



MONTHLY REPORT

FOR PERIODS ENDED 31 OCTOBER 2016

MONTH IN A SNAPSHOT

- As the world continued to struggle with the decision by UK to exit the European Union (known as Brexit), October became all about the widely anticipated Presidential Election in the US. While we know the outcome of the election now, in October many investors were second-guessing the decision which ultimately was made by the American people.
- Only the cash fund returned positive results for members in all three of the New Zealand Defence Force Savings Schemes and across all tax rates. Poor share market returns during the month, meant negative returns for the other investment options.
- As the New Zealand Defence Force KiwiSaver Scheme celebrated its first birthday in October, we are now able to start reporting one year returns where these options had member in the month of October 2015. Where the returns are available all options had positive returns. We should see one year returns being available for more options in the KiwiSaver and also the New Zealand Defence Force FlexiSaver Scheme next month.

Read more about the markets and investment performance in this monthly report.



LOOKING THROUGH THE EMOTION

The recent US election which saw Donald Trump elected US president certainly came as a shock to the pollsters, media and large portions of the world population. Trump polarised people during the election so emotions ran high between those who loved or hated him.

Financial markets like consistency and when there is lots of uncertainty, the markets tend to 'sell off' and decline. This does not mean that money deserts the market – it simply means that money moves from shares to cash or bonds. Investors seek out lower risk parking places for their money until certainty returns to the markets or else until share prices fall to such a level that they are so attractive that one needs to buy.

This is exactly what happened in October with the NZDF funds. The value of the funds fell along with that of most comparable funds in the market. This made the October monthly performance look sick and it dragged down the overall 12 month performance.

Now that Trump has won the election, investors have had time to settle down and look more rationally at what has occurred and the implications for the world and investment portfolios. The more people remove the emotion, the more they see that investment markets will recover and move forward. People are realising that:

- Trump intends to spend up large on infrastructure projects and probably defence and this could stimulate the markets;
- Some of Trumps more extreme campaign comments will be moderated once he is in office and he will likely lead a responsible government; and
- Trump will drive change, but change creates opportunity and New Zealand has a history of quickly adapting and taking advantage of opportunities created via uncertainty.

Mercer manages the NZDF savings schemes. Mercer takes a relatively conservative approach with your money and this is evidenced with the well diversified portfolios they create for you. The markets took a massive hit just before the end of October (some markets were down 10% or more) yet most NZDF saving scheme funds suffered a loss of less than 1%. The higher risk funds such as the growth and shares funds suffered losses less than 2% which is pretty remarkable.

Prior to the US election, Mercer had a larger percentage of investor money in cash due to the uncertainty. As opportunities present themselves, the active managers in the NZDF schemes will be progressively looking for high quality assets to purchase.

The long term is a series of short terms and volatility (market ups and downs) is the key to often buying assets at good prices. We are confident that the medium term is not bleak – the shock of the US election will be temporary.

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A Disclosure Statement is available on request and free of charge.

MERCER COMMENTARY ENDED 31 OCTOBER 2016

Share and bond markets both finished lower in October as investors were moving away from riskier investments ahead of the upcoming US election and potential monetary policy changes. You couldn't turn on the news without hearing about the US presidential candidates – Hillary Clinton and Donald Trump. The re-opening of the FBI's e-mail investigation against Hillary Clinton at month end sharply narrowed her lead over Republican candidate, Donald Trump. Which markets took as a sign that perhaps Hillary wasn't the candidate-to-beat and that Trump had more trump-cards up his sleeve.

In a year that has given us Brexit and Iceland's Pirate Party, nothing is certain and markets don't like uncertainty and therefore continue to respond accordingly.

Oil prices surged to a 12-month high of more than \$53/bbl mid-month before dropping sharply following the news that OPEC and non-member producers couldn't reach a decision on terms surrounding proposed production cuts. The price at month-end was \$46.80/bbl. We saw this flow through to our petrol pumps with fuel prices rising and then falling again.

The New Zealand dollar fell against the US dollar and Australian dollar, but rose against the British pound.

