

Home country bias – Time to do something about it?

12 May 2021

10.00am – 10.45am

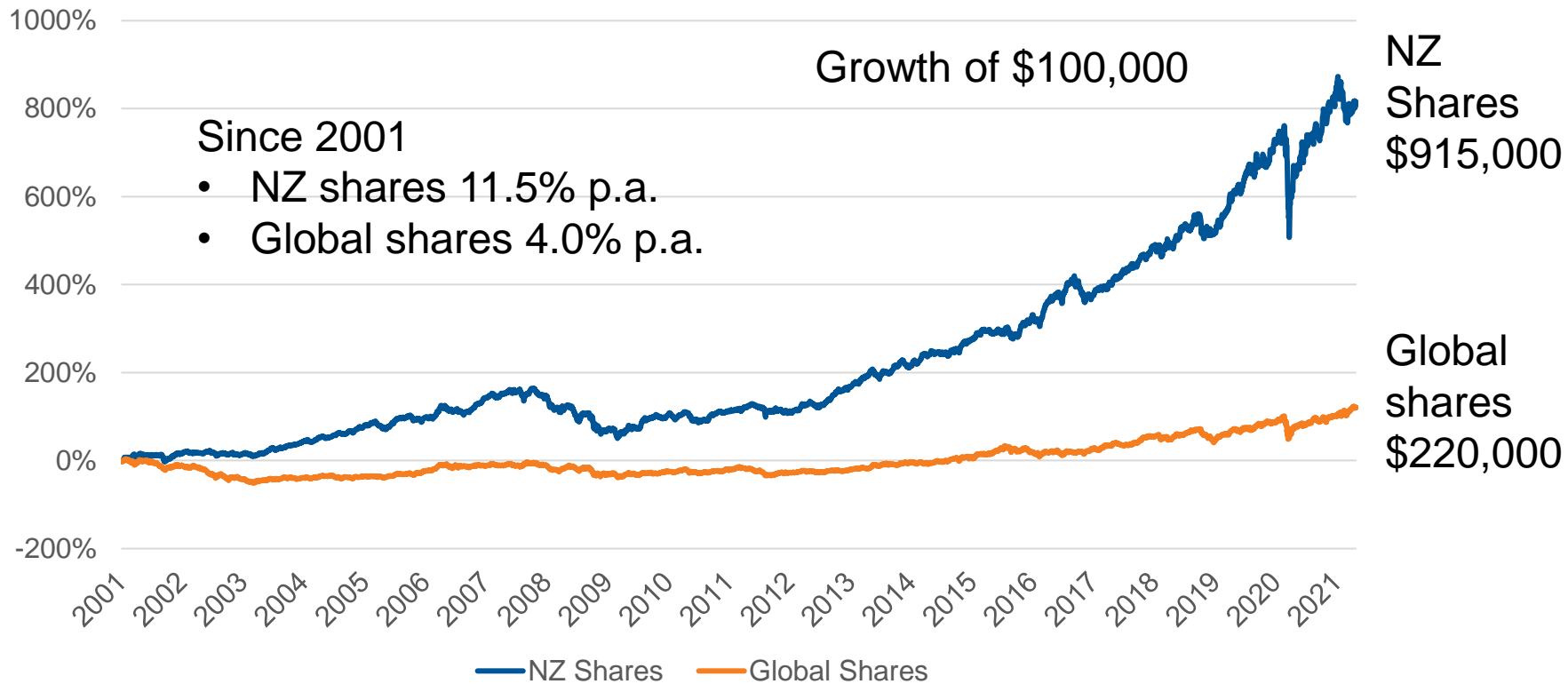
The webinar will begin shortly

Symon Parish
Senior Director, Head of Multi-Asset, APAC

Matthew Arnold, CFA, CAIA
Director, New Zealand

Team New Zealand has delivered...

Cumulative performance NZ shares and global shares 2001 – Apr 2021

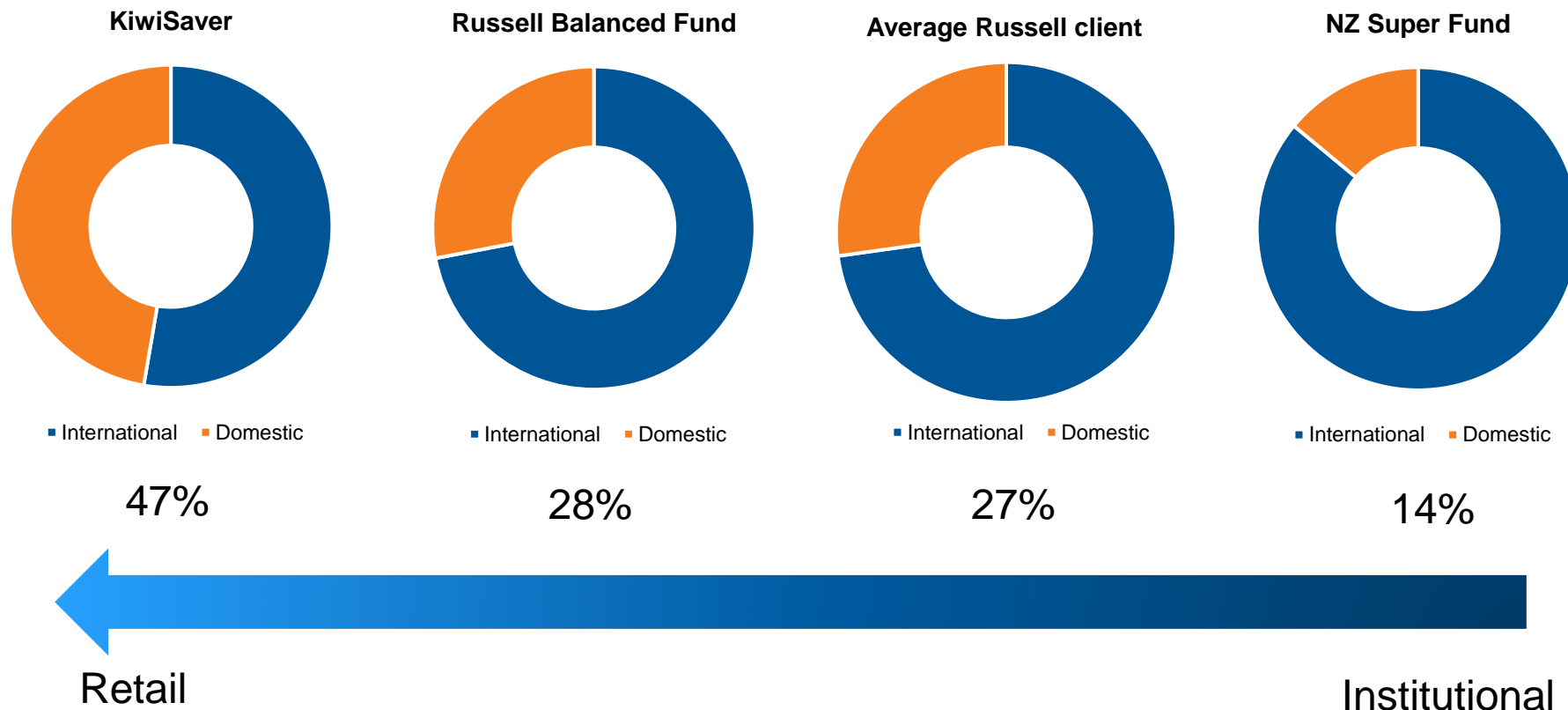


Source: Morningstar Direct, S&P/NZX 50 with ICs . MSCI ACWI NR in NZD. 1 Jan 2001 – 30 Apr 2021. Index returns do not include fees or taxes. Past performance is no guarantee of future results.

Just how big is the home country bias?

