

2018  
August

# MONTHLY REVIEW

Review of Fund Performance and Current Events



*Turkey is at ground zero of current Emerging Markets capital flight. With an increasingly despotic leader (PM Erdogan pictured) alienating Western allies the Turkish stock market is down 15% and the Lira off nearly 90% over one year.*



# MARKET UPDATE

"These are bullets, cannonballs and missiles of an economic war waged against our country"

*President Recep Tayyip Erdogan of Turkey*

## MARKET COMMENTARY

The S&P500 was up over August, delivering its fifth consecutive monthly gain. Equity valuations in developed markets - particularly the US - remain high, yet stock prices continue to rise. We maintain a defensive approach to our investing, steering towards sectors we believe will hold up better if markets turn. While the US equity prices have continued their relentless rise, emerging market have struggled.

**Emerging markets strife:** Emerging economies have recently been hit hard - Turkey's President (*quote above*) makes it sound like a Western plot, but the wounds are self inflicted. Argentina sought a US\$50 billion bailout and raised interest rates to 60% trying to stop further currency falls. Currencies of India, Indonesia, Brazil and Turkey hit multi-year lows against the US dollar. Investors have lost confidence in EM monetary policies and their ability to repay debt - when confidence is eroded investors respond by hitting the exits, and often finding liquidity (i.e. the ability to sell) in EM markets can be a problem.

**Amazon hits \$1 trillion:** In July Apple's market value hit US\$1 trillion, now it's Amazon's turn. Over 21 years as a listed company its share price has grown astonishingly from US\$18 to US\$2,050. The difference between Apple and Amazon - it took Apple 38 years to hit this milestone while Amazon did it in about half the time (*source: Craigs*).

**When big is too big:** Market dominance of the largest US companies is staggering. They don't just compete in a market, they are the market. Facebook and Google hoover up two thirds of US online advertising revenue. Amazon controls 40% of US online shopping. In some countries nine out of every ten

internet searches go through Google, while Apple's profits equal US\$8 for every person on earth! Tech giants have parallels with unregulated utility companies with a market stranglehold. This combination doesn't tend to lead to great long-term consumer outcomes.

**Anti-competitive action:** Past action against 6 massive anti-competitive companies (like Standard Oil in 1911, IBM in 1969 and Microsoft in 1998) started when their median profit was 0.24% of US GDP - Apple already exceeds this and within 10 years Amazon, Alphabet and Microsoft are expected to join (plus Facebook is close behind). Expect much more noise around regulation of large US tech giants (*Source: The Economist*).

**CEO pay:** How much should a boss be paid relative to the same firm's median pay? US firms now need to disclose this (some large corporates like GE, Johnson & Johnson and AT&T lobbied hard against this change). For US listed firms worth more than US\$1 billion, the average 'CEO to median' ratio is 130x. Across 700 companies the median CEO salary was US\$9 million compared to the "standard" employee median at US\$69,000. Particularly interesting is comparing similar companies - for example PepsiCo with a ratio over 600 is three times greater than Coca-Cola (which has a ratio just over 200).

**Something new to tax:** Financial analysts are not relying heavily on the CEO to median pay reporting - however it has been welcomed by the city of Portland in Oregon. The city has introduced a 10% business tax surcharge for companies where the pay ratio exceeds 100:1 and a 25% surcharge for a ratio above 250:1 (*Source: The Economist*).

## UNIT PRICES as at 31 August

Pathfinder Global  
Responsibility Fund  
**\$1.1039**

Pathfinder Global Water Fund  
**\$1.9685**

Pathfinder Global Property  
Fund  
**\$1.1764**

Pathfinder World Equity Fund  
**\$1.8977**

Pathfinder Commodity Plus  
Fund  
**\$1.0601**

## OUR PEOPLE

John Berry - Chief Executive Officer

Paul Brownsey - Chief Investment Officer

Karl Geal-Otter - Investment Analyst

Bob McCutcheon - Strategy, Compliance

## THE FOCUS | The Good-Bad-Good of Share Buybacks

"Corporate cocaine", "sugar high for corporations" and "stock price manipulation".

