



Australian
National
University

ANU Student Managed Fund

AA Rebalancing Report

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Notes:

All dollar amounts in this report are Australian dollars.

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Rebalancing decision and implementation

The Student Managed Fund (SMF) has decided to rebalance the growth/defensive asset weights within the SMF portfolio back to the target levels of 80%/ 20%. This follows the growth weight moving below 77% and the defensive weight moving above 83% on 16th September 2022, which established $\pm 3\%$ deviation from target thus triggering the rebalancing procedure. It was decided that the rebalancing be conducted as follows:

1. Purchase sufficient iShares Core S&P/ASX 200 ETF (IOZ) to achieve the overall target weight of 55% Australian equities.
2. Purchase sufficient Vanguard MSCI Index International Shares Hedged ETF (VGAD) to achieve the target weight of 10% in hedged developed market equities (DM, H).
3. Reduce holdings in the BT Cash Management Trust (CMT) to fund these allocations to align the growth/defensive weight towards the 80%/20% target weight.

The above rebalancing transactions were proposed with reference to portfolio weightings at the market close on 7 October 2022, which are reported in Table 1. As eliminating the entire deviation from target for the growth/defensive weight would have required enacting small but costly transactions that are unlikely to add significant value, the expectation is that some modest differences to target were projected to remain after these trades.

The trades were implemented on 10th October 2022 as follows:

- i. Purchase of 626 shares in IOZ for total cost of -\$16,837.96.
- ii. Purchase of 133 shares in VGAD for total cost of \$9,523.33.
- iii. The net balance was funded by reducing holdings in the CMT) by \$26,361.29.

The following should be noted with respect to the projected portfolio weights after the above trades, which were re-estimated by the Fund Convenor based on revised portfolio weightings just prior to placing the trades:

- An underweighting in growth assets (i.e. total equities) of -0.18% was projected.
- The projected counterpart overweighting by the defensive portfolio was attributable to an overweighting in Australian fixed income (AFI). The AA team is also in the process of reviewing the AC/AFI split within the defensive portfolio with the potential to increase the AFI weighting back to the originally endorsed weighting of 15%. Selling AFI and reversing this trade later would incur unnecessary transaction fees and hence was not pursued
- Within the growth portfolio, the trades were projected to leave emerging market equities (EM) underweight by -0.15%, Australian equities (AE) underweight by -0.05% and unhedged developed market equities (DM, U) overweight by 0.02%.

Background

On the 16th of September 2022, the SMF portfolio growth/defensive target weights deviated by $\pm 3\%$ thus triggering an informed rebalancing decision as per the SMF Investment Policy Statement (IPS). The deviation was a factor of two key variables. First, broad weakness in equity markets, largely in response to monetary tightening and associated implications for discount rates and growth expectations. Second, while equity prices have declined, AC has held its value increasing its weight within the SMF portfolio.

Table 1: Portfolio weights and proposed trades

Based on prices as of 7th October 2022

Total SMF portfolio	Current portfolio weights	Revised target weights	Deviation from target	Proposed trades	Proposed portfolio weights	Proposed deviation from target
Growth assets						
<i>Australian equities</i>						
AAE portfolio*	52.90%	55.00%	-2.10%	0.00%	55.00%	-1.88%
AA portfolio holdings	0.00%	0.00%	0.00%	+1.99%	0.00%	+1.99%
Total Australian equities	53.12%	55.0%	-2.10%	+1.99%	55.00%	-0.11%
<i>International equities</i>						
Emerging market equities	9.90%	10.00%	-0.10%	0.00%	9.90%	-0.10%
Developed market equities, hedged	8.83%	10.00%	-1.17%	+1.06%	9.89%	-0.11%
Developed market equities, unhedged	5.10%	5.00%	0.10%	0.00%	5.10%	0.10%
Total international equities	23.83%	25.0%	-1.17%	+1.06%	24.89%	-0.11%
Total growth	76.73%	80.0%	-3.27%	+3.05%	79.78%	-0.22%
Defensive assets						
Australian fixed income	7.72%	7.50%	0.22%	0.00%	7.72%	0.22%
Australian cash & accruals						
AAA	9.68%	-	-	-	-	-
CMT	4.00%	0.50%	3.50%	-3.05%	0.95%	0.45%
Accruals	0.13%	-	-	-	-	-
Franking credits	1.73%	-	-	-	-	-
Total cash	15.55%	12.50%	3.05%	-3.05%	12.50%	0.00%
Total defensive	23.27%	20.00%	3.27%	-3.05%	20.22%	0.22%
Total SMF portfolio	100%	100%	0%	0%	100%	0%

