Quarterly Commentary
**ETF Model Portfolios**

**Q1 2022**

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# State Street ETF Model Portfolios

- Global equity markets had a rough start to the year. Russia's shocking invasion of Ukraine and the tightening stance adopted by central banks in the wake of surging inflation weighed on both equities and bonds.
- Overall, global equity markets registered negative gains over the first quarter, down -8.4%.[3]
- The State Street ETF Model Portfolios are designed with varying objectives to deliver diversified risk-adjusted returns over the long term through multi-asset allocation.

## The Market in Review

Global economic growth faced multiple headwinds in the first quarter. Rising geopolitical tensions with Russia pushed energy and commodity prices to extreme levels, which led to a further surge in inflation, increased supply chain disruptions, and global growth risks.

On the economic front, the latest data in the United States (US) point towards resilient activity amid higher energy prices and inflation. The unemployment rate fell to 3.6%,[20] just 0.1% higher than the pre-pandemic low and aggregate consumer demand remained solid. In Europe, the re-opening of the economies gave a boost to growth, however, soaring energy costs and the Russia-Ukraine War threatened to derail the recovery. In Australia, consumer demand soared late last year, offsetting softness elsewhere, particularly in residential investment. The labour market is essentially fully healed, the participation rate is high, and wage growth and inflation is starting to move higher. Compared with the US or United Kingdom (UK) experience, current inflation levels of either price (3.5% y/y as of Q4)[20] and wage (2.8% y/y as of Q4)[20] remain modest.

Equity markets declined in the first two months of the quarter. Although the markets recovered some losses toward the end, they were still down for the quarter. Investor sentiment was weighed down by concerns around the Russia-Ukraine War and the tightening stance adopted by central banks in the wake of surging inflation. Developed market equities were down by 8.2%[4] while, emerging market equities fell by 8.5%[10] as Omicron cases hit China and put additional pressure on the Chinese equity markets. On the other hand, the Australian equity market registered positive returns and was an outlier amongst global peers. Massive gains in the energy and materials sectors outweighed technology losses leading to a 2.2%[9] gain for the ASX200 index in the first quarter. The Australian dollar also rallied steadily throughout the quarter to finish up 3.0%[2] versus the US dollar. The continued rapid recovery from Omicron and near-record strength in commodity terms of trade supported the currency.

