Aurora Capital

Aurora Liquidity Fund

QUARTERLY UPDATE SEPTEMBER 2023

Welcome to the new and improved Aurora KiwiSaver Scheme!

WHAT WE'VE BEEN DOING IN THE AURORA MULTI-ASSET PORFOLIOS

We get that your KiwiSaver funds are currently invested in the Aurora Liquidity Fund, which is a cash fund. That said, we're excited to you know that we've recently made important enhancement to the other Aurora Capital portfolios, which invest in multiple investment sectors. We've added new specialist fund managers to manage specific investment sectors. This approach, where multiple managers are combined in a portfolio, is called multi-manager.

The move to multi-manager was completed in August. With that done, we'd like to tell you all about the fantastic new fund managers we've appointed. We thought this would also be a good time to update you on how we invest. That's because we believe it's important to be open and transparent about how and where the Aurora KiwiSaver Scheme is being invested.

This Quarterly Update report is therefore a little different to previous reports, but usual transmission will return in the next Quarterly Update. We hope you stay tuned!

HOW WE INVEST

We’re focused on delivering solid investment returns so that you can grow your wealth with your KiwiSaver money. To help us get there, we select best-in-class, specialist fund managers from around the world to actively manage the underlying assets of each asset class. We invest in assets that can grow over the long-term and use a mix of responsible investing approaches that can help to improve the climate and the environment.

We actively manage the portfolios

Active management in the Aurora portfolios takes place at two levels: through active asset allocation decision-making; and by selecting actively managed underlying investment strategies. We believe that actively managed portfolios are better equipped to manage the risk of loss during periods where markets are falling, disorderly and going through high levels of instability.

We build well-diversified portfolios to help manage risk

All investments involve some level of risk. While risk can't be eliminated, it can be managed. Diversification is a good way to manage risk by investing in assets that are expected to perform differently to one another in normal market conditions. Put simply, if one asset falls and a different asset rises, this can reduce the volatility of returns. We diversify risk by investing across different asset classes, geographies, and sectors. We also select fund managers that have different investment drivers and portfolio characteristics.

We aim for competitive investment returns while investing to improve the health of the planet.

We're biased to a mix of investment strategies that target a low-carbon economy and can contribute to a more sustainable future. All of the underlying asset class strategies we select aim to outperform their respective benchmarks.

We use a mix of responsible investing approaches:

- **Sustainability**: We're biased to investing in companies and securities that are contributing to a more sustainable future. We support the United Nations (UN) Sustainable Development Goals (SDGs), and we specifically focus on the SDG's that can positively influence the climate and environment.

- **Exclusion:** Our portfolios exclude companies that we believe do more social or environmental harm than good. While exclusion is important in avoiding the most harmful activities, our view is that exclusion alone can't create the change that's needed to improve the climate crisis, as companies need capital to fund the replacement of carbon emitting processes. For more information on exclusions, please read the Aurora Statement of Investment Policy and Objectives.

- **ESG integration**: we aim to reduce and manage environmental, social and governance ("ESG") risks by making sure that the managers we select integrate ESG factors into their investment processes.

Figure 1: We use a mix of responsible investing approaches and prioritise the climate and environment.

We monitor and report financial and non-financial performance

For non-financial measures, we use independent third-party sources to track the carbon emissions of a portfolio and its alignment to sustainability goals. You can find these in every Quarterly Update and the monthly Fact Sheets, available on the Aurora Capital website.

OUR NEW LINEUP OF SPECIALIST FUND MANAGERS

ASSET CLASS	FUND MANAGER	ABOUT
Global Equities	Dimensional DIMENSIONAL FUND ADVISORS LTD.	A large global asset manager founded in 1981. They have 1400 staff in 14 offices globally. They have a high calibre research team who collaborate with leading academics in finance and economics to develop their investment strategies.
Global Equities	Stewart Investors	A large global equity fund manager with offices in Edinburgh, London, Singapore and Sydney. Founded In 1988. They are long-term focused and actively engage with companies on sustainability issues.
NZ Equities	mint ASSET MANAGEMENT	Leading NZ fund manager, founded in 2006. They have strong ESG credentials with ESG integrated into their decision-making, with a focus on negative / positive screens and active engagement.
Global Infrastructure	First Sentier Investors	Founded in Australia in 1988, they are now a global asset management business with operations in Asia, Europe, North America, and Australia. They invest in companies that are positioned to benefit from sustainable development.
Global Bonds	AIM Affirmative Investment Management	AIM was established in in 2014, making them of the first global impact bond managers. The business is headquartered in London, with offices around the globe. They have the longest track record in impact bond investing.
NZ Bonds	Mercer	The Cash and bond capability is managed by the highly rated former AMP Capital Fixed Income team. Mercer has an international network of 2000 investment experts, based in 43 countries.
Cash	Mercer	The Cash and bond capability is managed by the highly rated former AMP Capital Fixed Income team. Mercer has an international network of 2000 investment experts, based in 43 countries.