Reasons for rebalancing

The AA team has decided to rebalance the SMF portfolio back towards target weights of 80% growth and 20% defensive for the following reasons:

- A decision to withhold from rebalancing and wait for a $\pm 5\%$ deviation in growth/defensive weights to occur requires conviction that equity markets are likely to continue to fall. The AA team believes there is insufficient evidence to withhold from rebalancing, and as it sees attempting to forecast equity markets in the short term to be both unreliable and speculative. We also note that equities tend to mean revert.
- The decline in equity markets has presented an opportunity for the AA team to rebalance the portfolio and purchase equities at a reduced price, while still following the SMF's long-term investment horizon and objectives. Forward P/Es in Australian and international equity markets are below historical averages (see Figure 2 and Figure 3 in the Appendix). Thus, the AA team can be confident that we are not purchasing equities at an inflated price. If anything,

it presents a rebalancing opportunity to capitalise on equity prices that have priced in potential for future weakness in earnings to at least some degree.

- Both our 3-year and 10-year return modelling favours rebalancing. Across both investment horizons, AE and DM(H) generate higher expected returns than AC, except for the 'Crisis' and 'Stagflation' scenario states. Our expected return projections are shown in the Appendix as Figure 1. Our modelling assumes that AC earns the returns on Betashares Australian High Interest Cash ETF (AAA) which historically outperforms the CMT by 0.7% p.a.

Funding the rebalance

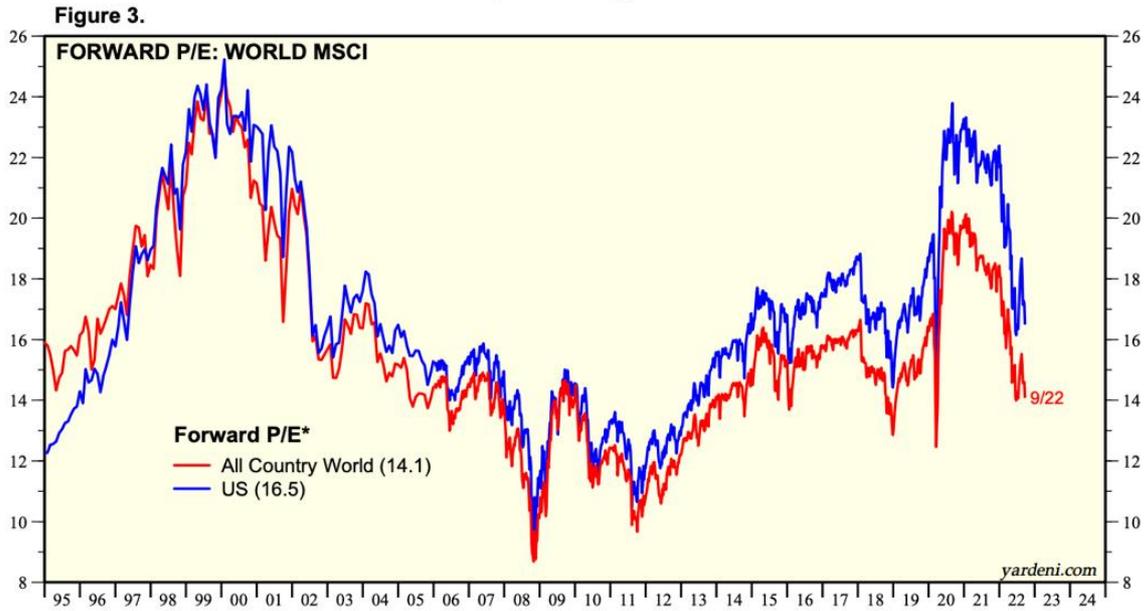
The AA team has decided to fund the rebalance decision by reducing holdings in the currently overweight CMT. This means both IOZ and VGAD can be returned to target weights without incurring excess and unnecessary transaction costs from other sources. Also of relevance is that BT Panorama requires maintenance of at least \$2,000 within the CMT, which amounts to a minimum CMT weighting of 0.28% at the current SMF portfolio value.