This month we discuss the good-bad-good of share buybacks. Buy backs are in vogue in the US, with Goldman Sachs predicting US\$1 trillion of buybacks this year.

[Click here to read the full story](#)



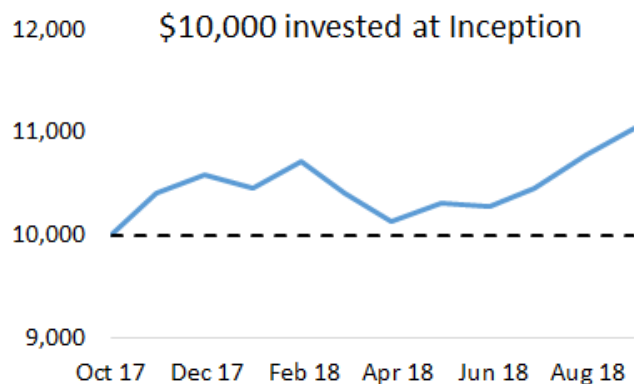
Phone : 09 489 3802

# PORTFOLIO UPDATES

## GLOBAL RESPONSIBILITY FUND

The socially responsible Global Responsibility Fund is designed to provide diversified equity exposure to developed markets. There are 3 tiers to the responsible investment process: (1) exclusion of corporate activities like tobacco and gambling (2) elimination of high controversy companies and (3) investment focus on high environmental, social and governance ratings. Currency hedging is used to reduce foreign currency exposure.

|                        |                                |  |
|------------------------|--------------------------------|--|
| Performance<br>1 month | Performance<br>since inception | \$10,000 invested at<br>inception is now worth |
| <b>2.4%</b>            | <b>10.4%</b>                   | <b>\$11,039</b>                                |



## FUND COMMENTARY

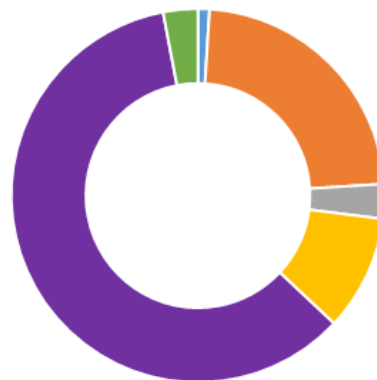
The Fund rose 2.4% over August. Its underweight of fossil fuel energy stocks helped - this was the worst performing US sector for the month (down 3.8%). The underweight to IT stocks didn't help - their strong run continued. The Fund is also underweight to Asia ex Japan - interestingly, Credit Suisse recently identified 4 significant challenges to Asian markets:

- (1) economic factors such as China's de-leveraging (debt reduction)
- (2) currency stress driven by expectations of higher US interest rates coming soon
- (3) geopolitical tensions, in particular the trade standoff between the US and China
- (4) trading issues like the unwind of illiquid EM investments



Donut chart showing the asset allocation of the Global Responsibility Fund:

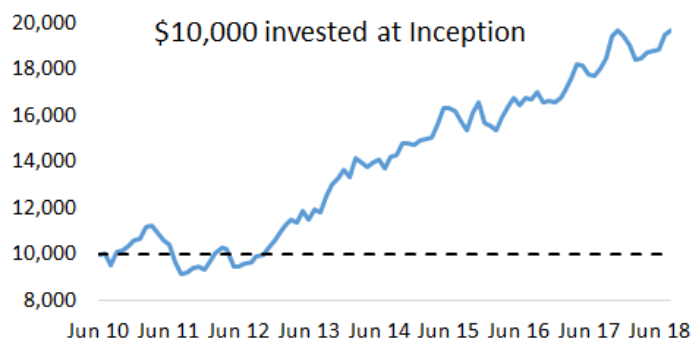
- Cash | 1%
- Europe ex UK | 23%
- Asia Pacific ex Japan | 3%
- Japan | 10%
- North America | 60%
- UK | 3%



## GLOBAL WATER FUND

The Global Water Fund is designed to provide socially responsible investment in the water industry. This includes listed water utility, industrial, tech and materials companies. Currency hedging is used to reduce foreign currency exposure.

|                        |                             |  |
|------------------------|-----------------------------|--|
| Performance<br>1 month | Performance<br>5 years p.a. | \$10,000 invested at<br>inception is now worth |
| <b>0.9%</b>            | <b>10.7%</b>                | <b>\$19,685</b>                                |



## FUND COMMENTARY

The Water Fund rose by 0.9%. It is a conservative fund by nature as it currently has a weighting of around 30% to utility companies - capital and revenue stable companies by definition.

