to companies listed in emerging markets and is also valued in USD which reduced returns. Emerging markets fared better as investors looked for value and the US dollar again strengthened.

COMMODITIES

Our terms of trade hit a new high in the 2nd quarter due to very strong export performance (despite Covid conditions), while our demand for imported oil dropped sharply. Dairy, fruit, and timber prices all lifted, and NZ powdered milk is now selling at a significant global premium to other producers. Given the rising trade tensions between China and most of the rest of the world (including NZ), there are increasing concerns regarding the concentration of our exports to China. The chart opposite shows the sharp rise in reliance since our free trade agreement in 2008, with China now representing more than 80% of our log exports, 73% of milk powder, 34% of dairy, 40% of meat and 36% of seafood. To date we have managed to walk the diplomatic tightrope with China, but we remain especially vulnerable. Elsewhere, energy prices continue to be impacted by lower global demand and excessive production. Iron ore, copper and aluminium prices have all lifted strongly as government funded infrastructure projects jump globally. The sharp rise in aluminium prices may also give Rio Tinto pause regarding the closure of the Tiwai Point facility.

FIXED INTEREST

igure 1: Global Central Bank Policy Rates



The nexus between central banks and governments continues to tighten as more governments deliver ever extraordinary fiscal stimulus packages funded by record issuances of debt. Benign inflation allows rates to keep low and provide headroom for cheap financing. The circle is now closed between fiscal and monetary policy responses. Central banks are not only delivering an ultra-low or even negative interest rate environment which presently ensures the affordability of all this record borrowing, but their on-market purchases monetizes (prints money) each new issue of treasury debt. These global on-market and in some cases “unlimited” central bank buying program have driven yield curves down even further over the quarter while also compressing credit spreads to record low levels. Cheap and effectively “free” money (in real terms) is creating massive money supply globally that is looking for somewhere to go.

NZ interest rates dipped below 0% for the first time in history and bonds maturing out to 5 years traded at small negative rates. The 10-year NZ Govt bond yield slipped to a record low of 0.45% after touching 1% earlier in the quarter. The system is awash with liquidity as the RBNZ continues to buy back bonds from the market and the banks use proceeds to buy more bonds exacerbating the demand for yield. In another first, the Auckland City Council issued our first 30-year bond in the NZ market. The bond was issued as a Green Bond to support infrastructure initiatives at a yield of 2.97% and was very well received by institutional investors.

The Reserve Bank of NZ continues to perceive significant risks to growth and unemployment as the wage subsidy rolls off and is therefore looking to drive retail interest rates even lower to encourage spending and investment. The RBNZ expanded its quantitative easing (QE) program to $100bn in August, has asked banks to prepare for a negative Overnight Cash Rate (OCR) and is proposing a Funding for Lending Program which would see the RBNZ directly lending to banks at a rate close to the OCR. Markets are pricing in a negative OCR of -0.2% in a year’s time, while there remains considerable debate about whether negative interest rates are an effective tool. Detractors argue that all that happens is that savers are punished (and hence reduce consumption), while investment is further directed into non-productive assets such as residential housing.

<table>
<tr><th>Security</th><th>Quarterly Performance In NZ$ terms</th><th>Commentary</th></tr>
<tr><td>AMP Capital NZ Fixed Interest Fund</td><td>2.3%</td><td rowspan="2">Globally, core inflation pressures remain very low and yields are expected to trend sideways (at best), as they remain artificially supressed by central bank activity and safe haven buying. Asset quality is deteriorating in the corporate space, yet the risks are being masked by the flood of liquidity. By comparison, NZ bonds are better positioned than their global peers and may offer short term gains due to RBNZ support. However, they are expensive by historical standards and offer a poor yield at current levels. At present the manager prefers cash over fixed interest as the risk of capital loss is lower and over the medium-term returns appear similar.</td></tr>
<tr><td>AMP Capital NZ Short Duration Fund</td><td>0.8%</td></tr>
<tr><td>Harbour Wholesale NZ Core Fixed Interest Fund</td><td>2.8%</td><td rowspan="2">In light of RBNZ comments, the manager has positioned the portfolios for lower interest rates in the 0-3-year maturity bucket. While this part of the curve has moved to negative yields for the first time in history, the manager believes there remains scope for additional falls. In addition, they have purchased high quality corporate bonds to increase credit exposure. The additional yield offered over Government bonds has attracted plenty of investor interest although with a range of new issues available the manager has focused on companies who a less exposed to Covid-19 related risks.</td></tr>
<tr><td>Harbour Enhanced Cash Fund</td><td>0.4%</td></tr>
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Summary