Average NZ exposure of different investors

International vs. domestic exposure by investor type

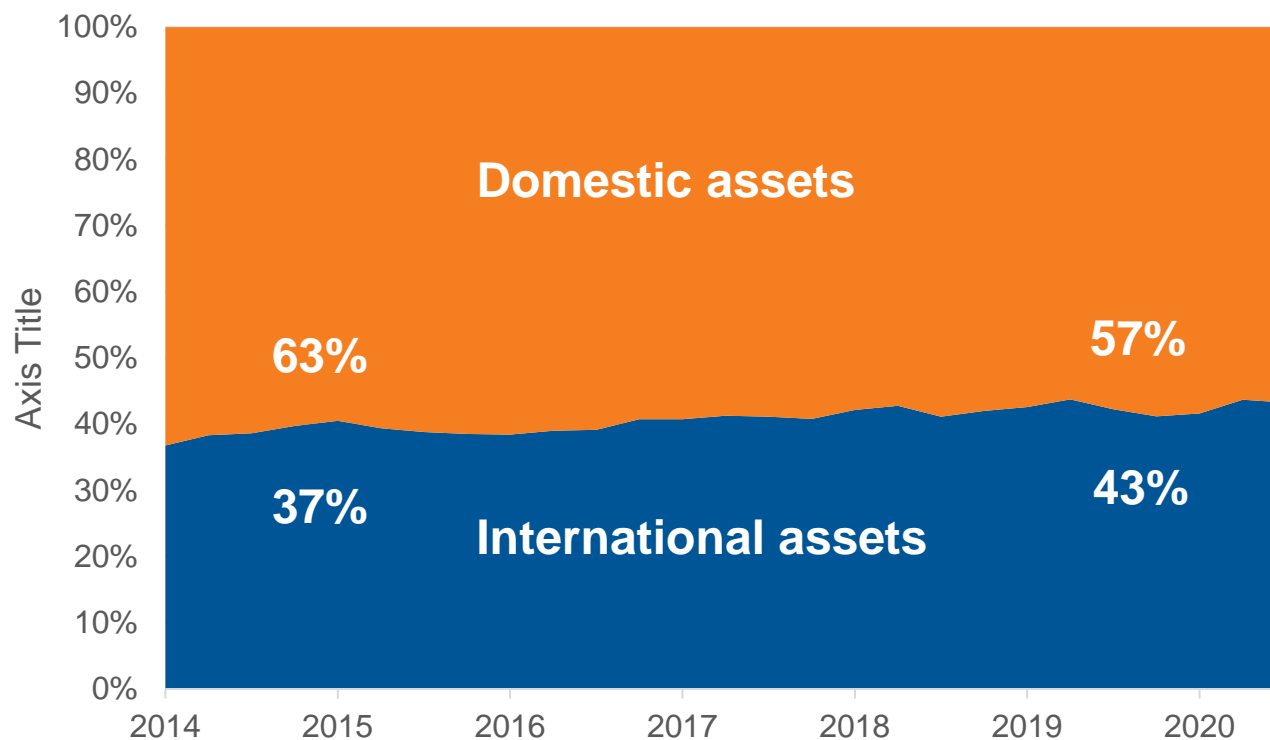


Source: Russell Investments, Morningstar, NZ Super fund website. Estimated KiwiSaver Asset Allocation and Average Russell Investments includes all risk profiles. Data as of 31 March 2021, except NZ Super June 2020.

NZ Managed Funds...

Some (modest) evidence of reduction in home bias...

International vs. domestic exposure in New Zealand managed funds



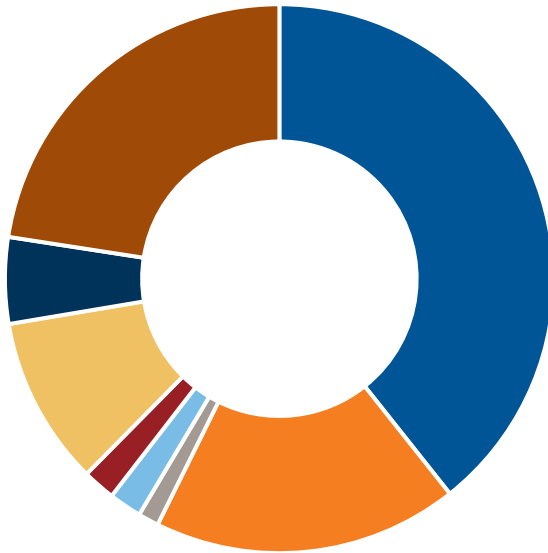
- Modest reduction, i.e. increase in international
- Note, does not capture 'offshore' funds

Source: Reserve Bank of New Zealand, Managed fund statistics, 2014 – 2020. .

KiwiSaver...

Some more evidence of reduction in home bias...

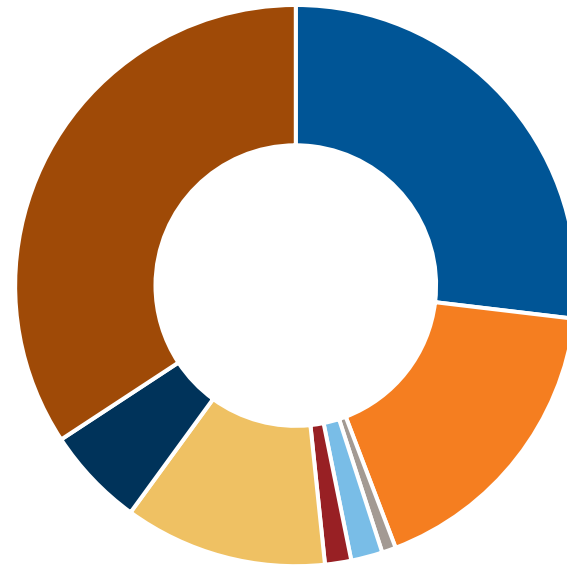
2012 Q4



- NZ Fixed (inc. cash)
- International fixed
- NZ Unlisted Property
- NZ Listed Property
- International listed property
- NZ Shares
- Australian Shares
- International Shares

International allocation: 42%

2021 Q1



- NZ Fixed (inc. cash)
- International fixed
- NZ Unlisted Property
- NZ Listed Property
- International listed property
- NZ Shares
- Australian Shares
- International Shares

International allocation: 53%

Source: Morningstar KiwiSaver Survey, as of December 2012 and March 2021.

Why do (NZ) investors have a home bias? ... is it 'rational'?

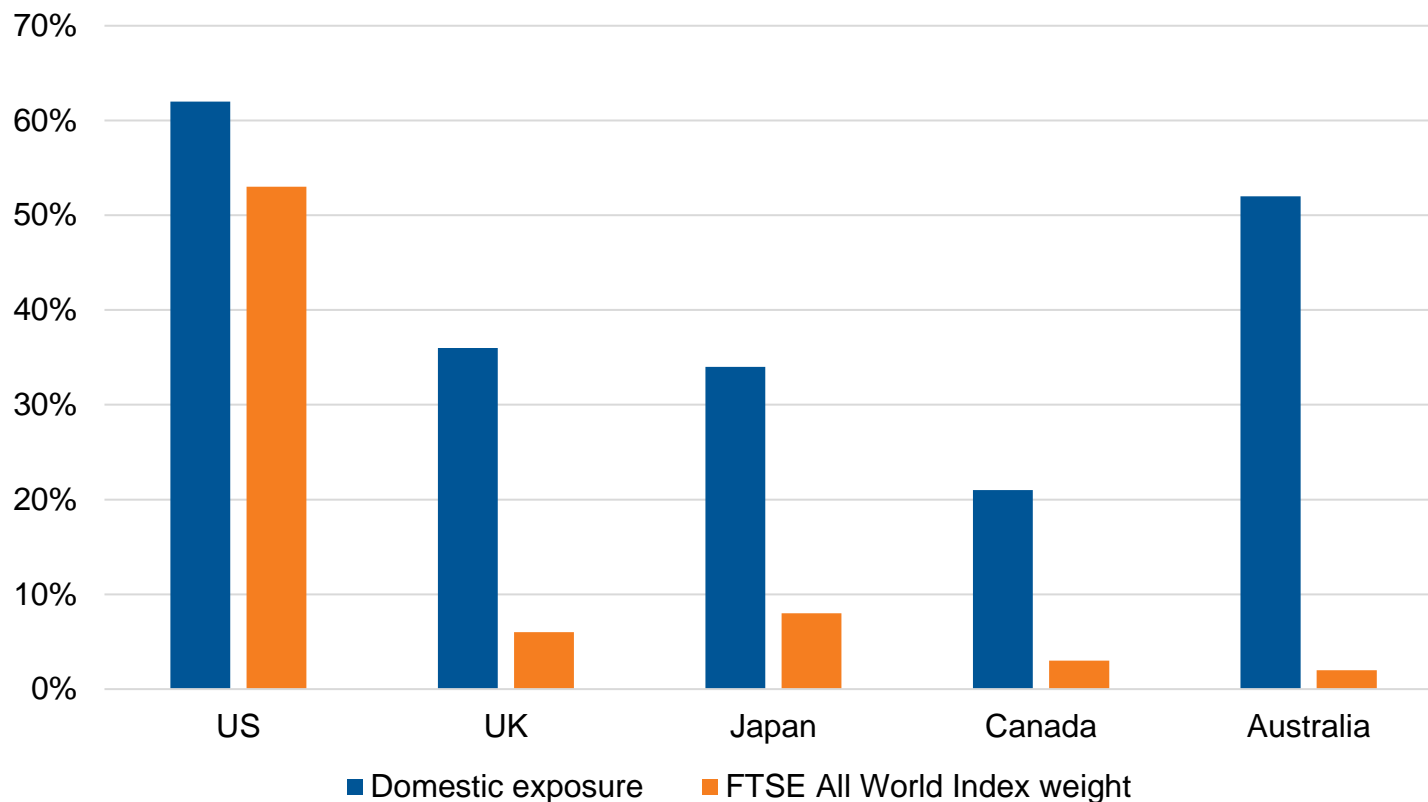
- > Investors typically start from 100% domestic (i.e. savings account, property investments etc.)...
- > **Familiarity bias** – buy what you know...
- > **Liabilities** in NZD (even though international assets can be hedged)
- > **Product availability** – products or services that offer access to NZ securities, managed/researched by local teams are (still) more readily available
- > Historically **higher costs** for international investing
- > Cash, fixed income allocations tend to be domestic focused
- > NZ dividends benefit from **imputation credits** which can 'add' c. 1.3% to after tax return for taxable investors, while cap gains are typically not taxed*
- > Research suggests **7% - 11%** 'overweight' in NZ shares is 'rational' relative to weight if there was no tax advantage**

