BT Index Defensive Fund

Monthly report – 30 September 2022

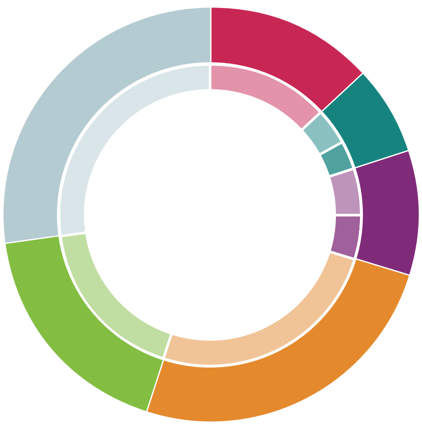
Fund overview

Inception date	1 August 2016
APIR code	WFS0588AU
Fund size (AUD millions)	$232.68
Investment objective	To provide investors with predominantly income and some growth returns, with a low probability of loss over the short term which tracks the overall return of a diversified portfolio of underlying investments.
Recommended investment timeframe	3 years
Minimum initial investment	$500,000
Distribution frequency	Quarterly
Management costs (%) pa[1]	0.34
Buy/sell spread (%)	0.06 / 0.06

Performance review[2]

Period ending 30 September 2022	1 month	3 months	1 year	3 years	5 years	Since inception
	%	%	%	% pa	% pa	% pa
Total return	(3.43)	(1.65)	(9.01)	(0.88)	2.17	2.12
Growth return	(3.67)	(1.89)	(12.11)	(4.27)	(1.25)	(1.27)
Distribution return	0.24	0.24	3.10	3.39	3.42	3.39

Actual asset allocation %[3]



Equity – Australian Listed – 12.78%
- BT Australian Shares Index Fund – 12.78%

Equity – International Listed – 6.99%
- BT International Shares Index Fund (Unhedged) – 3.98%
- Blackrock Index Hedged International Equity Fund – 3.01%

Property – International and Australian Listed – 9.92%
- BT Property Securities Index Fund – 4.96%
- Blackrock iShares Global Listed Property Index Fund – 4.96%

Fixed Income – Australian – 25.14%
- BT Australian Fixed Interest Index Fund – 25.14%

Fixed Income – International – 17.95%
- BT International Fixed Interest Index Fund – 17.95%

Cash – 27.22%
- Advance Cash Multi-Blend Fund – 27.22%

Please refer to the end of this report for the footnotes

Market update

Markets continued to fall over September as rate rises were delivered over the month. The expectations of rate hikes in the near future also sparked the acceptance that a global recession has a high probability of occurring, as the fight to temper inflation continues. With the UK in a state of economic flux, and no end in sight with the war in the Ukraine, there remains a deep uncertainty as to what lies ahead.

Australia

In early September the Federal Government's Jobs and Skills Summit took place, which included two days of speeches and discussions with industry, government, unions, and business leaders.

The Government announced 36 outcomes and initiatives that would be implemented following the Summit. These are grouped into five key themes and categories:

- A better skilled, better trained workforce.
- Addressing skills shortages and strengthening the migration system.
- Boosting job security and wages, and creating safe, fair and productive workplaces.
- Promoting equal opportunities and reducing barries to employment.
- Maximising jobs and opportunities in our industries and communities.

One of the main policies coming out of the summit included changes to the migration program to accelerate and increase the number of people coming to Australia to help employers fill the record number of job vacancies across the economy.

For permanent migrants, the annual intake will be increased to 195,000 in 2022-23, up from 160,000 prior to the pandemic. Additional funding will be provided to speed up visa processing to streamline the visa application process and clear backlogs. Students and holders of training visas will also be allowed to stay in Australia longer, with work rights, following the completion of their studies.