All of the fund managers we've selected have a focus on sustainability, climate and the environment while also aiming for strong financial returns. We undertake rigorous research of the fund managers in our selection and monitoring process. You can learn more about the factors we consider when appointing fund managers in Other Material Information about the Aurora KiwiSaver Scheme.

Each of the new fund managers have a strong business, a highly regarded investment team, and a proven investment process. They are each signatories to the UN Principles for Responsible Investment UNPRI and are making positive contributions to the UN SDGs in the strategies we've selected. Five out of the six fund managers that we've appointed have Responsible Investment Certification from the Responsible Investment Association Australasia (RIAA), and the sixth manager is currently in the process of getting certified.

- Great Business
- Quality investment team
- Proven investment process
- Signatory to UNPRI
- Positive contribution to UN SDG's

Investment markets

WHAT HAS DRIVEN INVESTMENT MARKETS?

After charging higher over the first half of 2023, equity markets started the September quarter strong but couldn't hang onto these early gains and ended the period weaker. This was most likely due to a shift in sentiment about future interest rates. At first, there was optimism that an economic downturn in the United States would be soft (a mild recession that doesn't lead to a huge rise in the unemployment rate) in coming months, and as a result, the era of high interest rates would soon be over. This optimism, however, soon evaporated as the US Federal Reserve indicated that high interest rates were likely to remain that way for some time, that is, that rates would stay 'higher for longer.'

Why? Simply put, the U.S economy has proven to be stronger than expected. Despite the dramatic interest rate increases from the U.S central bank, the economy is holding up quite well. We can thank low unemployment and healthy consumer spending for this stunning resilience in economic growth. In the meantime, core inflation appears to be slowing down (year-on-year) in the U.S and also across most economies. While this is good to see, inflation still remains well above target ranges. As long as economic growth remains feisty, policy makers will be in no rush to lower interest rates from their current high levels. On balance, we think it's likely that rates will rise one or two times more in the U.S, and will not be lowered for some time. A soft landing is still possible, although uncertainty remains. It's worth remembering that the majority of interest rate hiking cycles in the U.S do usually end up as recessions, with job losses.

Government bonds also weakened in the quarter, as bond yields rose. In the U.S, the most dramatic increase in bond yields was seen in longer dated maturities, with 10 year bonds rising to their highest levels since 2007. While the continued strength of the economy pressured yields higher, there were also increased worries about the enormous debt levels being run by the government. This resulted in lenders demanding higher compensation in the form of higher bond yields, for bonds with longer-dated maturities. Debt burden concerns in the U.S even led to a credit rating downgrade of the U.S, by Fitch Ratings. Central banks in the U.S, Europe (ECB) and the U.K all raised official interest rates in the September quarter, in acknowledgement of stubbornly high inflation.

Financial performance returns

AURORA LIQUIDITY FUND AS AT 30 SEPTEMBER 2023

	RETURNS		
	3 month %	6 month %	1 year %
Strategy (after fees, before taxes)	1.29	2.55	4.63
Benchmark**	1.42	2.78	4.96

** Benchmark is the Bloomberg NZ Bond Bank Bill Index
As at 30 September 2023

Positive returns for the quarter were underpinned by healthy cash yields. The official (overnight) cash rate in New Zealand was kept steady at 5.5%. Over the 1 year period, cash has continued to provide solid returns to investors in an environment characterised by uncertainty and price volatility in other asset classes.

Looking ahead, it's likely that cash rates have peaked or are very close to peaking. The dominant sentiment is that the N.Z official cash will stay higher for longer, which is also the prevailing sentiment for official cash rates in the rest of the world. The Reserve Bank of New Zealand indicated in August that the cash rate would need to stay higher for longer in order to bring down inflation, and that there was a small chance of another rate hike of 25 basis points in 2024, which would take the cash rate to 5.75%. The central bank also indicated that the cash rate was unlikely to be lowered until the first half of 2025.

All eyes are on signs of easing inflation, which would give the central bank a reason to lower the cash rate sooner. If inflation continues to hover near its current levels, we can expect that the cash rate will stay at this higher level for longer.

Questions?

If you have questions about this report, please contact your adviser who will be happy to help.

We welcome all feedback and would like to hear from you if you have any questions or concerns about your investment, as this can form the basis of future articles and reports that we write. We invite you to ask us questions through our website: www.aurora.co.nz, and through your adviser.

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