Locally, New Zealand Shares underperformed other developed markets such as the US and UK, falling -5.7%, we believe the fall in New Zealand Shares is due to high dividend paying shares being sold off due to increasing global interest rates (which make the high dividends look relatively less attractive compared to bond yields). All multi-sector funds are underweight New Zealand Shares, which helped performance.

New Zealand Government Bonds fell -1.3%. Even global Listed Property and Infrastructure assets which are considered as more stable investments, didn't have a good month, returning -4.4% and -0.9% respectively.

All of these factors impacted on the performance of the NZDF Savings Schemes. However, November has improved to be a better month so far.



SIGNIFICANT RECENT ITEMS INCLUDE:



▼ UNITED STATES

US third quarter GDP grew by +2.9% on an annual basis, the fastest quarterly growth rate in the past two years, making an interest rate rise there even more likely as the economy appears to be on solid footing.

▼ UNITED KINGDOM

A timeline for the UK triggering article 50 (the intention to leave the European Union) was announced over the month. Prime Minister, Theresa May, indicated the government was prepared to pursue a "hard Brexit" (e.g. achieve full withdrawal within two years) and will start the formal proceedings before the end of March 2017. However, the saga took another turn as the High Court ruled that parliament must vote on the exit. The government is appealing the ruling.

▼ EUROPE

The European Central Bank (ECB) kept monetary policy unchanged. ECB President, Mario Draghi, suggested that the Bank would decide in December whether or not to extend its €80 billion quantitative easing program beyond the current deadline of March 2017. Monetary policy support from the ECB has helped keep interest rates low in Europe and has increased the perceived safety of Eurozone economies.

▼ NEW ZEALAND

Statistics NZ owned up to an error that has seen inflation over the last year double (from previously reported numbers) to 0.4%.

INVESTMENT RETURNS FOR PERIODS ENDED 31 OCTOBER 2016

DEFENCE FORCE SUPERANNUATION SCHEME

Investment options		1 Month	3 Months	FYTD*	1 Year	3 Years p.a.	5 Years p.a.
28% PRESCRIBED INVESTOR RATE (PIR)	Cash	0.12%	0.35%	0.87%	1.63%	–	–
	Conservative	–0.56%	–0.47%	1.74%	3.03%	–	–
	Moderate	–0.66%	–0.55%	2.15%	3.39%	–	–
	Balanced	–0.86%	–0.79%	2.39%	3.58%	5.55%	7.74%
	Growth	–0.95%	–0.95%	2.74%	3.23%	–	–
	High Growth	–1.26%	–1.30%	2.83%	3.28%	–	–
	Shares	–1.59%	–1.73%	2.15%	2.69%	–	–

Investment options		1 Month	3 Months	FYTD*	1 Year	3 Years p.a.	5 Years p.a.
17.5% PRESCRIBED INVESTOR RATE (PIR)	Cash	0.13%	0.40%	1.00%	1.88%	–	–
	Conservative	–0.60%	–0.47%	2.01%	3.24%	–	–
	Moderate	–0.69%	–0.49%	2.47%	–	–	–
	Balanced	–0.88%	–0.73%	2.80%	4.19%	6.01%	8.29%
	Growth	–0.97%	–0.87%	3.08%	3.68%	–	–
	High Growth	–1.28%	–1.18%	3.35%	4.00%	–	–
	Shares	–1.56%	–1.62%	2.91%	3.60%	–	–

Investment options		1 Month	3 Months	FYTD*	1 Year	3 Years p.a.	5 Years p.a.
10.5% PRESCRIBED INVESTOR RATE (PIR)	Cash	0.15%	–	–	–	–	–
	Conservative	–0.63%	–	–	–	–	–
	Moderate	–0.71%	–	–	–	–	–
	Balanced	–0.89%	–0.70%	3.06%	4.57%	6.30%	8.63%
	Growth	–0.95%	–	–	–	–	–
	High Growth	–1.19%	–1.02%	3.72%	–	–	–
	Shares	–1.54%	–1.53%	3.03%	–	–	–