On industrial relations, changes will be introduced to the Fair Work Act and rules around workplace bargaining, including the development of legislation to introduce a multi-employer wage bargaining system. This has been a contentious issue as some employer groups have argued that such a move may lead to excessive wage claims and increased risks of industrial action at a time when inflation is elevated. Additional changes include simplifying the 'Better Off Overall Test', which employers have previously flagged as a challenge to negotiating new agreements.

On skills and training, more funding will be allocated for a range of education initiatives. An additional $1 billion of funding will be provided by the Federal Government and state and territory governments to provide an additional 465,000 fee-free TAFE places, with 180,000 in 2023.

There were additional changes announced to encourage greater levels of workforce participation, particularly among older workers and women. This included increasing the amount of income that pensioners can earn before their pension entitlements begin to be reduced. There were also announcements around strengthening reporting standards on the gender pay gap and reporting and targets around gender equality in the workplace for larger businesses and the public service.

The Government has hailed the Summit as a success. However, the proof will be in the pudding. Focus will now turn to the communication and implementation of the large range of policies announced. Some announcements will require consultation and collaboration with the public and key stakeholders as legislative changes need to be brought forward to Parliament to give them effect. Submissions from and engagement with the public are expected over the next 12 months.

Another big piece of economic news was the release of the National Accounts mid-September which showed that the economy expanded by 0.9% in the June quarter and by 3.6% over the year to the June quarter, confirming the RBA's view that the economy remains strong.

Propelling the economic engine forward was household spending (up 2.2% over the quarter) and exports (up 5.5%). Households splashed out on services, such as airline travel, hotels, cafes & restaurants, and recreation & culture. These sectors had been at the coalface of closed borders and mobility restrictions. They're also likely to be the first to start feeling the squeeze from higher mortgage rates.

The one area where higher interest rates are beginning to take their toll is the housing market. The National Accounts showed that housing construction declined by 2.9% in the June quarter, and by 4.6% in annual terms. Forward indicators, most notably building approvals, suggests that the pipeline of projects has peaked, and we should expect a continued easing in activity.

The August 2022 read had consumer confidence well entrenched in negative territory. The consumer sentiment index had fallen for a ninth consecutive month, sliding to 81.2 points. This was the lowest reading since August 2020 and was around the lows recorded during the Global Financial Crisis.

On balance, the negative effects are likely to outweigh the positive offsets and continue to weigh on confidence. A key uncertainty remains how far confidence will fall before hitting a trough.

While confidence is low, consumers continue to spend big. We expect this anomaly to eventually correct itself with the headwinds from rising cost-of-living pressures and higher interest rates to lead to a slowdown in household consumption, particularly as we head into 2023.

The ASX300 Accumulation Index shed -6.29% over September to bring the 1-yr rolling return down to -8%.

United States

US stocks were highly volatile over September as investors digested a slew of economic releases. The Fed's preferred inflation measure, the US core PCE price index, came in well above expectations in August, worrying investors that inflation may be stickier than anticipated. In addition, a report from the US Commerce Department showed that personal spending rebounded in August, pointing to a still resilient economy.

All major US indices finished the month with three straight quarters of decline. For the S&P this is the first time since 2009, and for the Nasdaq since the dot-com bubble.

The dollar index steadied near 112 around September close, after retreating from a 20-year high of 114.778 over the month - another strong monthly gain on expectations that the Federal Reserve will tighten monetary settings further to bring down high inflation.

The index finished up about 3% over the month and is trading nearly 7% higher for the quarter. Fed policymakers reiterated that the central bank needs to raise interest rates to restrictive levels amid persistent inflationary pressures, despite concerns about growth and market volatility. The $USD also benefited from increased haven demand, given the US economy's strength relative to other developed nations.

Other data released over September was the personal consumption expenditure price index which rose 0.3% month-over-month in August of 2022, after a 0.1% decrease in July. Prices for services increased 0.6%, after being unchanged in July while the cost of goods decreased 0.3%, extending a 0.4% drop, reflecting a shift in spending. Food prices increased 0.8% (vs 1.3%) while energy prices tumbled 5.5% (vs -4.9%). Excluding food and energy, the PCE price index advanced 0.6%, faster than market expectations of a 0.5% rise, suggesting inflation is becoming more entrenched in the economy.