We're particularly interested in new technologies helping solve the world's water crisis. In Brazil 37% of water that enters their network disappears (from leaks, theft etc). A new smartphone app can "listen" to a pipe's flowing water. Artificial Intelligence then uses a huge database of pipe sounds to determine where leaks or theft occurs nearby. The software is like phone apps "Shazam" or "Soundhound" that listen and identify music. This new tech could be a welcome game changer for identifying significant water loss in failing infrastructure worldwide (source: *The Economist*).



Donut chart showing the asset allocation of the Global Water Fund:

- Cash | 1%
- Europe ex UK | 25%
- Asia Pacific ex Japan | 2%
- Japan | 6%
- North America | 51%
- UK | 10%
- Emerging Markets | 5%



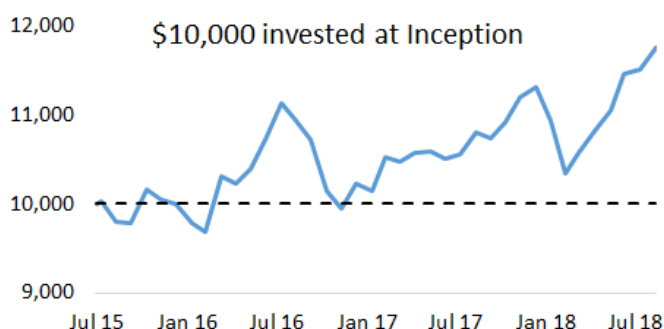


# PORTFOLIO UPDATES

## GLOBAL PROPERTY FUND

The Global Property Fund is designed to provide socially responsible investment in global listed property stocks. It has a significant allocation to NZ listed property, recognising the preference of NZ investors to overweight the local market. Currency hedging is used to reduce foreign currency exposure.

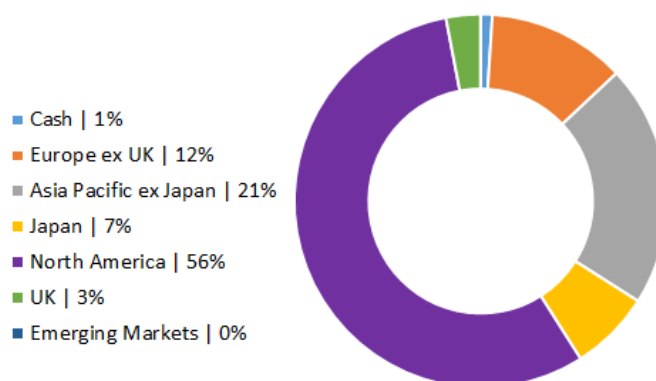
|                                       |  |   |
|---------------------------------------|--|---|
| Performance<br>1 month<br><b>2.2%</b> | Performance<br>3 years p.a.<br><b>6.3%</b> | \$10,000 invested at<br>inception is now worth<br><b>\$11,764</b> |
|---------------------------------------|--|---|



## FUND COMMENTARY

Listed property stocks continued higher over August with our fund up 2.2%. One year fund performance remains strong at 8.9%, which is almost 2.5% ahead of its benchmark and more than 2.4% ahead of both the AMP and ANZ property funds.

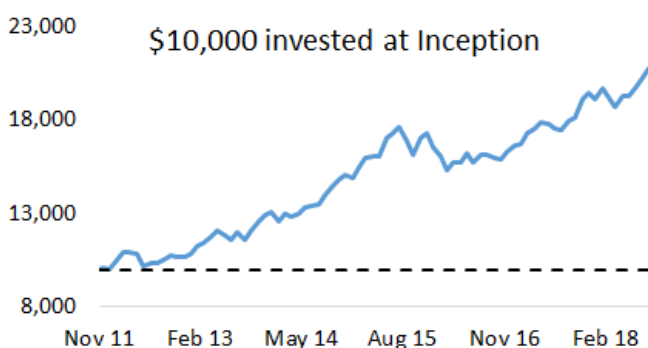
US commentator Ben Carlson recently looked at the correlation of listed property relative to broader US stocks. Since 2009 stocks have outperformed, returning 15.1% p.a. to 13.5% for property, but what's really interesting is the very low correlation between them (at 0.20). Correlations do change over time, and it is correlation in falling markets that matters most (as you want some portfolio assets going up as equities fall). At a time when fixed income portfolios contain massive interest rate and credit risk and in a world where rates are more likely to rise than fall, property provides a useful counter balance to core equities.