Notes

- The investment returns shown on this page are based on the unit price movements of each investment portfolio and are after tax at the rate indicated and after fund charges that are charged within the unit prices.
- Each investor's returns within an investment portfolio will depend on timing of contribution payments and actual fees charged allowing for any fee rebates. The after tax and fees returns shown are therefore indicative of investment results but may differ from the actual after fees and tax returns achieved by individual investors.
- '–' indicates that investment option was not operating for the full period or did not have funds invested for the full period.
- * FYTD means Financial Year to Date, which is from 1 April 2016

INVESTMENT RETURNS FOR PERIODS ENDED 31 OCTOBER 2016

NEW ZEALAND DEFENCE FORCE KIWISAVER SCHEME

Investment options		1 Month	3 Months	FYTD*	1 Year
28% PRESCRIBED INVESTOR RATE (PIR)	Cash	0.12%	0.33%	0.83%	–
	Conservative	–0.57%	–0.51%	1.68%	–
	Moderate	–0.64%	–0.57%	1.96%	–
	Balanced	–0.88%	–0.86%	2.37%	3.54%
	Growth	–0.96%	–1.01%	2.52%	2.04%
	High Growth	–1.23%	–1.33%	2.59%	3.37%
	Shares	–1.59%	–1.95%	2.09%	0.59%

Investment options		1 Month	3 Months	FYTD*	1 Year
17.5% PRESCRIBED INVESTOR RATE (PIR)	Cash	0.14%	0.39%	0.97%	–
	Conservative	–0.60%	–0.50%	1.90%	–
	Moderate	–0.70%	–0.55%	2.33%	–
	Balanced	–0.91%	–0.80%	2.76%	3.49%
	Growth	–0.96%	–0.92%	3.08%	3.44%
	High Growth	–1.25%	–1.24%	2.86%	3.45%
	Shares	–1.59%	–1.71%	2.58%	3.04%

Investment options		1 Month	3 Months	FYTD*	1 Year
10.5% PRESCRIBED INVESTOR RATE (PIR)	Cash	0.15%	0.42%	1.05%	–
	Conservative	–0.63%	–0.47%	2.22%	–
	Moderate	–0.67%	–0.53%	2.55%	–
	Balanced	–0.91%	–0.81%	2.83%	–
	Growth	–0.95%	–0.84%	3.37%	–
	High Growth	–1.21%	–1.11%	3.59%	–
	Shares	–1.58%	–1.69%	2.86%	1.93%

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INVESTMENT RETURNS FOR PERIODS ENDED 31 OCTOBER 2016

NEW ZEALAND DEFENCE FORCE FLEXISAVER SCHEME

Investment options		1 Month	3 Months	FYTD*
28% PRESCRIBED INVESTOR RATE (PIR)	Cash	0.11%	0.24%	0.69%
	Conservative	-0.55%	-0.55%	1.60%
	Moderate	-0.68%	-0.69%	1.87%
	Balanced	-0.85%	-0.90%	2.11%
	Growth	-0.95%	-1.03%	2.53%
	High Growth	-1.22%	-1.35%	2.63%
	Shares	-1.60%	-1.99%	1.98%

Investment options		1 Month	3 Months	FYTD*
17.5% PRESCRIBED INVESTOR RATE (PIR)	Cash	0.18%	0.37%	0.91%
	Conservative	-0.65%	-0.73%	1.59%
	Moderate	-0.69%	-0.70%	2.09%
	Balanced	-0.89%	-0.80%	2.78%
	Growth	-0.95%	-0.93%	3.07%
	High Growth	-1.25%	-1.39%	3.00%
	Shares	-1.50%	-1.79%	2.46%