*S&P/NZX 50 TR versus TR with imputation credits, 10 years ending 30 Apr 2021. **The potential effect of taxes on the equity home bias in New Zealand PIEs, S McDowell, J Lee, A Marsden (2021)

Is home bias a feature globally?

Average home vs. total equity (pension funds)

Estimated pension fund allocation to domestic equities relative to market cap weight (2018)



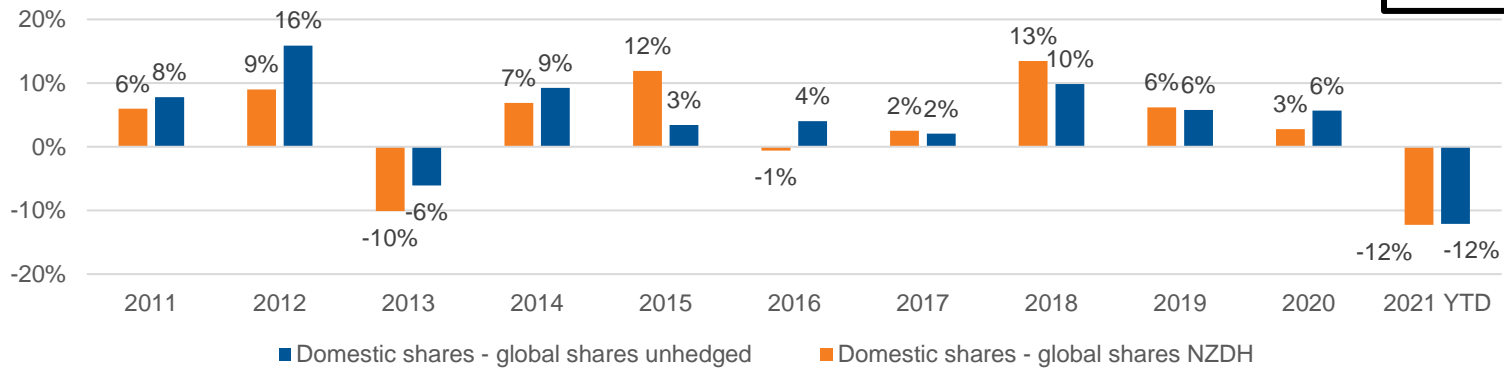
Source: FTSE Russell, Willis Towers Watson, as of Dec 2018.

Has it paid off to have a home bias?

Yes for shares? Hmmmm.... For fixed interest

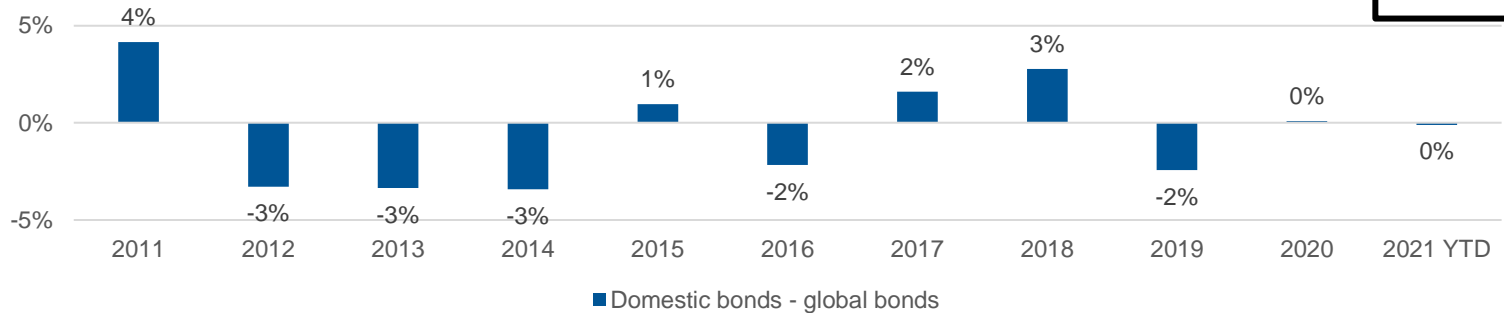
Outperformance of NZ Shares vs. global (hedged and unhedged) 2010 – 2021 year-to-date April

- 9/10 NZD
- 8/10 NZD-H



Outperformance of NZ fixed interest vs. global (hedged) 2010 – 2021 year-to-date April