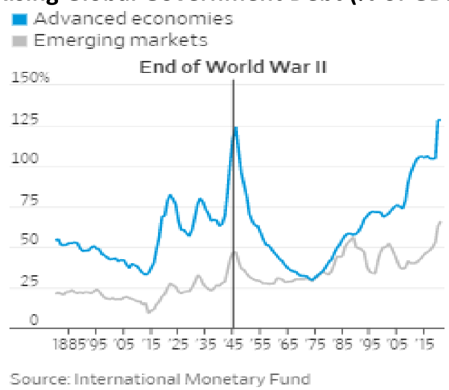
Climbing back out of the hole. The pandemic induced the deepest global recession since the 1930's. The OECD estimated that the damage to major economies is more than 4 times worse than that inflicted by the 2009 global financial crisis. The sharp rise in growth over the second half of the June quarter and the September quarter has been better than expected and has built as a result of pent up demand. Investment markets have taken confidence from the bounce and been reassured by government spending (at levels previously only seen during wartime) and historical levels of central bank support. In reality, the real recovery is only just starting. The next 12 months will be a critical time, requiring bold and effective policy implementation. It will also be a time for industries to recognise the sharp structural shifts whose trends have been accelerated by the pandemic. This provides massive opportunity but also terminal risk for those that do not position themselves quickly enough. It will be an exciting time and a juncture point for many of the themes that have been emerging over the last decade – de-globalisation, geo-power shifts, online commerce, energy conversion, artificial intelligence, bio-tech and transport. Economies are also going to have to quickly grapple with productivity growth and the role of labour as it plays a diminishing part in economic success. In addition to providing fiscal support, governments will need to define the role they are going to play in providing that support. Transformative infrastructure projects for example are rarely privately implemented and most post-war regeneration has required a heavy government hand. Achieving the balance between state and private activity will be politically tricky for traditional democratic societies as will be the balancing of the role government over both short and then longer timeframes. Certainly, countries with centralised state structures (China) seem better positioned to drive change over the short term (witness their economic recovery from the pandemic), while historically, state driven economies tend to not thrive over longer term. The next 12 months will also see how the nexus between central banks (monetising government debt) and fiscal stimulus plays out. Traditionally separated functions, governments are now increasingly relying (gambling) on central banks to set ultra-low interest rates costs in the future to manage their budgeting. This includes central banks being prepared to let inflation 'run a little hot' so as not to spoil the spending party and any chance of a sustained recovery. With this backdrop, growth asset markets should be well supported and extend the market cycle.

Our overall view is that the global economy will show signs of plateauing over the coming quarter as additional Covid-19 measures are re-implemented, but that it should then gain steam early in 2021 on the back of new fiscal stimulus, central bank quantitative easing and the start of public vaccine programmes.

Global Manufacturing Activity

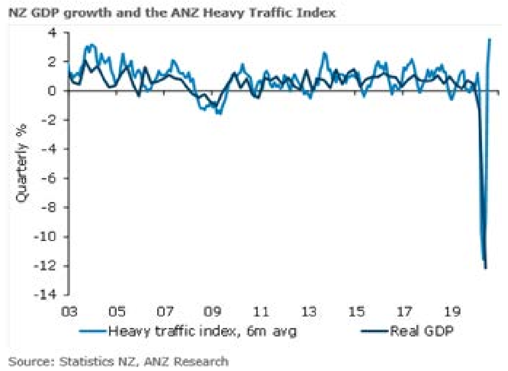
Global Data Surprise Index …beating expectations

Rising Global Government Debt (% of GDP)