The S&P Global US Manufacturing PMI was revised higher to 52 in September of 2022 from a preliminary of 51.8 and above 51.5 in August.

Still, the reading pointed to subdued operating conditions although output and new orders returned to growth. Nonetheless, firms expanded their workforce numbers at the fastest pace since March 2022, although labour shortages continued to hamper firms' ability to work through incoming new orders.

Outstanding business rose again and at a quicker rate. At the same time, cost pressures softened amid reports of lower prices for some inputs. Although slower than those seen earlier in the year, the rate of selling price inflation picked up slightly as firms continued to pass-through higher cost burdens to customers.

The S&P500, NASDAQ, and Down Jones lost -9.21%, -10.44%, and -8.76% respectively over the month. These results drag the 1-yr rolling returns further down to -15.47%, -26.25%, and -13.40%.

Asia

China's currency woes continued over September, albeit the yuan significantly strengthened to 7.1 per USD as the month closed, after Chinese state media emphasised that the currency is unlikely to depreciate further.

The move was consistent with the People's Bank of China's (PBoC) warning against speculative trading, delivering clear verbal interventions to support the yuan amid its plunge against the dollar. The PBoC also raised the foreign exchange risk reserves for financial institutions when purchasing FX through currency forwards to 20% from the previous level of zero starting on September 28th, making it more expensive to bet against the domestic currency. Either way, as the month closed, the yuan fell to 7.26 per USD, its lowest level since the data first became available in 2011 and is set to drop for the seventh straight month as China's monetary policy diverges with the US and as a gloomy domestic economic outlook dented sentiment further.

Data supporting China's economic slowdown was underpinned by the official NBS Non-Manufacturing PMI declining to a four-month low of 50.6 in September 2022 from 52.6 a month earlier, reflecting the impact of hot weather and anti-COVID measures.

Both new orders (43.1 vs 49.8 in August) and foreign sales (46.0 vs 48.9) fell for the third month in a row and at a much steeper rate, while employment continued to drop (46.6 vs 46.8).

On inflation, input costs stabilised for the second straight month, with the index being unchanged from August (at 50); while output prices dropped for the sixth month in a row, with the rate of decrease softening slightly (48.2 vs 47.6).

Japanese industrial production rose by 2.7% month-over-month in August 2022, accelerating from an upwardly revised 0.8% growth a month earlier and easily beating market consensus of 0.2%, data showed. This was the third straight month of an increase in industrial output, mainly contributed to by production machinery (6.1% vs 6.0% in July), iron, steel, and non-ferrous metals (3.6% vs -1.6%), and chemicals (2.7% vs -4.8%). On a yearly basis, industrial output grew by 5.1% in August, reversing from a 2.0% drop in July and increasing for the first time in six months.

The au Jibun Bank Japan Manufacturing PMI was at 50.8 in September 2022, compared to the flash reading of 51.0 and after a final 51.5 in August. This was the softest growth in factory activity since a drop in January 2021, due to rising inflation and a slump in the yen.

New orders fell the most in two years amid weaker demand from foreign markets, particularly China, South Korea, Europe, and the US.

Also, output shrank for the third consecutive month, with the rate of fall the fastest in a year; and buying levels contracted further.

The consumer confidence index in Japan declined to 30.8 in September of 2022 from August's 3-month high of 32.5, amid lingering global economic uncertainty. All sub-indexes deteriorated: 'employment perceptions' (down 1.7 points from a month earlier to 35.4), the measure of 'overall likelihood' (down 2.1 points to 29.0), views toward income growth (down 0.6 points to 35.4), and willingness to buy durable goods (down 2.5 points to 23.5).