## WORLD EQUITY FUND

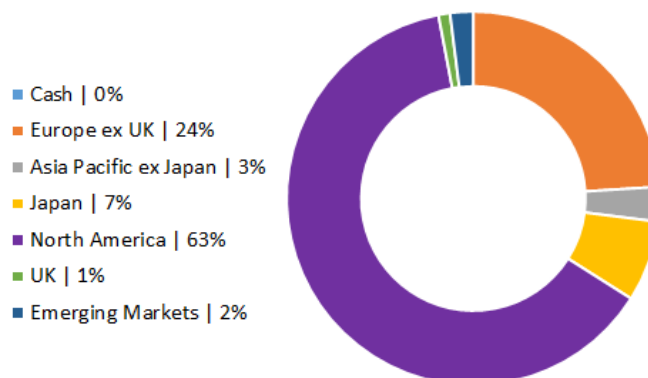
The World Equity Fund is designed to provide diversified socially responsible exposure to global equities (across both developed and emerging markets). The fund invests in ETFs to access global equity sectors and regions, and uses currency hedging to reduce foreign currency exposure.

|                                       |   |   |
|---------------------------------------|---|---|
| Performance<br>1 month<br><b>2.5%</b> | Performance<br>5 years p.a.<br><b>12.4%</b> | \$10,000 invested at<br>inception is now worth<br><b>\$20,742</b> |
|---------------------------------------|---|---|



## FUND COMMENTARY

The World Equity Fund performed well in August, up 2.5%. Over 5 years the fund is up 12.4% per annum. Key positioning at the moment includes a very low weight to emerging markets and a relatively un-hedged position at around 24%. A low hedging ratio is important as it provides a healthy insurance policy should global markets enter a serious "risk off" phase as typically, falling global markets are accompanied by a fall in the NZD which will help mitigate the downside. While we don't see an immediate catalyst for the end of the current bull market we are conservative. Lots of possible speedbumps from trade wars to North Korea to Iran to Russia to Emerging markets to Italian elections to Brexit negotiations to US Debt concerns to inflation but certainly in the US, earnings and economic growth remain on a solid footing.



# PORTFOLIO UPDATES

## COMMODITY PLUS FUND

The Commodity Plus Fund is designed to provide exposure to global commodity markets. The investment process targets the "mean reverting" nature of commodities and can also allocate to cash for downside protection. The fund will not invest in thermal coal, uranium or the shares of commodity producers. Currency exposures are fully hedged.

Performance  
1 month

0.7%

Performance  
5 years p.a.

1.6%

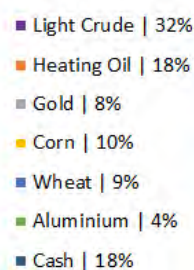
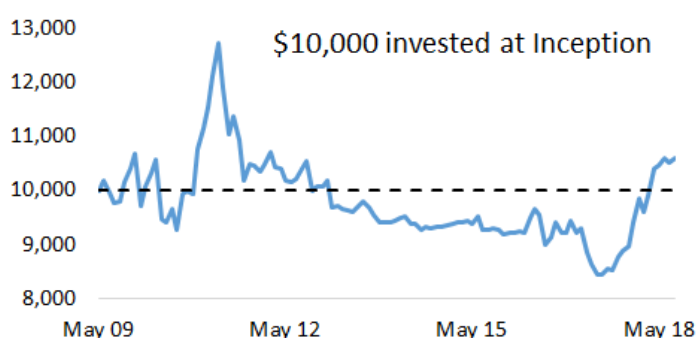
\$10,000 invested at  
inception is now worth

\$10,601

## FUND COMMENTARY

Commodities are taking something of a breather right now with some negative pressure on US agriculturals and industrial metals as China targets US exports for retaliatory tariffs. Oil prices are broadly stable, strong demand continues to keep stockpiles under pressure and fears of Russian and Iran supply disruptions keeping oil prices firm.