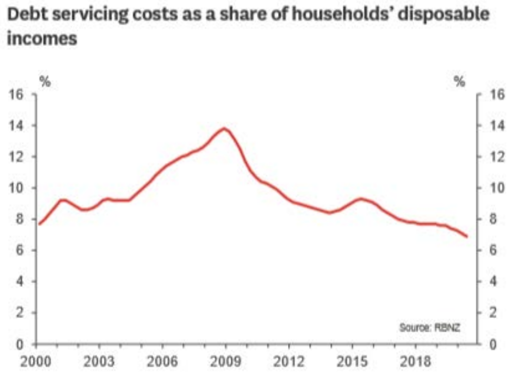


New Zealand Although we endured further lockdowns in the quarter, NZ is faring the recession well with a substantial recovery in activity. The end of the wage subsidy for some 120,000 jobs or 4.5% of the labour force will be fully felt in coming period. The ANZ Business Outlook flash results for October show confidence is rising despite the recessionary conditions and back at pre-Covid levels, although business borrowing remains weak. The rate of job filling is also encouraging and back to pre-covid levels however with wage support ending unemployment could still rise to 10%. The worst affected are lower income workers in retail, hospitality, tourism, and travel industries. The border closure has stopped seasonal workers from entering, providing some opportunity for lower skilled local workers to fill the void. Employers are saying that finding skilled workers remains their primary problem with net migration running near 0% since April. The number of New Zealanders re-entering the country for the long term has plunged by more than two thirds (Westpac). The government (presuming re-election) has intentions to borrow and spend for recovery ("Rebuilding Together" campaign) but will find skilled labour shortages an insurmountable barrier unless our borders can be more effectively re-opened. The slow down in net migration is expected to take some pressure off our grossly undersupplied housing market (50,000 house deficit), although cheap mortgages and relatively lower household debt servicing costs (see chart opposite) are currently supporting a surprising housing market boom. In addition, building permits are rising which is an encouraging sign for activity into 2021. While Kiwis have done their bit to support domestic tourism, with their onshore holiday spending providing much needed help, this may not be enough as we enter the normally peak summer season for offshore tourists. In addition to the massive government spending plans, the RBNZ may introduce additional stimulus through a Funding for Lending Programme (FLP) next month. This programme would provide even lower cost funding for banks to enable them to further reduce their lending rates. We also expect a negative official cash rate to be introduced in March 2021. These actions will lower borrowing costs but also reduce the consumption and spending from those who rely on interest income to live. After GDP dropped sharply (-12.2% annualised in the 2nd quarter), growth in the 3rd and 4th quarters should see total 2020 GDP come in around -5%.

NZ GDP Growth & ANZ Heavy Traffic Index



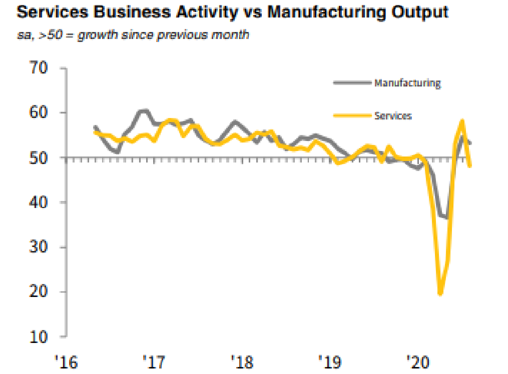
NZ Household Debt Servicing Costs



Australia

The reimposed lockdowns in greater Melbourne and state border closures clipped the momentum of Australia's recovery in the 3rd quarter. Rather than having a strong rise in activity the 3rd quarter will be flat or marginally positive. By keeping their economy more open under Covid, Australia's economy fared better than NZ bottoming at -7% in the 2nd quarter. GDP for 2020 should be around -4% and their unemployment rate 8%. The federal government announced an aggressive budget recovery package aimed at supporting employees and businesses, transport infrastructure projects and regional support. The cost of the package is eyewatering and dividing opinion. Canberra is forecasting a deficit next year of $214bn which is 10% of GDP and gross public debt levels are expected to reach at least $1trn or 43% of GDP by 2023 (twice current levels) and some commentators suggesting it could rise to more than twice this amount over the next 15 years. In

