

Quarterly update for month ending December 2023

Investment objective

To outperform the benchmark over the medium to longer term.

Key information

Code	NTH1072
Manager name	Mercer
Inception date	30 November 2020
Benchmark	Morningstar Australia Balanced Target Allocation NR
Asset class	Diversified
Number of underlying assets	19
Minimum investment horizon	4 years
Portfolio income	Paid to Cash Account
Management fees and costs	0.63%
Performance fee	0.02%
Estimated net transaction costs	0.04%
Estimated buy/sell spread	0.17%/0.17%
Risk band/label	4/Medium
Minimum investment amount	\$500

About the manager

Mercer

Mercer is a multi-national investment manager, using specialised investment tools and strategies to provide robust and diversified portfolios for their clients. The team manages approximately \$200 billion worldwide, with approximately \$33 billion invested in Australia and New Zealand. With Australian operations commencing in 1972, Mercer's primary driver in portfolio construction is risk management - spreading investments across investment types and different risks to mitigate periods of market volatility and protecting investments from loss. Using a multi-dimensional framework, Mercer uses active management in asset classes offering the greatest opportunity for skilled investment managers to add value while using passive management to manage risk or constructing a portfolio to deliver close to market returns.

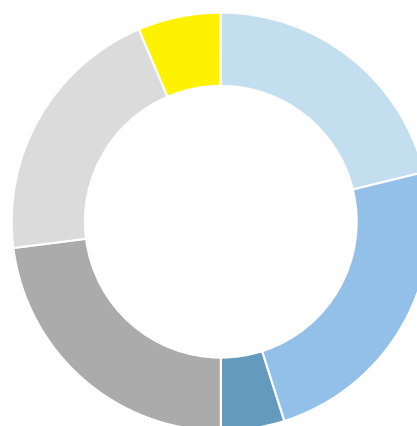
Returns

as at 31 December 2023

	Since inception*	1 Month (%)	3 Months (%)	6 Months (%)	1 Year (%)	3 Years (%)	5 Years (%)
Total return ¹	2.94	3.64	5.56	4.39	9.55	2.81	-
Income	3.59	0.11	0.40	1.78	2.92	3.48	-
Growth	-0.65	3.53	5.16	2.61	6.63	-0.67	-
Benchmark ²	3.61	3.66	5.78	4.79	10.46	3.64	-

* Since inception returns begin from the month end immediately following portfolio launch.

Asset allocation



as at 31 December 2023

Growth assets		Allocation (%)
	Australian Equities	21.2
	International Equities	23.9
	Property	4.9
	Other	0.0
Total		50.0%
Defensive assets		Allocation (%)
	Australian Fixed Interest	23.0
	International Fixed Interest	20.6
	Cash	6.4
Total		50.0%

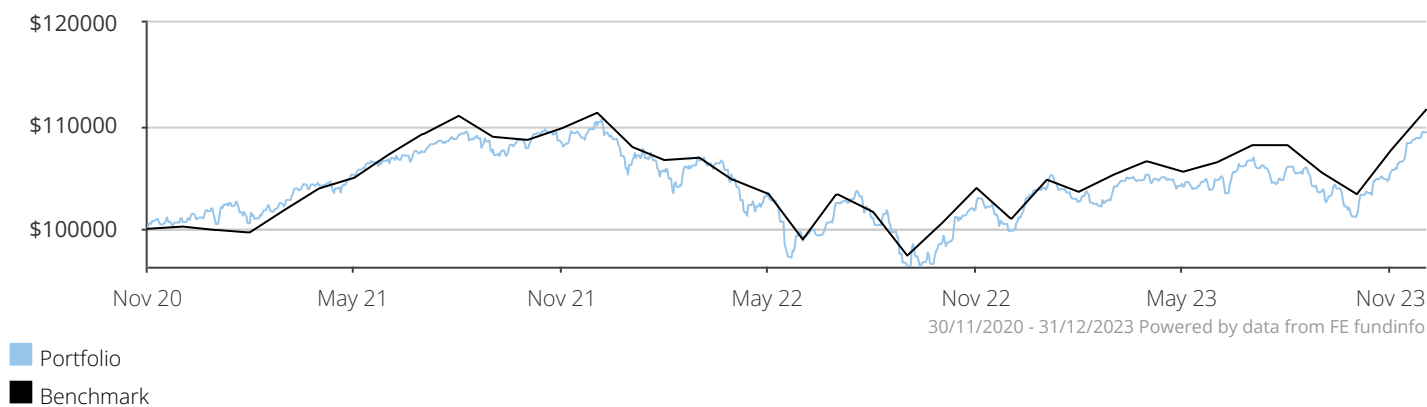
Asset allocation data sourced via Morningstar® from the underlying fund manager.