The Korean KOSPI ended September down 12.81% and the Japanese Nikkei 225 down -6.59%. The KOSPI's 1-yr rolling return is now -29.78%. The Chinese Shanghai Composite and Hong Kong's Hang Seng continued to fall, closing the month down -5.55% and -13.69% respectively; both still under strain for the year with their 1-yr rolling returns at -15.24% and -29.92%.

Europe

The economic sentiment indicator in the Euro Area slumped 3.6 points from a month earlier to 93.7 in September 2022, the lowest level since November 2020 and below market expectations of 95.0, amid concerns over rising inflation and interest rates, as well as a weakening economic outlook and an intensifying energy crisis due to the war in Ukraine.

There were declines in confidence among consumers (-28.8 vs -25.0 in August), retailers (-8.4 vs -6.5), service providers (4.9 vs 8.1), manufacturers (-0.4 vs 1.0), and constructors (1.6 vs 3.4). On the price front, the inflation expectations index rose to 41.3 from 37.0 a month earlier, while the gauge for selling price expectations among manufacturers increased to 50.3 from 44.6. Amongst the largest EU economies, the ESI fell markedly in Germany (-4.8 points), the Netherlands (-3.7 points), Italy (-3.7 points), France (-3.2 points) and, to a lesser extent, Spain (-1.0 points).

Adding to the Euro region's economic slump, the euro continued to fall toward US$0.95 in late September, a fresh low in 20 years. It is down almost 20% so far on the year, pressured by a stronger dollar as the Fed continues to deliver its big interest rate hikes, and as recession prospects in Europe are increasing due to the energy crisis.

Meanwhile, the European Central Bank (ECB) already started the tightening cycle by raising key interest rates by 125 basis points since July and pledging to continue to increase the borrowing cost as inflation shows no signs of peaking. ECB President Lagarde recently reinforced that the central bank must keep raising interest rates to tame inflation, even if the side effect of the tighter policy will be weaker growth, while several ECB members recently advocated another 75-basis point hike in October.

On a more positive note, the Euro region unemployment rate was unchanged at 6.6% for a second consecutive month in August of 2022, a record low reading and in line with market forecasts.

A year earlier, the jobless rate was much higher at 7.5%. There were 10.966 million unemployed persons, down by 30 thousand from July 2022. Youth unemployment also declined by 17 thousand to 2.136 million, pushing the rate down to 13.9% from 14.0% in July. Among the biggest economies in the Eurozone, declines in the jobless rate were seen in France (7.3% vs 7.4%) and Italy (7.8% vs 7.9%) while the jobless rate was steady at 3.0% in Germany.

Over to the UK, news that shocked global markets was the panic selling across UK's markets which saw the 10-year yield note topping 4.5% for the first time since November 2008, after the government announced sweeping tax cuts as part of a mini-budget from the newly appointed Truss government. The market's reaction also sent the sterling crashing to an all-time low of US$1.03, as investors worried about the repercussions of British finance minister Kwasi Kwarteng's economic proposals. While Kwarteng said his £45 billion of tax cuts would support the economy, the IMF noted the strategy is likely to increase inequality and rating agency Moody's warned that unfunded tax cuts were credit negative.

This saw the Bank of England imminently announcing plans to carry out temporary purchases of long-dated UK government bonds from September 28th until October 14th, to restore orderly market conditions.

The Europe 600 STOXX Total Return index fell -6.57%. The French CAC 40 fell -5.92%, the German DAX -5.61%, and the UK FTSE100 followed with a -5.36% drop. Their 1-yr rolling returns fell to -11.62%, -20.62%, and -2.72% respectively.

Footnotes

1 The Management Costs included in this fact sheet are inclusive of the Management Fee and any Performance Fees and includes the effect of GST (net of RITC). They do not include other indirect costs. Refer to the Product Disclosure Statement and online disclosures for further information.

2 Past performance is not a reliable indicator of future performance. Performance returns are calculated net of management fees and costs. Growth and distribution returns may not equal the total net return due to rounding.

3 Allocations may not equal 100% due to rounding.

For more information

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