- 5/10 NZD-H

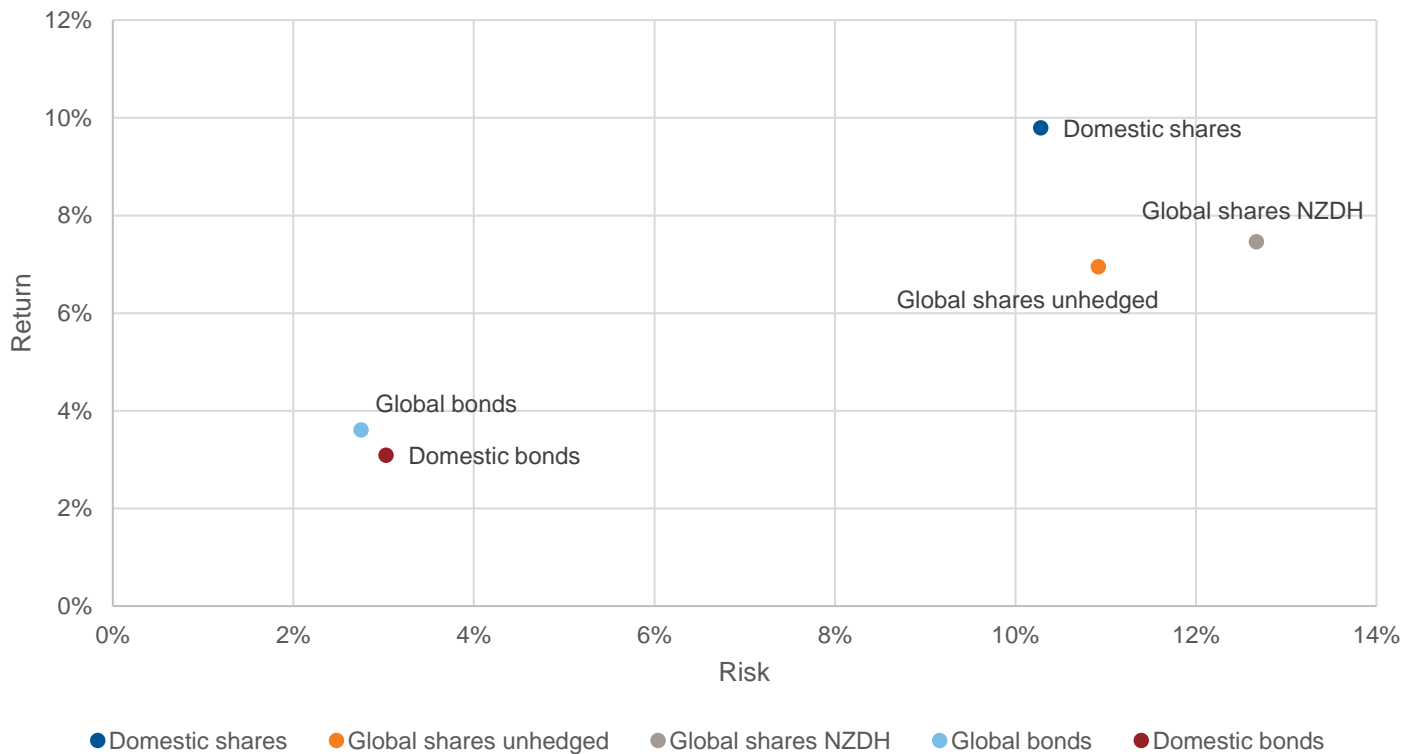


Source: Morningstar Direct. Domestic shares: S&P/NZX 50 index GR including imputation credits. Global shares: MSCI ACWI NR index, MSCI ACWI NR - NZDH index. Global bonds: Bloomberg Barclays Global Aggregate NZDH index. Domestic bonds: S&P/NZX NZ Composite Invest Grade. YTD ending 30 April 2021. In NZD. Past performance is no guarantee of future results.

How about when risk is considered?

... generally, yes...

Risk-return characteristics (Trailing 10 year period ending 20 Apr 2021)



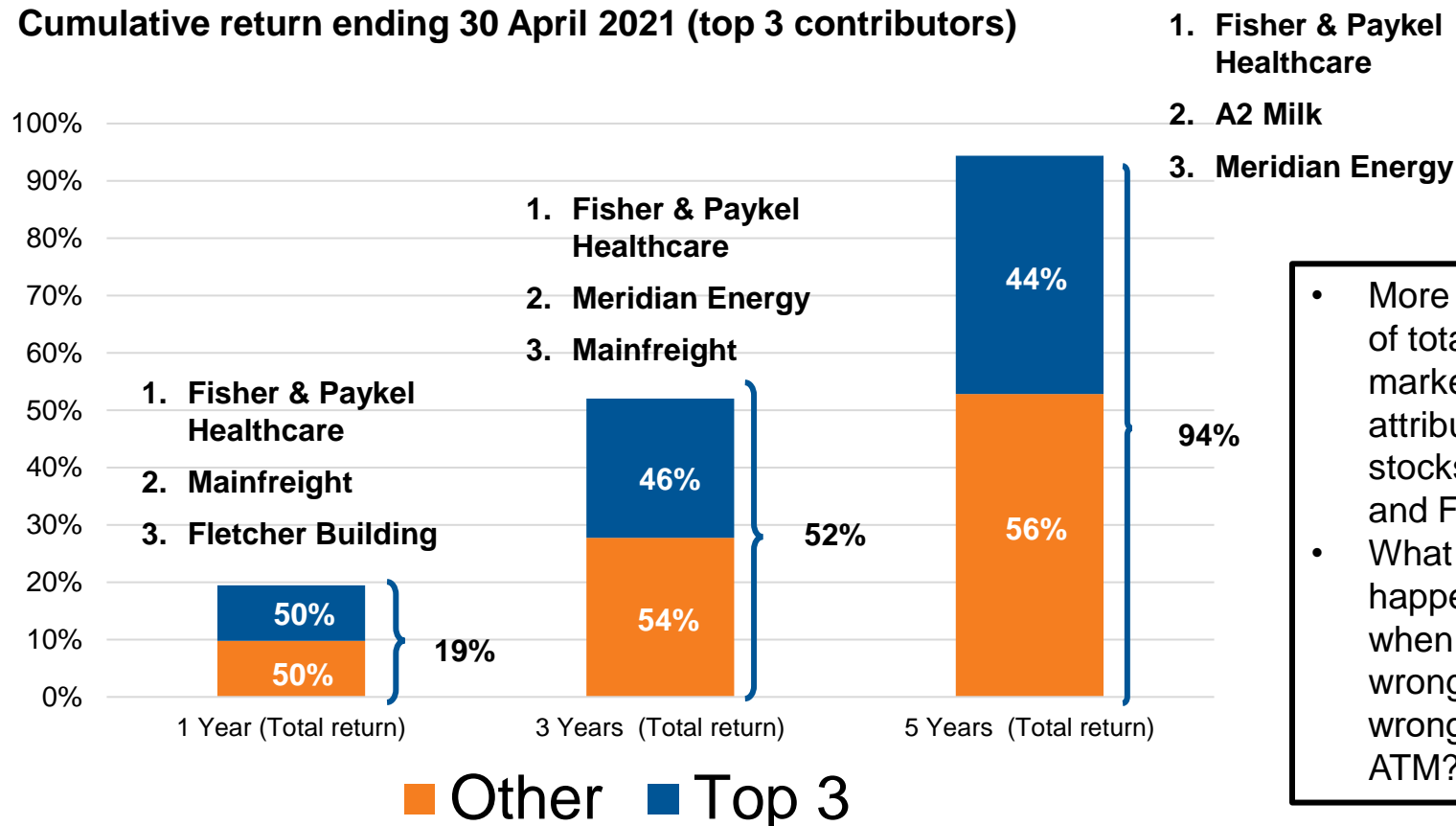
• NZ Shares have been 'lower' risk and generated higher returns

Source: Morningstar Direct. Domestic shares: S&P/NZX 50 index GR including imputation credits. Global shares: MSCI ACWI NR index, MSCI ACWI NR - NZDH index. Global bonds: Bloomberg Barclays global aggregate NZDH index. Domestic bonds: S&P/NZX NZ Composite Invest Grade. Currency: NZD, Data as at 30 April 2021. Past performance is no guarantee of future results.

Performance attribution of the NZX50

FPH and ATM have dominated....

Cumulative return ending 30 April 2021 (top 3 contributors)



1. Fisher & Paykel Healthcare
2. A2 Milk
3. Meridian Energy

1. Fisher & Paykel Healthcare
2. Meridian Energy
3. Mainfreight

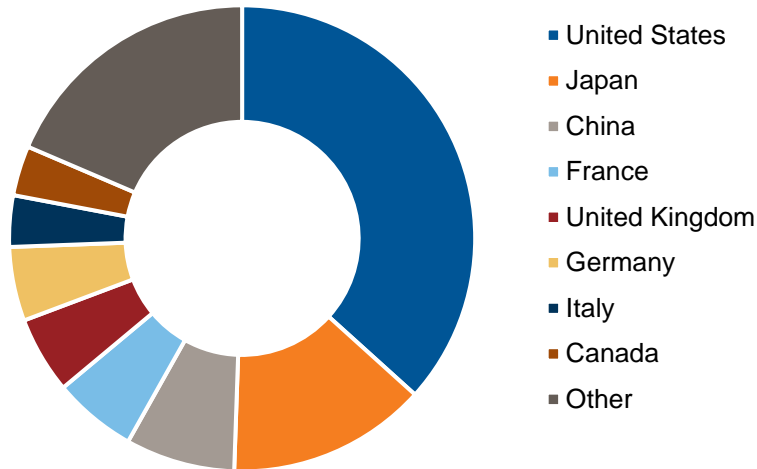
1. Fisher & Paykel Healthcare
2. Mainfreight
3. Fletcher Building

- More than 1/3 of total market return attributed to 2 stocks, ATM and FPH
- What happens when it goes wrong (very wrong... ATM?)

Source: Factset, performance attribution, total cumulative return of S&P/NZX 50 TR with top 3 contributors. Ending 30 April 2021. Some rounding errors, for illustrative purposes only. Past performance is no guarantee of future results.

But, it's a world of opportunities...