The power of the mean reversion approach we follow was shown in August with the broad Bloomberg commodity index (with static weightings) down 1.8% versus our +0.7%. Over one year the Commodity Plus Fund has outperformed the index by nearly 24%.



## FUND PERFORMANCE

| As at 31 August 2018                                | 1 Month | 3 Month | 6 Month | 1 Year | 2 Years (p.a.) | 3 Years (p.a.) | 5 Years (p.a.) | 7 Years (p.a.) | Volatility |
|---|---------|---------|---------|--------|----------------|----------------|----------------|----------------|------------|
| Global Responsibility Fund                          | 2.4%    | 7.3%    | 6.1%    |        |                |                |                |                | 8.0%       |
| Morningstar Developed Markets Index NR (50% Hedged) | 2.6%    | 7.1%    | 8.5%    |        |                |                |                |                | 7.8%       |
| Global Water Fund                                   | 0.9%    | 4.8%    | 7.0%    | 9.1%   | 8.6%           | 7.7%           | 10.7%          | 11.6%          | 8.5%       |
| PIO Global Water ETF (50% Hedged)                   | 1.3%    | 4.6%    | 7.7%    | 13.6%  | 12.2%          | 8.2%           | 9.1%           | 9.4%           | 10.5%      |
| Global Property Fund                                | 2.2%    | 6.5%    | 13.8%   | 8.9%   | 3.8%           | 6.3%           |                |                | 8.9%       |
| Morningstar Real Estate Index TR (75% Hedged)       | 2.1%    | 6.2%    | 12.9%   | 6.5%   | 3.5%           | 7.8%           |                |                | 10.1%      |
| World Equity Fund                                   | 2.5%    | 7.7%    | 8.2%    | 15.7%  | 13.5%          | 7.2%           | 12.4%          | 10.2%          | 9.1%       |
| Morningstar Global Markets Index NR (50% Hedged)    | 2.2%    | 6.1%    | 6.8%    | 16.3%  | 17.0%          | 11.2%          | 11.7%          | 10.9%          | 8.1%       |
| Commodity Plus Fund                                 | 0.7%    | 1.3%    | 10.3%   | 24.2%  | 7.7%           | 4.6%           | 1.6%           | -0.4%          | 6.8%       |
| Bloomberg Commodity Index TR (100% Hedged)          | -1.8%   | -7.2%   | -4.1%   | 0.5%   | 1.7%           | -1.9%          | -8.0%          | -8.8%          | 11.7%      |

**Disclaimer:** Pathfinder is a fund manager and does not give financial advice. Before making any decision to invest you should (a) consult your financial adviser and (b) read the Product Disclosure Statement. This report is for information purposes only. Opinions constitute Pathfinder's judgment at the time of writing and are subject to change. All returns calculated after fees before tax using the unit price.

Disclosure of interest: All of our staff invest in Pathfinder's funds on the same terms as you.

The Global Water Fund and Global Responsibility Fund have been designated a Certified Responsible Investment by the RIAA (Responsible Investment Association Australasia). See [www.responsibleinvestment.org](http://www.responsibleinvestment.org) for more details

\*The Certification Symbol signifies that a product or service offers an investment style that takes into account environmental, social, governance or ethical considerations. The Symbol also signifies that the Pathfinder Global Water and Global Responsibility Fund Fund adheres to the strict operational and disclosure practices required under the Responsible Investment Certification Program for the category of Product Provider. The Certification Symbol is a Registered Trade Mark of the Responsible Investment Association Australasia (RIAA). Detailed information about RIAA, the Symbol and the Pathfinder Global Water Fund's and the Pathfinder Global Responsibility Fund's methodology, performance and stock holdings can be found at [www.responsibleinvestment.org](http://www.responsibleinvestment.org), together with details about other responsible investment products certified by RIAA.

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