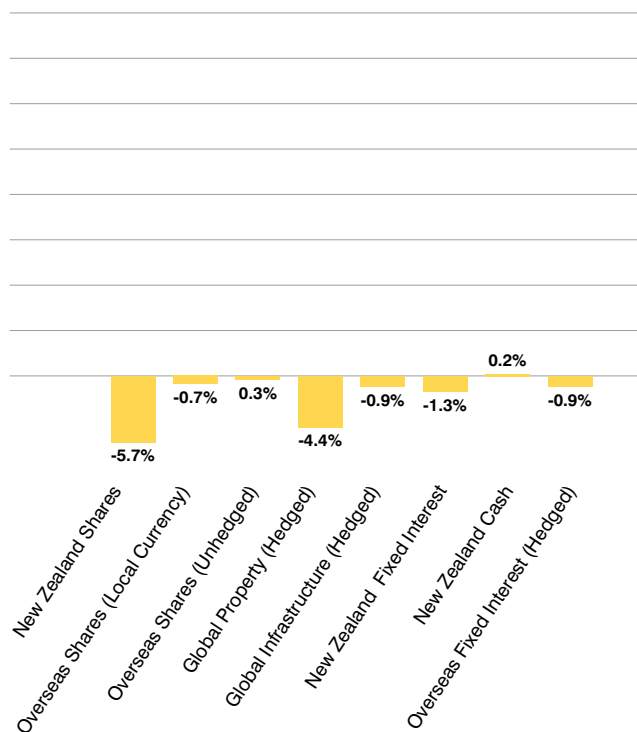
Investment options		1 Month	3 Months	FYTD*
10.5% PRESCRIBED INVESTOR RATE (PIR)	Cash	0.12%	0.31%	0.85%
	Conservative	-0.62%	-0.49%	2.11%
	Moderate	-0.70%	-0.75%	2.28%
	Balanced	-0.90%	-0.79%	3.00%
	Growth	-0.92%	-0.84%	3.31%
	High Growth	-1.21%	-1.20%	3.35%
	Shares	-1.54%	-1.67%	2.92%

Notes

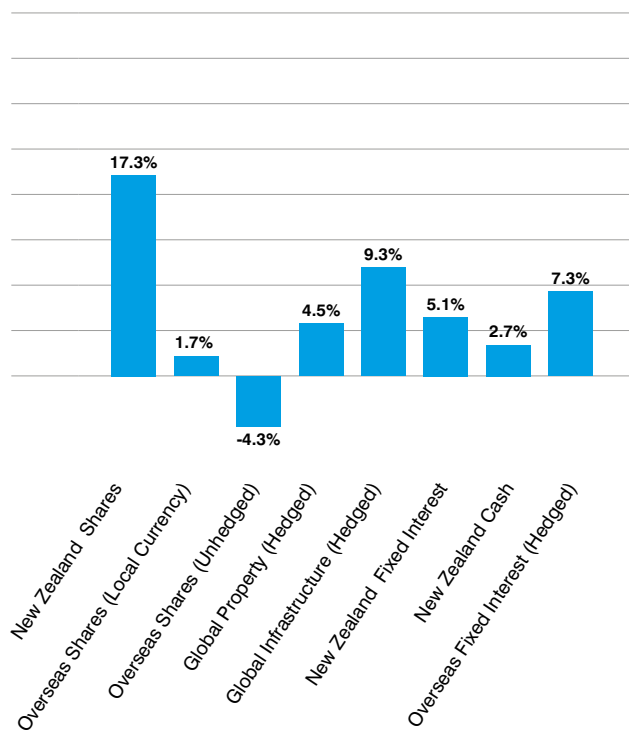
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FINANCIAL MARKETS FOR PERIODS ENDED 31 OCTOBER 2016

ONE MONTH



ONE YEAR



KEY

NZ SHARES

S&P/NZX 50 (with ICs)

OVERSEAS SHARES (LOCAL CURRENCY)

MSCI World (Local Currency)

OVERSEAS SHARES (UNHEDGED)

MSCI World (Unhedged)

GLOBAL PROPERTY (HEDGED)

FTSE EPRA NAREIT Developed

GLOBAL INFRASTRUCTURE (HEDGED)

FTSE Global Core Infrastructure 50/50

NZ FIXED INTEREST

S&P/NZX NZ Government Bond

NZ CASH

ANZ 90 Day Bank Bills

OVERSEAS FIXED INTEREST (HEDGED)

Barclays Capital Global Aggregate

JARGON BUSTERS

HEDGE

It is a defensive strategy used to minimise investment risk. Often used for funds, investing in overseas investments, to reduce the negative effects of moves in currency exchange rates. When a fund, such as a overseas shares, is *unhedged*, investors are exposed to changes in the currency.

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