Victorian Lockdown Impacting Recovery



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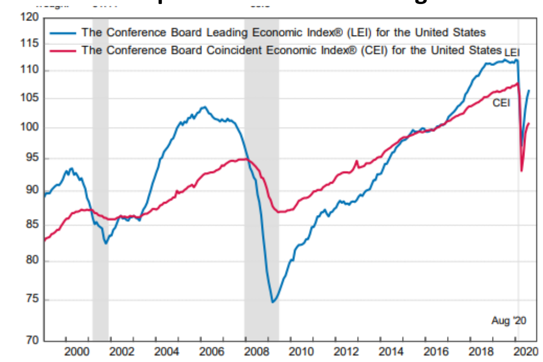
addition to spending, tax cuts for those earning less than $120,000 are being introduced. The Reserve Bank of Australia is also likely to cut rates to a record low of 0.1% in December but has ruled out a negative cash rate. As a buyer of Australian Government debt, the Reserve Bank, like ours in NZ, is monetising their spending programmes as well. Future generations in Australia and NZ may look back in wonder at the financial burden being placed on them today.

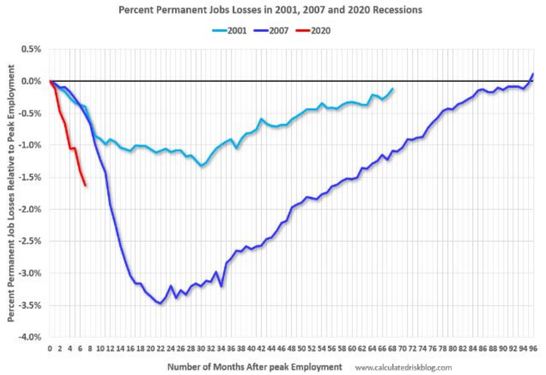
US

By keeping their economy as open as possible, the recovery in America has also been better than expected though it has also recently lost some steam. Softer retail sales driven by the expiry of the federal $600 per week unemployment top up and the resurgence in virus infections are having an impact. The chart opposite shows the Leading Indicator index of activity (blue line) just starting to head sideways after a very strong bounce. At the time of writing, Congress had still not agreed a new stimulus package required to keep vulnerable household consumption and businesses functioning. Some deal is expected before the election which now looks like Biden's to lose – particularly if Trump is re-hospitalized for his infection. Positive news across the US economy includes record high house prices, falling unemployment (back to 7.9% as employment rates lift to pre covid levels), the sharpest gain in consumer confidence in 17 years, an 8 year high in capital goods orders and their ISM services index lifting well into expansionary territory. Services are the largest part of the US economy though manufacturing activity has dipped after reaching a 2-year high. From here, and assuming a Democratic win and control of both houses, corporate tax breaks will be unwound - although we can also expect a substantial increase in government stimulus (net public debt to rise to more than 110% of GDP by 2023). This spending may not be enough to recover parts of the American economy, including tourism and retail, leaving behind lower skilled workers. This will result in deeper permanent job losses which are now tracking down more steeply than during the GFC and 2001 recessions (red line in chart opposite). Despite media attention being focussed on a divided America (racial, wealth and political) their economy (presuming there is no election driven constitutional crises) is well positioned to recover strongly in 2021 as vaccine solutions are delivered.

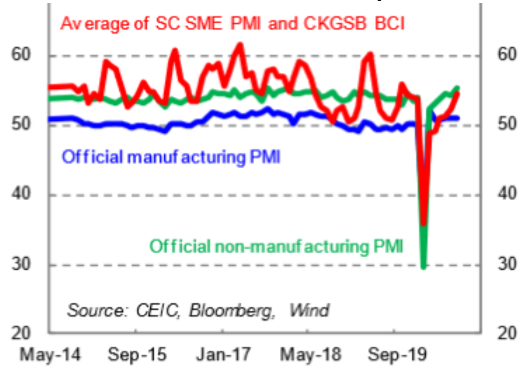
US Improvement now Slowing



US Permanent Job Losses (2020 in red)