Appendix

Figure 1: Forecasted year 3 and 10 real horizon returns of AE, DM, H, and AC

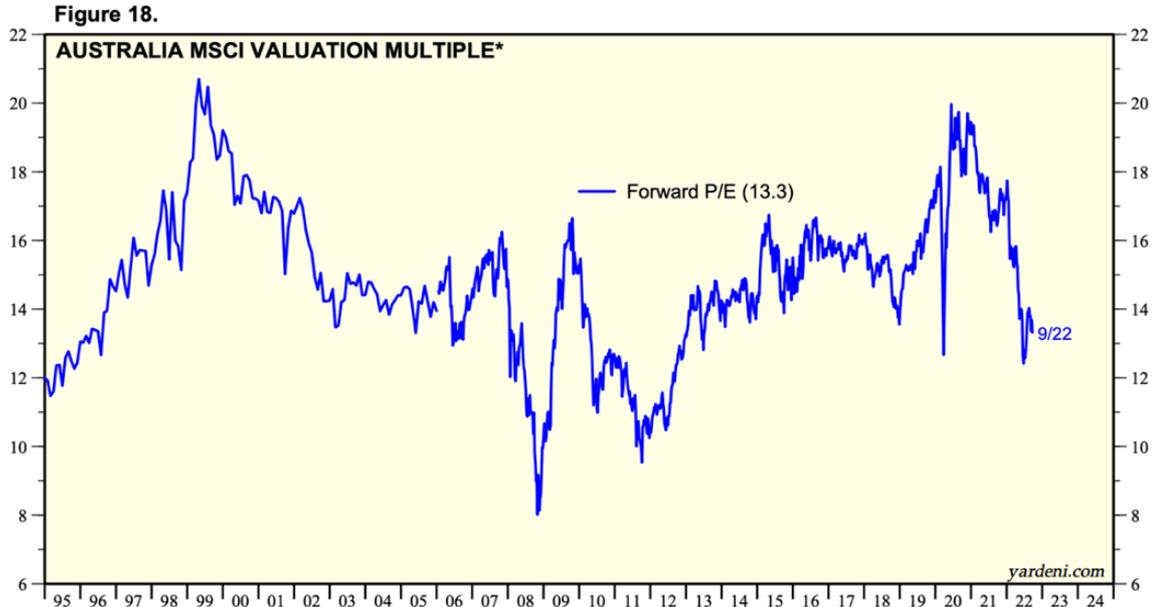
Scenarios				Year 3 real horizon return under 11 scenarios			Year 10 real horizon return under 11 scenarios		
No.	Inflation	Growth / Potential	Weight	AE	DM, H	AC	AE	DM, H	AC
1	High	High	6%	7.78%	6.77%	-1.82%	6.01%	5.12%	0.18%
2	High	Medium	17%	5.78%	4.67%	-1.93%	3.95%	2.44%	-0.45%
3	High	Low	6%	2.74%	2.74%	-2.04%	0.62%	-0.24%	-0.98%
4	Medium	High	9.5%	10.45%	8.67%	-1.47%	8.00%	7.32%	-0.08%
5	Medium	Medium	25%	12.51%	10.38%	0.37%	7.10%	6.47%	0.66%
6	Medium	Low	14%	8.56%	6.20%	-1.71%	5.10%	3.43%	-1.00%
7	Low	High	3%	15.57%	6.18%	-1.10%	10.48%	9.30%	-0.44%
8	Low	Medium	6%	12.04%	9.56%	-1.45%	7.67%	6.51%	-0.87%
9	Low	Low	8%	8.75%	7.01%	-1.52%	5.02%	3.71%	-1.18%
10	Stagflation	Stagflation	2%	-19.66%	-19.42%	-0.94%	-17.69%	-17.49%	0.70%
11	Crisis	Crisis	3.5%	-34.93%	-35.02%	-1.63%	-0.61%	-5.72%	-0.67%
Probability-weighted			100%	7.96%	6.02%	-1.16%	5.61%	4.51%	-0.26%

Figure 2: MSCI World PE multiple



* Price divided by 12-month forward consensus expected operating earnings per share. Monthly through December 2005, weekly thereafter.
Source: I/B/E/S data by Refinitiv.

Figure 3: MSCI Australia PE multiple



* Price divided by forward consensus expected earnings per share. Monthly data through December 2005, weekly thereafter.
Source: I/B/E/S data by Refinitiv.

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