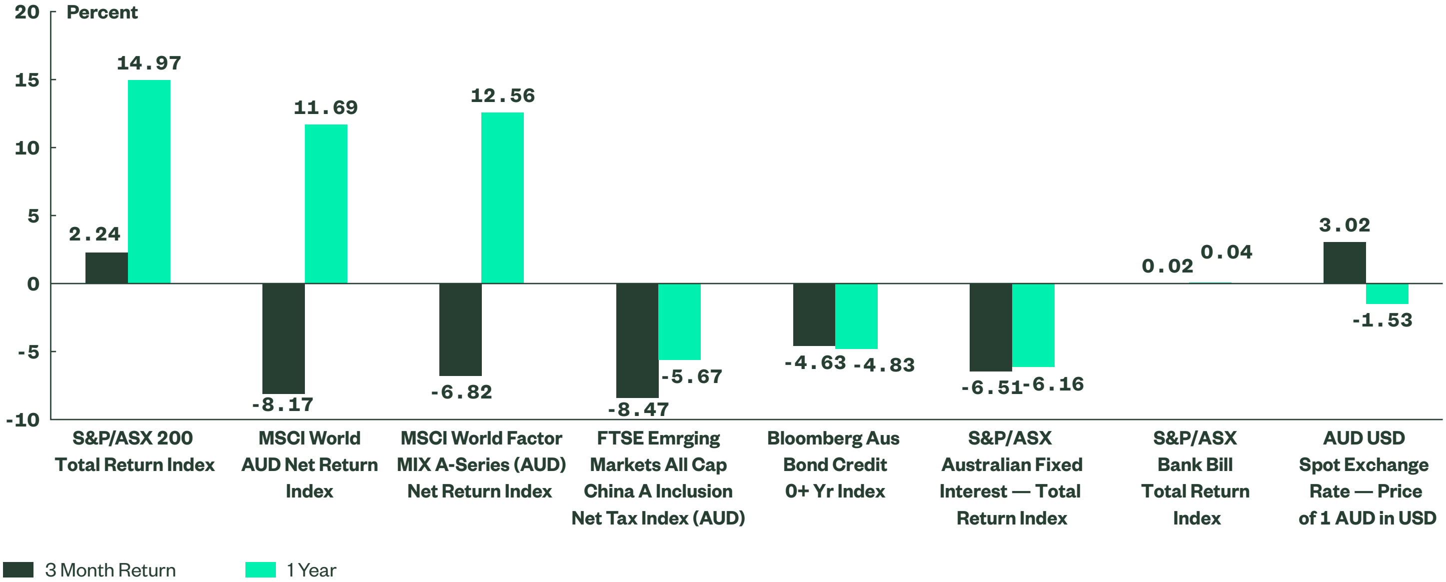
Global bonds posted negative returns for the first quarter.[11] Increased volatility caused by inflation and expected rate hikes by key central banks led to a global bond sell-off. The US 10-year Treasury yield increased from 1.51% to 2.35%,[16] with the 2-year yield rising from 0.73% to 2.33%.[17] The short end of the curve increased the most and yield curve inversion was visible across the longer end of the curve. The UK 10-year yield rose from 0.97%[18] to 1.61%.[18] The Bank of England raised rates twice during the quarter, by 25 bps each to 0.75%.[20] The AUD 10-year Treasury yield increased based on expectations of quicker interest rate hikes, from 1.67% to 2.84%.[15]

Globally the Russia-Ukraine War has lowered growth expectations and raised inflation forecasts. However, the underlying fundamentals, at least for now, remain positive with the impact of Omicron fading, this should improve mobility and sustain demand. Robust household savings and strong job market may help consumers weather higher inflation and energy prices. This combined with solid corporate financials should help underpin economic growth. Overall, the macroeconomic environment is less certain than it was a few months ago but at present, we are not forecasting a global economic downturn and still expect growth to remain positive.

## Asset Class Performance (in AUD) [1]

- The **Australian dollar** strengthened against the US Dollar, up 3.0%.[2]
- **International Equities** were negative, down -8.2%[4] with the **multi-factor** (minimum volatility, quality and value) strategy posting similar losses, down -6.8%.[5]
- **The quality factor** declined the most, down -11.2%.[7] **Minimum volatility and value** also returned negative, down -5.8%[6] and -3.6%,[8] respectively.
- **Australian equities** advanced up 2.2%[9]
- **Emerging markets** were negative, down -8.5%.[10]
- **Global bonds** were negative, down -5.0%.[11]
- **Australian bonds** were negative, down -4.6%.[12]
- Global **corporate bonds** were also negative, down -5.7%.[13]
- **Cash** returns in the Australian money market were flat.[14]

Figure 1
**Major Asset Class Performance**




Source: As of 31 March, 2022, Bloomberg Finance L.P, MSCI. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. The index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income. Past performance is not a reliable indicator of future performance.

## Positioning and Hypothetical Model Portfolio Performance

### State Street Risk-Based ETF Model Portfolios

For the first quarter of 2022, the multi-factor international equity allocation and the Australian government bond allocation were the major detractors to the risk-based portfolios' total return. The portfolios' multi-factor international exposure, SPDR MSCI World Quality Mix Fund (QMIX) declined (-6.8%)[5] for the quarter. This was driven mainly by the quality factor (-11.2%).[7] The allocation to emerging market equities also had a negative impact to the risk-based portfolios' performance as geopolitical tensions took centre stage. On the contrary, the Australian equity allocation had a positive contribution to the risk-based portfolios' performance. Australia has minimal exposure to Russia, and soaring commodity prices lifted by the Russia-Ukraine War helped domestic equities, notably energy and materials shares. On the fixed income side of the ledger, both government and credit bonds detracted during the quarter and contributed negatively to the risk-based portfolios' total return. Australian government bond yields which rise when bond prices fall, increased during the quarter on the back of expectations of quicker interest rate hikes.