China Business Surveys



China

China remains the comeback king of Covid-19. Their centralised state control has enabled them to best respond to their health (containing the virus and having 5 of the phase-3 vaccine candidates) and economic crises. China's economic data continues to surprise and by the end of 2021 consensus numbers suggest their economy will be up to 11% above pre-Covid levels. Both consumption and production response (services and manufacturing) have recovered and with less cost (fiscals stimulus) than any other major economy. China has also managed to increase its share of global exports in this tough environment also lifting their current account surpluses. This is a remarkable achievement. Should China continue to growth real GDP above 4.5%

p.a. over the next 10 years it will put China into the bracket of high-income countries. History suggests that state focussed economies are not well positioned to achieve the structural changes required for productivity growth but, China may prove to be the exception given its core focus on technology development. Geo-politically, China faces greater challenges as its accelerating expansionism rattles established world orders and leads to a faster rate of de-globalisation including a potential de-coupling from the US. China is also increasingly comfortable to use its trade and capital muscle to retaliate against those asking difficult questions.

Europe & UK

The new surge in Covid-19 infections has taken the gloss off the decent European and UK recovery. This has had a direct hit on a now subdued services sectors (especially retail) detracting from their sharp recovery in the 2nd and early 3rd quarters. Spain, France and Ireland have slipped back into contraction with only Italy and Germany still in expansion. With manufacturing now at a 2.5yr high, Germany has managed to maintain its momentum (pink line opposite) and despite the new infection surge. The UK economy has been one of the hardest hit from Covid dropping -20% annualized in April. It also has managed a strong recovery in the 2nd and 3rd quarters but overall, GDP will contract around -11% in 2020. The sharp rise in infection rates, more social restrictions and the end to their Job Retention Scheme will result in sharply higher unemployment and be a drag on their economy this quarter. Having bumbled its way through Covid management, the UK is now desperately holding out for a vaccine roll-out in early 2021. Brexit negotiations are also not going well with the UK confirming they will quit talks if no deal is achieved by October 15th. Though some “skinny deal” is still expected by year end, the more complex financial services rules are unlikely to be resolved any time soon which has seen many large (European and US) London based firms now re-locating to Europe.

Japan

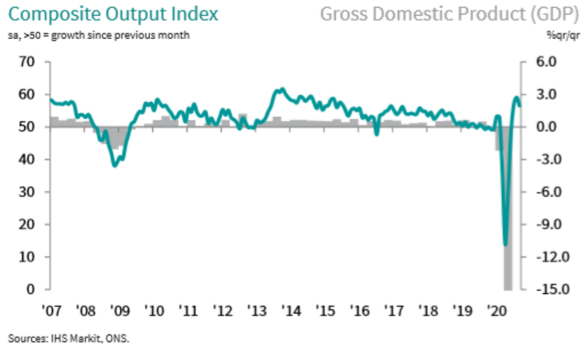
A disciplined society, Japan has managed the virus well, but their economy has struggled to achieve a meaningful recovery to date. Recent business sentiment has improved for manufacturing exports on rising global demand prospects while domestic demand remains subdued as social distancing rules and reduced working hours weigh on consumption. Their new prime minister Yoshihide Suga is expected to continue down the same path as the retired Shinzo Abe and rely on the Bank of Japan to stimulate growth from here. Any significant structural change to their economy remains frustratingly unlikely.

Emerging Economies

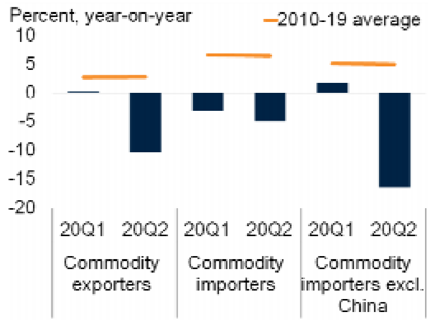
Sharply rising Covid cases, restricted tourism and falling energy prices continue to impact hard on emerging economies. Capital inflows have also been weakening, reducing available funding and weighing down exchange rates. This makes it additionally difficult for those countries with large US dollar debt obligations.

Euro Recovery Led by Germany

UK also Softening as Covid Re-flares



Commodity Reliant Emerging Economies hit Hardest



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