¹ The managed portfolio performance represents total return for the periods. Returns have been calculated using the time-weighted method, they assume distributions are reinvested and are after investment management fees and indirect costs. Total and growth returns include accrued distributions, while income return includes paid distributions only. Returns do not take into account tax payable. Individual client returns may vary based on the contributions, withdrawals, and timing differences within the managed portfolio

² The applicable Benchmark for this portfolio is shown in the Key Information section.

Performance history

\$100,000 invested since 30/11/2020



Managed portfolio holdings³

Holding	Asset class	Allocation (%)
Macquarie True Index Australian Fixed Interest	Australian Fixed Interest	14.8
T. Rowe Price Dynamic Global Bond	International Fixed Interest	8.0
Macquarie Income Opportunities No. 1 Fund - Class W	Australian Fixed Interest	7.7
AB Concentrated Australian Equities Fund	Australian Equities	6.9
Vanguard International Shares Index Fund (Hedged)	International Equities	6.8
PIMCO Global Credit Fund - Wholesale Class	International Fixed Interest	6.7
Pendal Focus Australian Equities Fund	Australian Equities	5.2
Solaris Core Australian Equity Fund (Performance Alignment)	Australian Equities	5.1
Resolution Capital Global Property Securities Fund - Class C	Property	5.0
Lazard Global Infrastructure Fund (Hedged) - S Class	International Equities	4.9
Bentham Professional Global Income Fund - Class C	International Fixed Interest	4.9
Pzena Global Focused Value Fund - P Class	International Equities	4.8
IFP Global Franchise Fund (Wholesale)	International Equities	4.0
Hyperion Australian Growth Companies Fund	Australian Equities	4.0
Coolabah Floating-Rate High Yield Fund - Institutional Class	Australian Fixed Interest	3.1
Colchester Global Government Bond Fund - Class R	International Fixed Interest	2.7
T.Rowe Price Global Equity - M Class (Hedged)	International Equities	2.7
T.Rowe Price Global Equity - M Class	International Equities	1.6
Cash Account	Cash	1.2

Quarterly manager commentary

Market Update

Global equities rose in most regions in the fourth quarter of 2023, primarily driven by a decrease in bond yields. A combination of marginally softer than expected inflationary data across the globe and comments from US Federal Reserve Bank (Fed) Chair Jerome Powell, noting that interest rate cuts in 2024 are now being pencilled in, were the key drivers. Australian shares also followed this trend, rising 8.4% over 4Q23. The lift in risk appetite and lower bond yields led to a strong performance in the Materials, Real Estate, and Healthcare sectors.

Government bond yields ended the December quarter lower on the back of these dovish signals from the Fed, as well as the US Treasury announcing a lower-than-expected increase in the issuance of longer-dated bonds. The US 10-year government bond yield declined by a substantial 71bps to 3.87% p.a. over the period. Similarly, the Australian 10-year yield decreased by 59bps to 3.90% p.a., as local investors began to anticipate RBA interest rate cuts in 2024. Weaker 3Q23 GDP data and a moderation in business confidence also contributed. The Australian dollar (AUD) appreciated against the weakening US dollar (USD), with the Fed's rhetoric shifting expectations across currency markets.