Investment grade fixed income

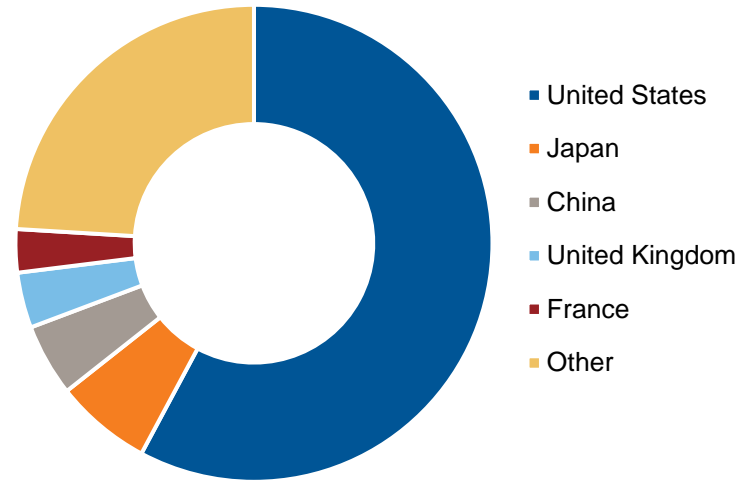


NZ\$ 92 trillion opportunity set

- + Global high yield ~ NZ\$ 4 trillion
- + EMD local currency ~ NZ\$ 4 trillion
- + EMD hard currency ~ NZ\$ 6 trillion

NZ fixed income ~ \$130 billion

Global equities



NZ\$ 89 trillion opportunity set

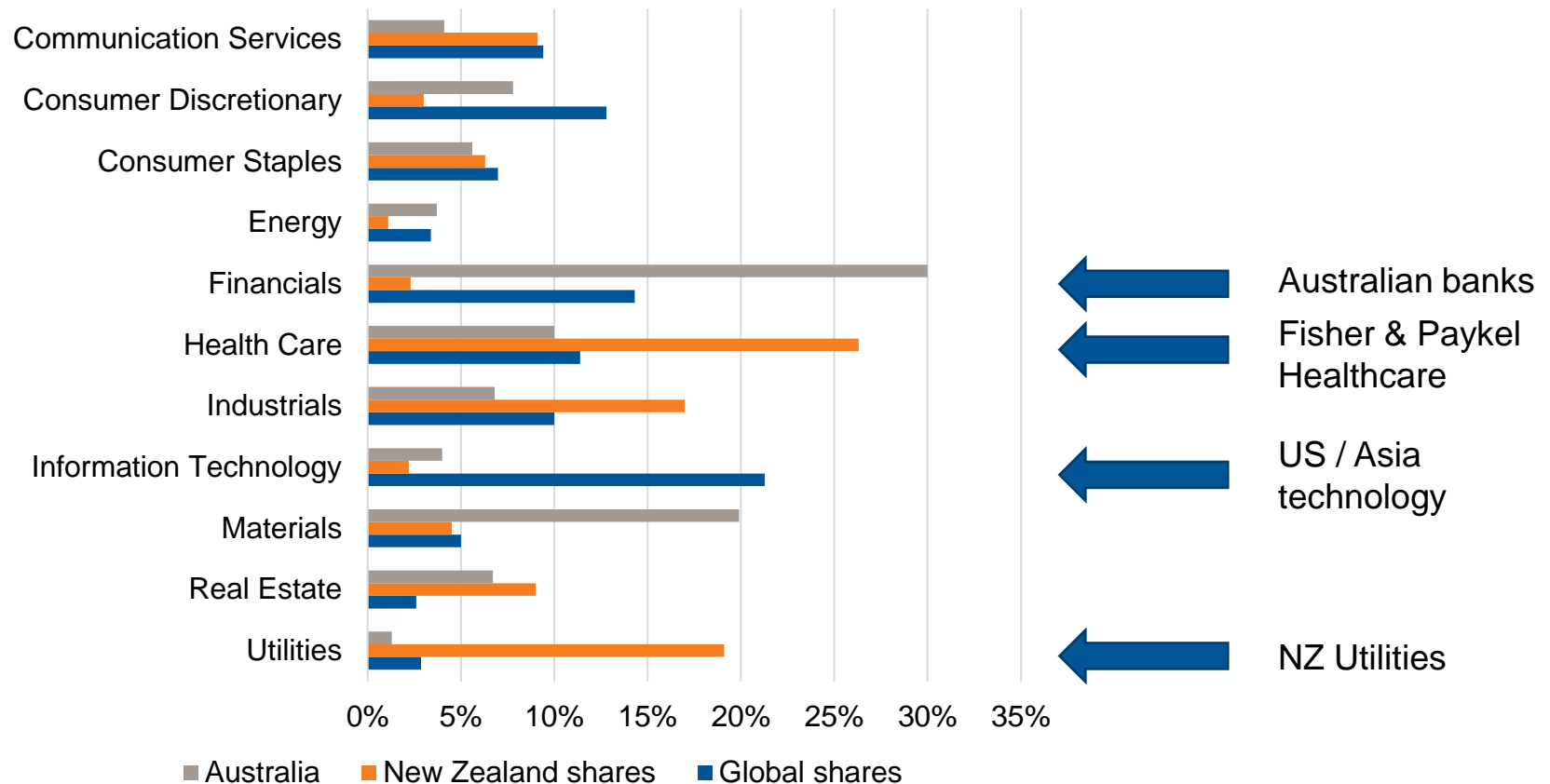
- + Global small caps ~ NZ\$ 12 trillion
- + Frontier markets ~ NZ\$ 110 billion

NZ shares ~ \$165 billion

Source: Fixed income opportunity set represented by Bloomberg Barclays Global Aggregate, Global High Yield, Global EM local and hard currency indices. Global equities represented by MSCI ACWI, MSCI ACWI IMI, MSCI Frontier Markets. NZ assets represented by S&P/NZX 50 and Bloomberg 0+ NZBond Composite. As of 31 March 2021.

Local market sectors vs. international

Sector weights Global, NZ and Australia

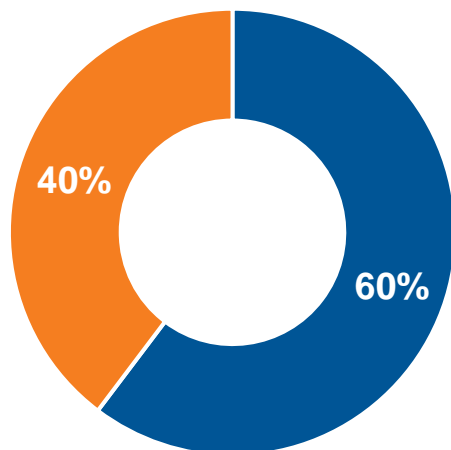


Source: MSCI and S&P. Sector weights as of 31 March 2021 for the MSCI ACWI, S&P/NZX 50 and the S&P/ASX 200.

Local market concentration

S&P/NZX 50

Market cap in top 10 names



- Top 10 market cap
- Other

Top holdings	Market cap (NZD m\$)	Weight	Sector
Fisher & Paykel Health Care	18,215	14.3%	Health Care
Auckland International Airport	9,321	7.3%	Industrials
Spark	8,168	6.4%	Communication Services
Meridian Energy	6,663	5.2%	Utilities
a2 Milk	6,302	4.9%	Consumer Staples
Ryman Healthcare Group	6,251	4.9%	Health Care
Mainfreight Limited	5,780	4.5%	Industrials
Fletcher Building	5,745	4.5%	Materials
Contact Energy	5,280	4.1%	Utilities
Infratil	5,071	4.0%	Utilities

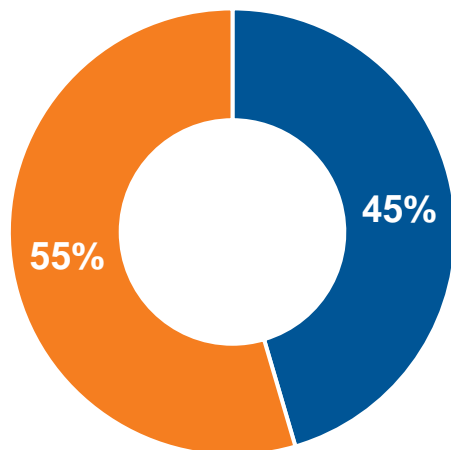
Characteristics	
Number of constituents	50
Total market cap	\$127.4 B.
Largest	\$18.5 B.
Average	\$3.2 B.
Coverage of New Zealand market cap	c. 90%

Source: MSCI, Market capitalisation as of 31 March 2021 for S&P/NZX50

Australia market concentration

S&P/ASX 200

Market cap in top 10 names



- Top 10 market cap
- Other

Top holdings	Market cap (AUD m\$)	Weight	Sector
Commonwealth Bank Australia	152,750	8.0%	Financials
BHP Group	133,447	7.0%	Materials
CSL	120,415	6.3%	Health Care
Westpac Banking Group	89,550	4.7%	Financials
National Australia Bank	85,725	4.5%	Financials
ANZ Banking Group	80,187	4.2%	Financials
Wesfarmers	59,719	3.1%	Consumer Discretionary
Macquarie Group	51,979	2.7%	Financials
Woolworths Group	51,715	2.7%	Consumer Staples
Rio Tinto	41,112	2.2%	Materials

