GSS Index Managed Models – Annual Asset Allocation Review & Re-weight February 2020

Adviser Use Only

The GSS Index Models use a strategic asset allocation to determine the percentage weights to each underlying asset class. Strategic asset allocation ('SAA') takes a are long term view to determine appropriate weights to each asset class and typically are stable through the economic cycle. The key input to determining the SAA are the capital market assumptions ('CMA's'). CMA's include forward looking assumptions on economic growth, inflation and interest rates, currencies and asset class valuations.

Once per year, the CMA's are reviewed and the new assumptions are then used to re-calculate the strategic asset allocation for the models. Post the review, the Models asset allocation is re-balanced to the new strategic asset allocation.

The CMA's 2020 review concluded with no change to the CMA assumptions. As a result, there has been no change to the GSS Index Models long-term strategic asset allocation (SAA) since the last review in January 2019.

The models were re-balanced back to the strategic asset allocation detailed below with an effective trade date of 7th February 2020.

Asset class	GSS Conservative Index Model	GSS Balanced Index Model	GSS Growth Index Model	GSS High Growth Index Model	GSS Total Growth Index Model
Australian equities	17	27.9	39.1	47.5	54.6
International equities	14.5	23.1	31.4	37.7	43.4
Australian fixed interest	27	19	11	5	0
International fixed interest	39.5	28	16.5	7.8	0
Cash	2	2	2	2	2
TOTAL	100	100	100	100	100

SAA Review

- There have been no sizeable shifts in the capital markets assumptions. Blackrock maintains the view that global GDP growth will edge higher in 2020 due to expansionary financial conditions which also aide to limit recession risks. Growth is expected to shift as manufacturing recovers from coronavirus disruptions. Interest rate-sensitive sectors such as housing are also expected to improve. The expected improvement in growth is expected to be delayed in the first half of 2020 due to the impact of coronavirus. As a direct result, a moderate, pro-risk stance is maintained by retaining the existing allocation to global equities. With central banks monetary policy easing and the expansion in equities valuation multiples largely behind us, we expect an improvement in economic growth to support growth assets. Valuations still look reasonable.

- Blackrock believe economic fundamentals will drive markets in 2020, with less risk from reduced trade tensions. In addition, BlackRock also believe there is less scope for further monetary easing surprises or fiscal stimulus packages. Major central banks appear intent on maintaining pro-growth monetary policies and hence current interest rates and bond yields look likely to remain low. Blackrock are overall neutral on global interest rates. Major central banks are likely to keep monetary policy on hold in the near term, even as economic growth and inflation improve. This tilts risks toward a steepening of the yield curve. Yields remain low in many developed markets, making many government bonds less effective portfolio ballasts in case of equity market selloffs.

- The cash position has been maintained at neutral for risk mitigation. We also see cash as a robust buffer against risks around regime shifts, especially those triggered by a negative supply shock that could drive both stocks and bonds lower together.

GSS Index Models Performance Review

- Global equities rebounded in 2019 as measured by MSCI World ex Australia index. The Netwealth Unhedged International Equities Index Fund returned 27.9% for twelve months to December 2019. Improved global GDP (albeit slowing), expansionary monetary policy by central bankers, and developments in US-China trade negotiations were key drivers of equities return for the year. US, Europe, and China all improved their GDP over the year.

- Global fixed income indices recorded strong positive returns over 2019 with the Bloomberg Barclays Global Aggregate Hedged AUD index returning 7.19% whilst the Bloomberg AusBond Composite 0+Yr Index returned 7.26%. The US Federal Reserve maintained the dovish stance and there is potential for an interest cut in the near future by the US Federal Reserve that would support bonds valuation. Domestically, the RBA delivered 25 bps rate cut in early June, after keeping the Cash Rate stable for nearly three years and this was followed by another rate cut in July and October bringing the cash rate down to a historic low of 0.75%.

- Over 2019, the GSS Index Models returned 12.1%, 15.6%, 19.2%, 21.9%, and 24.5% for the Conservative, Balanced, Growth, High Growth, and Total Growth options respectively. This is compared to their respective passive benchmark return of 10.8%, 15.5%, 19.1%, 23.2%, and 23.2% for the same period.

- Relative performance against the respective active peer group was also strong with all options outperforming their peer group return (Morningstar Multisector Peer Group).

- Key drivers of returns over the period was the exposure to growth assets as equities in general performed strongly.

- The defensive asset classes (domestic and global fixed interest) also performed strongly posting positive returns for the year on the back of a rally in bond yields in both domestic and global fixed interest.

- As the underlying funds employed in the models are passive index tracking strategies, the performance has mirrored the index being replicated.

- The underlying passive strategies assisted the relative performance of the models as passive outperformed most active strategies over the last 18 months. This is largely due to many active managers moving to a more defensive portfolio positioning whilst the positive momentum of the broader market continued.

- The strategic asset allocation provided by BlackRock in January 2019 was a key driver of returns in 2019 The attribution analysis the asset allocation was positive:
  - The increased asset allocation weight to domestic equities and fixed income asset classes contributed positively.
  - The reduced allocation to listed property slightly detracted from relative returns as the listed property asset class performed strongly. Listed property benefited from a reduction in yields as the asset class is seen as a proxy to duration. The models exposure to listed property is through the broader Australian equity allocation albeit at market weight.
  - The reduced allocation to hedged international equities also added value as the AUD depreciated against major currencies over the period further assisting relative performance of the models.