Commodity markets showed a mixed performance over the final quarter for 2023. Oil prices remained on a downward trajectory, dropping 18.6% to a six-month low of US\$77.69/barrel at end-December. A performance attributed to weakening global demand and strength in non-OPEC oil supply. On the flipside, Industrial Metals prices were stronger over the quarter. Iron Ore gained 19.2%, driven by positive sentiment towards the recent developments in the Chinese economy. Similarly, copper prices rose 3.8% during the quarter, fuelled by optimism for further Chinese stimulus and signs of improvement in manufacturing activities in the country. The precious metals sector saw gold prices rise 11.2% to US \$2,065.45/oz, a return aligned to USD weakness and growing anticipation of interest rate cuts in 2024.

Portfolio update

The portfolio delivered a return of 5.56% for the December quarter compared to its benchmark return of 5.78%.

Australian shares delivered a strong performance over the December quarter, with the S&P/ASX 300 Accumulation Index returning 8.4%. This performance can be attributed to market expectations adjusting to reflect the potential for lower interest rates in 2024 and a soft landing for the US economy. These shifting market dynamics were also beneficial for small-cap stocks, with the ASX Small Ordinaries index gaining 8.5% over the period. The Australian REITs sector was the best performing, returning 16.5% for the period, followed by Healthcare (13.3%) and Materials (13.2%).

The Hyperion Australian Growth Companies fund returned 16% over the quarter. Block Inc., REA Group Ltd., and James Hardie Industries were primary drivers of relative performance. The strategy offers investors exposure to quality Australian companies with a focus on those that have the ability to grow earnings over time. The AB Concentrated Australian Equities fund returned 4.3% over the quarter, underperforming the broader ASX benchmark. Underweight sector positions in Real Estate and Healthcare drove underperformance. The strategy is an actively managed, high-conviction equity portfolio of 20 stocks that seeks to generate outperformance through superior stock selection driven by the firm's proprietary fundamental research.

Global equities performed strongly over this last quarter for 2023. The MSCI World ex-Australia Index returned 9.2% in hedged terms and 5.3% in unhedged AUD terms. Positive market sentiment was boosted by the rapid repricing of US interest rate cuts combined with softer inflation data from around the world. Real Estate (10.6%) and Industrials (7.7%) sectors had positive returns over the December quarter, with Information Technology (11.2%) stocks continuing to lead the way as investor appetite for interest rate-sensitive assets increased on the back of declining bond yields. Emerging markets underperformed relative to developed markets, returning 2.0% for the period with China continuing to drag on performance. Mixed economic data from the region undermined investor confidence around a potential economic recovery as the impact from stimulus measures remained subdued.

The T. Rowe Price Global Equity Fund delivered 3.0% over the quarter. Its overweight allocation to both emerging and private markets negatively impacted performance. This strategy applies a truly global, high-conviction, core approach and focusses on companies with durable competitive advantages. The Pzena Global Focused Value fund returned 3.3% over the quarter. The strategy outperformed the MSCI ACW Value Index, however, trailed the broader market as the value style underperformed generally. As a deep value manager, Pzena invests in stocks on low valuation multiples, believing this 'cheap' section of the market offers the most attractive opportunities for long-term return generation.

Listed infrastructure outperformed broader equity markets over the quarter, with AUD-hedged FTSE Developed Core Infrastructure index returning 11.1% driven by falling bond yields and a depreciating US dollar. Domestic listed property (S&P/ASX 300 A-REIT Accumulation Index) delivered a 16.5% uplift over the December quarter, while Global REITs (FTSE EPRA/NAREIT Developed, in AUD hedged terms) rose by 13.0%. Positive returns for both indices were primarily driven by growing expectations of softer monetary policy settings and interest rate cuts in 2024. These factors are seen as beneficial for real estate property valuations and underlying earnings.

The Lazard Global Listed Infrastructure fund outperformed its benchmark over the quarter, returning 10.8%. Exposures to Railroads and Transport contributing positively to performance, whilst Satellite exposure detracted. The strategy offers investors diversification benefits to a portfolio, particularly during times of high inflation. The Resolution Capital Global Property Securities fund marginally underperformed its benchmark, returning 12.9%. An underweight position and stock selection in the Self-Storage, Diversified, Hotel and Office segments, and stock selection in both the Data Centres / Towers and Industrial segments contributed to relative performance over the quarter. The strategy offers Global Listed Property exposure with broad sector holdings and many inflation-linked cash flows, as well as diversification to equity investments and investments driven by Australian economic activity.