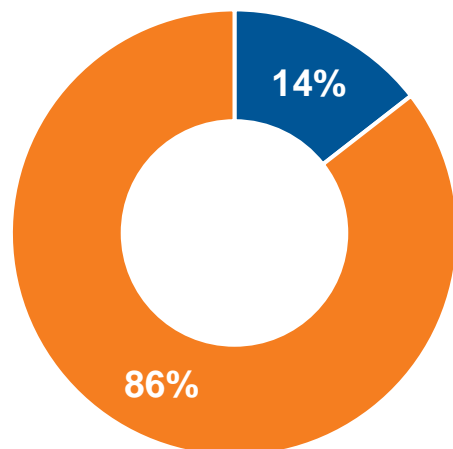
Characteristics	
Number of constituents	200
Total market cap	\$1.9 T.
Largest	152.8 B.
Average	10.3 B.
Coverage of Australian market cap	c. 90%

Source: S&P, Market capitalisation as of 31 March 2021 for S&P/ASX200

Global market concentration

MSCI ACWI

Market cap in top 10 names



- Top 10 market cap
- Other

Top holdings	Market cap (USD b\$)	Weight	Sector
Apple	2,077	3.4%	Information Technology
Microsoft	1,693	2.7%	Information Technology
Amazon.com	1,320	2.1%	Consumer Discretionary
Facebook	708	1.1%	Communication Services
Alphabet A	620	1.0%	Communication Services
Alphabet C	614	1.0%	Communication Services
Taiwan Semiconductor	507	0.8%	Information Technology
Tesla	507	0.8%	Consumer Discretionary
JP Morgan Change & Co.	464	0.8%	Financials
Tencent Holdings	451	0.7%	Communication Services

Characteristics

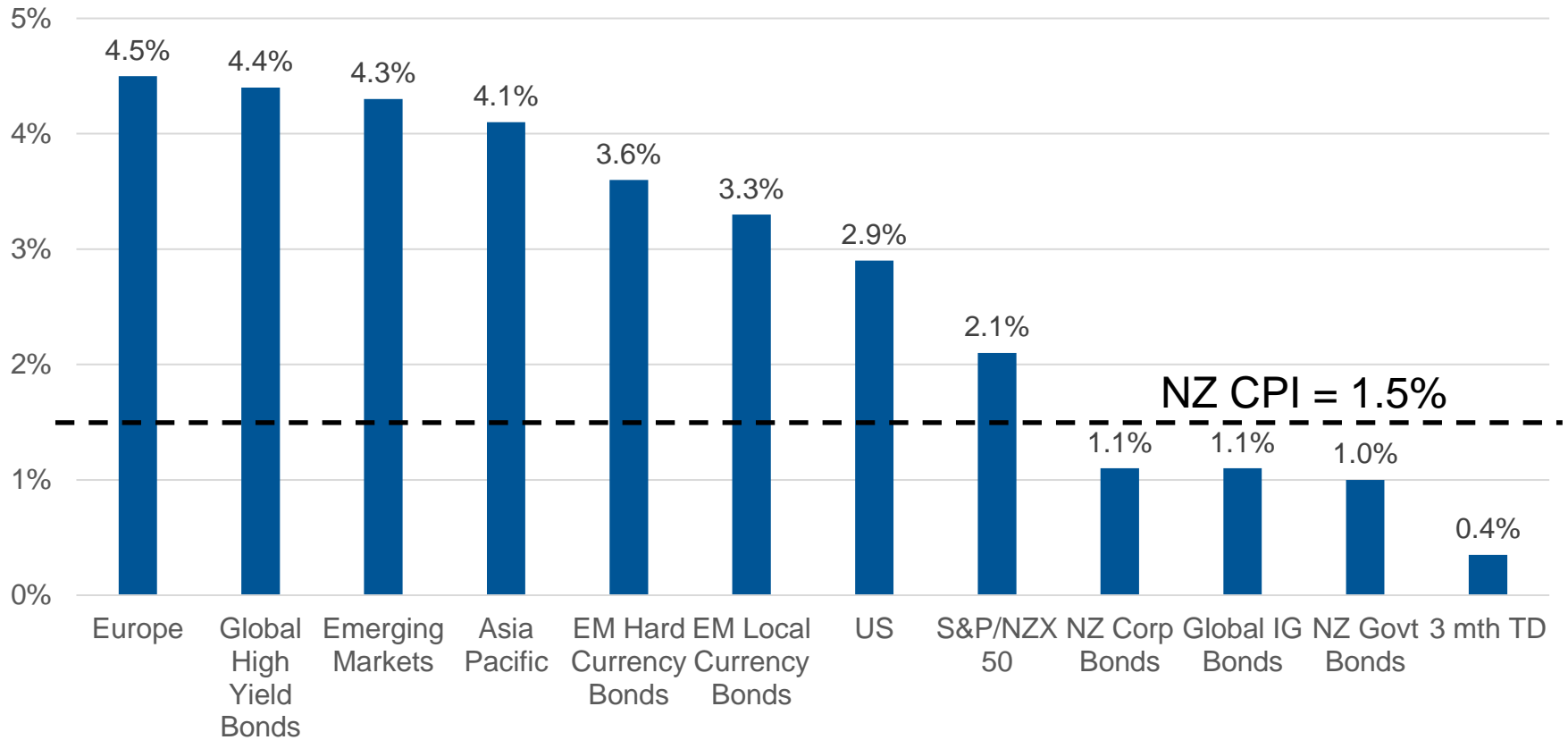
Number of constituents	2,978
Total market cap	\$61.9 T.
Largest	\$2.1 T.
Average	\$20.7 B.
Coverage of global market cap	c. 85%

Source: MSCI, Market capitalisation as of 31 March 2021 for MSCI ACWI (NR)

Income opportunities around the world...

Cash and fixed tends to be local, but better income globally...

(Pre-tax) Dividend yields (global high dividend shares) and yields (fixed income)



Source: MSCI, S&P, Bloomberg, Stats NZ. Dividend yields of MSCI High Dividend indices, Europe, EM, Asia Pacific and US. Yield to worst of Bloomberg Barclays Global High Yield, EM Hard Currency Aggregate and EM Local Currency Government and S&P NZX 50, NZ Government Fixed Interest and NZ Corporate Fixed Interest. 3 month average term deposit rate, BNZ, Westpac, ANZ and ASB. As of 30 Apr 2021.

Increase in international exposure?

Diversification benefits...

Correlation matrix

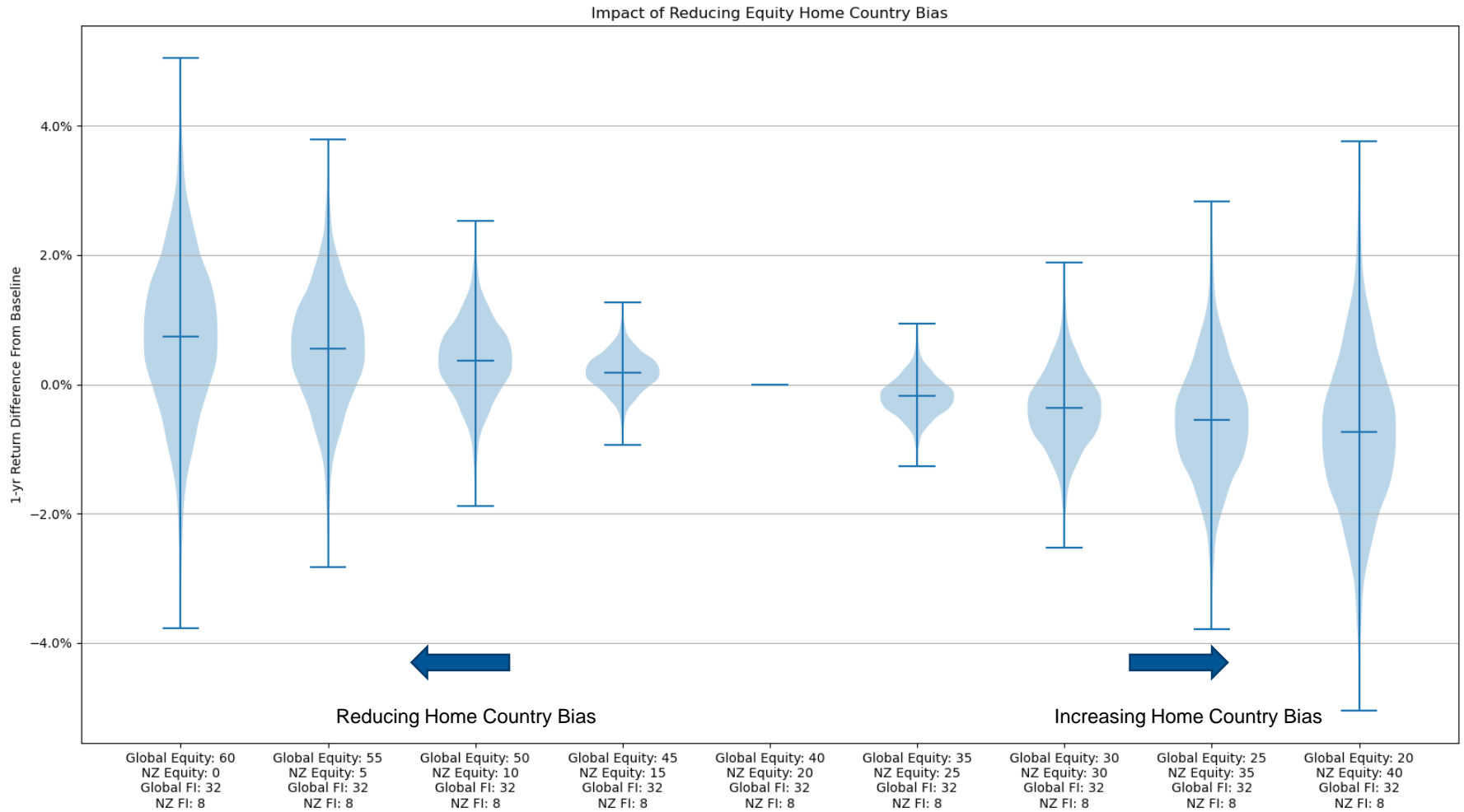
	1	2	3	4	5	6	7	8	9	10	11
1 - Global bonds	1.0										
2 - NZ fixed Interest	0.6	1.0									
3 - Global shares	-0.1	0.0	1.0								
4 - Global shares – NZDH	0.0	-0.3	0.6	1.0							
5 - Emerging markets	0.0	-0.1	0.7	0.6	1.0						
6 - NZ shares	0.1	0.0	0.5	0.7	0.5	1.0					
7 - Australian shares	0.1	-0.1	0.7	0.7	0.8	0.7	1.0				
8 - Global real estate securities	0.3	0.0	0.4	0.8	0.5	0.6	0.7	1.0			
9 - Global infrastructure	0.2	-0.1	0.5	0.8	0.6	0.7	0.7	0.9	1.0		
10 – Commodities	-0.2	0.0	0.4	0.1	0.4	0.0	0.4	0.0	0.1	1.0	
11 – Gold	0.2	0.5	0.1	-0.4	0.1	-0.2	0.0	-0.4	-0.3	0.4	1.0

Source: MorningStar direct. Domestic shares: S&P/NZX 50 index GR including imputation credits. Global shares: MSCI ACWI NR index, MSCI ACWI NR - NZDH index. Global bonds: Bloomberg Barclays Global Aggregate NZDH index. Domestic bonds: S&P/NZX NZ Composite Invest Grade. Emerging markets: MSCI EM NR. Australian shares: S&P/ASX200. Global real estate: EPRA FTSE EPRA NAREIT Developed NR NZDH. Global Infrastructure: S&P Global Infrastructure NZDH. Commodities: Bloomberg Commodity PR. Gold: LBMA Gold Price PM. April 2005 – March 2021 in NZD.

Is Peer Risk relevant?

- > Extent of home bias is v. important issue for many investors (opportunity set, risk-return, risk factors, income generation etc.)
- > Those in the business of comparing their returns to others (which, let's face it, is almost everyone), then 'peer relativity' becomes an issue...
- > What is peer relativity?
 - i. My KiwiSaver did better than yours
 - ii. Wealth manager A is 'better' than wealth manager B
 - iii. Superannuation scheme of company X beat scheme of company Y
 - iv. Press article calling out one investor relative to another
- > Should investors think about how others invest when they build their asset allocations? Does it really matter how others are doing?

Impact of Changing Home Country Bias

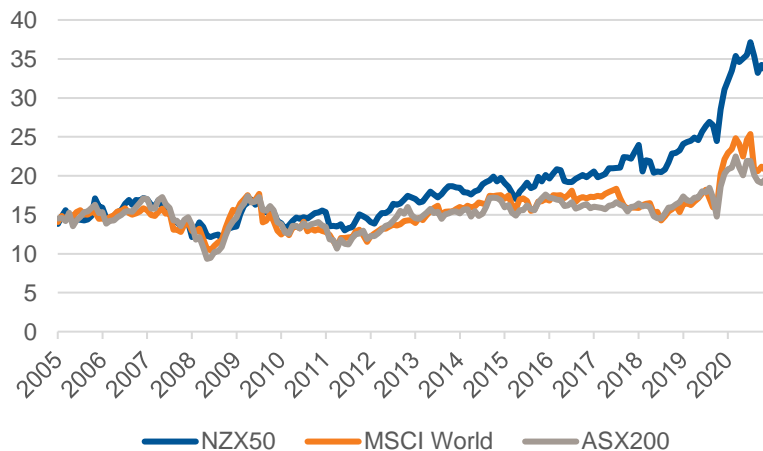


Source: Russell Investments. Impact of changing allocation to NZ equities based on Russell Investments Conditional Markets Forecasts. For illustrative purposes only.

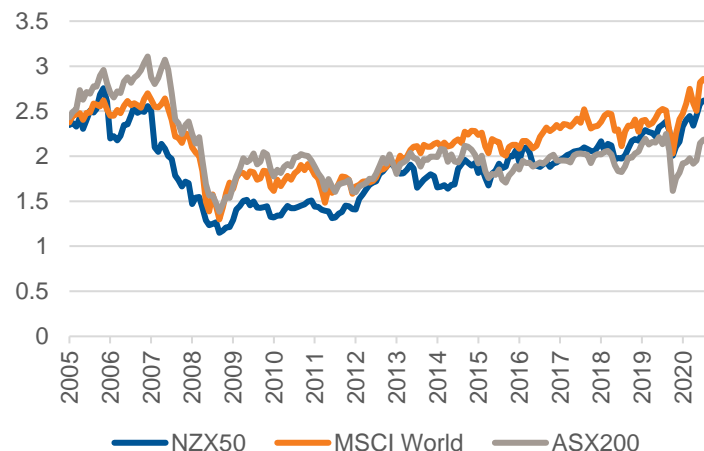
Increase in international equity exposure?

Valuation characteristics...

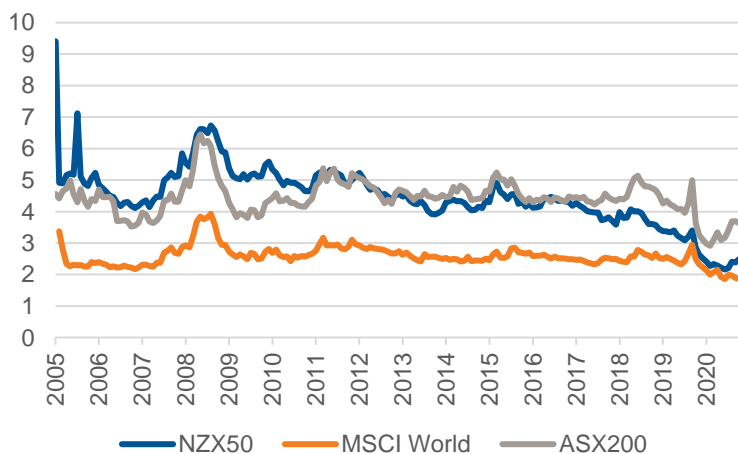
Forward P/E (x)



P/B (x)



Dividend Yield (%)