Global sovereign bond performance was mostly positive over the December quarter. After a rough start, where the US 10-year bond yields peaked at ~5.0% mark in October, yields declined sharply from early November. A combination of softer inflation and economic data fed through to a distinct change in tone from the US Fed, leading to a downswing in market expectations for interest rate cuts in the upcoming year.

Credit spreads widened in early October due to risk-off sentiment on the back of elevated government bond yields and global uncertainty in the context of an emerging Middle East conflict. However, spreads tightened later in the quarter, as market participants shifted expectations towards a soft-landing scenario for the US economy. Higher demand and lower levels of issuance for higher yielding investment-grade bonds was also supportive.

Domestically, bond yields across maturities declined in line with the global bond markets. Consequently, the Bloomberg Ausbond Treasury Index gained 4.0%. The domestic credit market, as tracked by the Bloomberg Ausbond Credit Index, also experienced gains with a rise of 3.2% over the quarter.

The PIMCO Global Credit fund returned 6.1%, outperforming its benchmark. The strategy offers investors high-yield global corporate bond exposures, which diversifies the growth asset and core fixed interest positions in the portfolio. As such, the fund's overweight to Australian duration and exposure to Agency MBS contributed positively to performance, as rates rallied over the period. The T. Rowe Price Global Dynamic Bond fund returned -0.4% over the quarter with its duration management a key detractor to performance, as the sharp rally in risk and duration over November and December offset gains posted in October.

Portfolio changes during the quarter:

Over the quarter, Mercer introduced the Coolabah Floating-Rate High Yield fund to improve the breadth of the portfolio's Fixed Income manager suite.

The strategy focusses on generating higher income than other traditional fixed income investments by investing in a portfolio of investment-grade Australian floating rate notes (FRNs) issued by Australian banks and insurance companies with enhanced yields.

Furthermore, the allocation to Resolution Capital Global Securities (Hedged) has increased by reducing hedged global equity positions within the T. Rowe Price fund. Valuations within Global REITs are trading at a significant discount to private real estate and the broader equity market, while earnings are less exposed to a slowdown in the global growth environment.

In line with Mercer's Dynamic Asset Allocation views, the nominal duration position of the portfolio was increased by lifting allocations to the T. Rowe Price Dynamic Global Bond fund and Colchester Global Government Bond fund. This was funded from Cash and exiting the Pandal Short Term Income Securities fund.

Market Outlook

Australian economic growth has proven resilient in recent quarters with several supporting factors. Households spending excess savings, population growth via immigration, a significant proportion of mortgages on (low) fixed rates and government expenditure have all been complementary. However, we expect growth to moderate as these stimuli diminish and the impact of higher interest rates flows through. Further, whilst inflation is expected to ease, the pace of decline is unlikely to be at the rate in other developed economies due to residential rental market pressures. We note that risks point towards a sharper slowdown in economic activity compared to expectations. Therefore, market pricing for two interest rate cuts in 2024 may prove to be fewer, and potentially slower, than what will ultimately occur.

Globally, we anticipate resilient growth, although it may vary across regions. Developed economies are expected to experience a moderation in economic performance due to tighter financial conditions. On the other hand, China is expected to see stronger growth driven by supportive fiscal, monetary and regulatory policies, as well as a turnaround in the manufacturing inventory cycle and a potential stabilisation in the housing sector. Other emerging economies are also expected to benefit from the current easing cycle in their central bank monetary policy settings.

In terms of asset class perspectives, we maintain a cautious view on developed markets due to high valuations and an optimistic earnings outlook. We hold a favourable view on emerging markets, which offer attractive valuations and more promising economic prospects. Domestically, considering the relative risks associated with interest rate expectations, we find Australian sovereign bonds attractive, despite the persisting risks posed by volatility in global sovereign bond markets.

3 A significant percentage of assets comprising this portfolio are only available through the managed portfolios and therefore can't be transferred out of the MyNorth Managed Portfolio Scheme. For more information relating to restrictions that may apply to asset transfers, refer to the 'Transferring assets in and out of your Portfolio' in Part 1 of the MyNorth Managed Portfolios PDS.

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