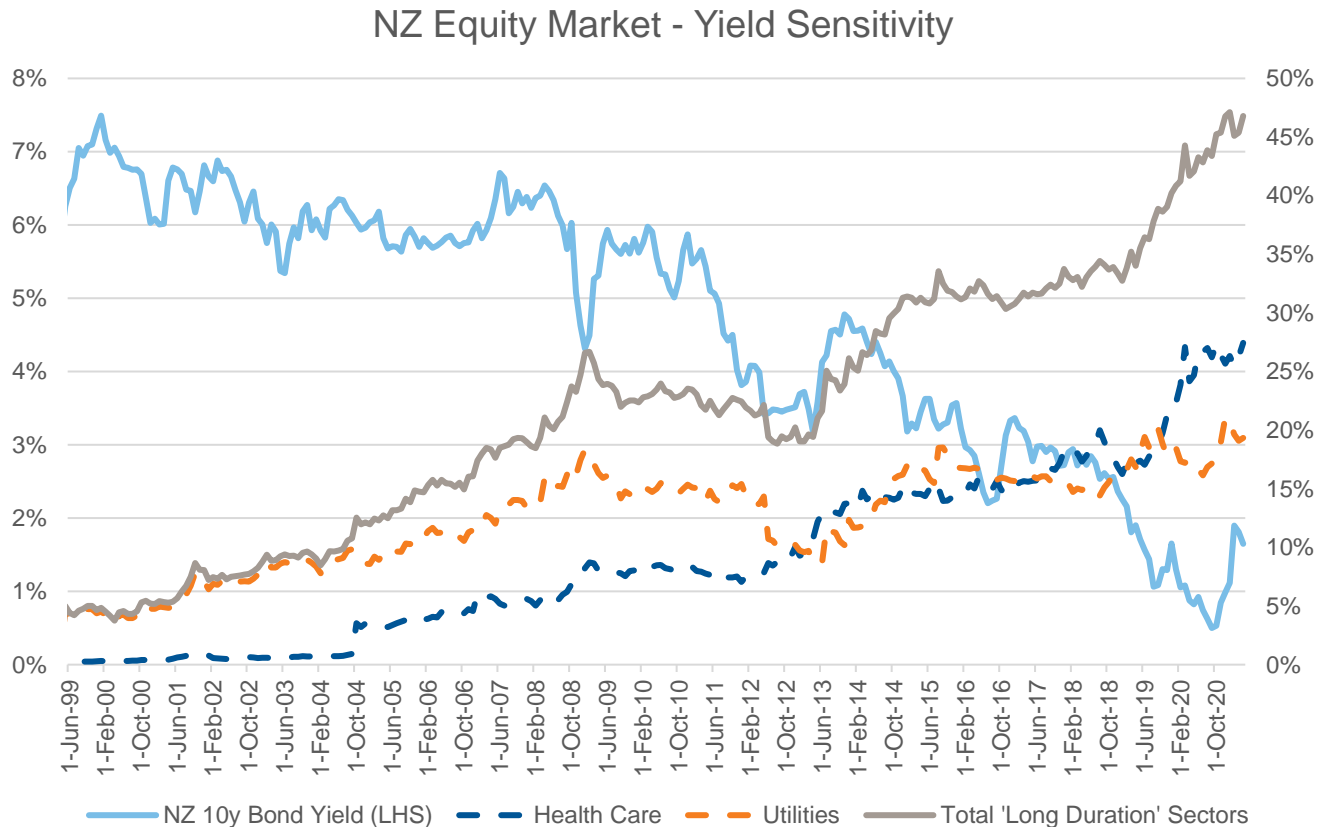


- > NZ has historically traded at a discount to both global and Australia
- > Currently 'expensive', particularly given the market profile (i.e. defensive, yield-oriented names)

Source: Bloomberg, Forward price-to-earnings ratio, forward dividend yield and price-to-book ratio. From 2005 -2021

Massive decline in yields... ... has been strong tailwind for rate sensitive stocks

NZ Health Care and Utilities – Yield sensitive sectors make up half of the market

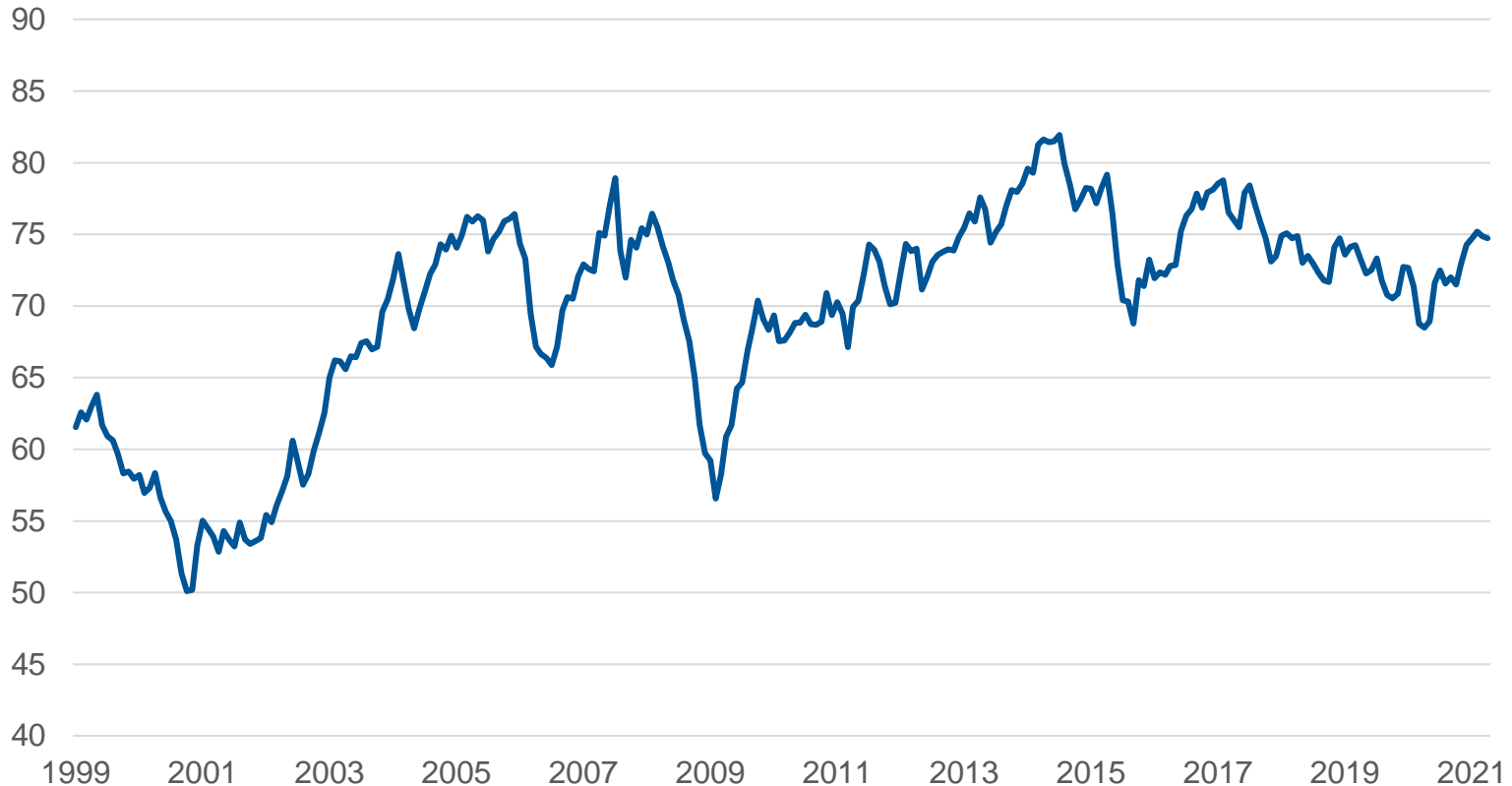


Source: Bloomberg, NZ 10 Yr government bond yield, Health Care and Utilities weights in NZ share market. 1999 – 2021. Past performance is no guarantee of future results.

The flying Kiwi?!?!?

Need to consider FX when considering international...

NZD Nominal Trade Weighted Index 1999 - 2021



Source: Reserve Bank of New Zealand, 1999-2021. Past performance is no guarantee of future results.

Is it time to ditch the home country bias?

- > There is rationale for 'some' home bias in fixed interest and equities (in particular), however many local investors have too much risk in NZ...
- > **But**.....It's a big world of investment opportunities...
- > Concentrated NZ market is not (at all) representative of the global economy today...
- > Expensive relative to history (as is everything) but also relative to global markets
- > Highly exposed to the results of a handful of companies, great if everything is working, v. difficult if not...
- > Limited fixed interest market – income-oriented investors have many global choices

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