**State Street Moderate ETF Model Portfolio** The moderate model portfolio seeks to provide optimal capital efficiency over a long-term horizon. The portfolio is designed to generate a moderate amount of capital growth along with some income with exposures to both defensive and growth assets.

**Overall performance of the hypothetical model portfolio for the quarter was negative, down -3.04%.**

**State Street Balanced ETF Model Portfolio** The balanced model portfolio seeks to provide optimal capital efficiency over a long-term horizon. The portfolio is designed to provide capital growth while taking a modest amount of risk with exposures across both defensive and growth assets although more heavily weighted to the latter.

**Overall performance of the hypothetical model portfolio for the quarter was negative, down -2.84%.**

**State Street Growth ETF Model Portfolio** The growth model portfolio seeks to provide optimal capital efficiency over a long-term horizon. The portfolio is designed to predominantly focus on capital growth with exposures weighted to growth assets although it does have exposures to defensive assets.

**Overall performance of the hypothetical model portfolio for the quarter was negative, down -2.87%.**

## State Street Target Income ETF Model Portfolio

The State Street Target Income ETF Model Portfolio is designed with an income objective that is determined on an annual basis. For the 2021/2022 financial year the portfolio aims to target, before expenses, an income objective of 3% per annum.

The portfolio's allocation to Australian high dividend stocks was the major contributor to the portfolio's total return as the materials and energy sector registered robust gains. The metals and mining sector has dominated the gains, rising over 23%[19] in first three months of the year. The international high dividend stock allocation had a negative contribution to the portfolio's total return. On the fixed income side of the ledger, all three components, government, credit and high yield declined for the quarter and had a negative contribution to the total return. Government bonds exposure was the major detractor, as sovereign bond yields increased sharply. Corporate bonds returned negative as spreads widened. High yield bonds outperformed investment grade corporates due to the higher coupons embedded within the asset class.

The income proportion of the portfolio's total return for the quarter was positive 0.78%, supporting the portfolio's primary objective to generate income.

**Overall performance of the hypothetical model portfolio for the quarter was negative, down -0.09%.**

**Model Portfolio Performance presented is hypothetical and has been provided for illustrative purposes only, it does not reflect the results of the actual trading of any account or group of accounts and actual results could differ substantially.**

The hypothetical State Street ETF Model Portfolio Total Returns are the sum of Growth Return and Distribution Return and reflect the investment strategy decisions made by State Street's investment professionals for each performance period presented. Returns greater than one year are annualised. The hypothetical model portfolio performance was achieved by mathematically combining the actual performance data of the underlying ETFs multiplied by the hypothetical model portfolio weights allocated to each ETF on a monthly basis. The performance assumes that all dividend distributions paid by the underlying ETFs were reinvested and is calculated gross of trading fees but does not reflect spreads or broker commissions for the hypothetical sale and purchase of the underlying ETFs or any other fees which would be charged by the product provider.

State Street has chosen to use the actual historic performance of the underlying ETFs rather than the underlying ETFs index performance to ensure that the model portfolios reflect as closely as possible of any actual investments that follow the model portfolio strategy, by reflecting differences such as tracking error of the underlying ETFs relative to the underlying ETFs indices.

Limitation of hypothetical results: Hypothetical results have inherent limitations because they do not reflect actual trading by State Street during the period described and may not reflect the impact that material economic and market factors might have had on State Street's decision-making if it was actually managing clients' money pursuant to the strategies. There is no guarantee that any of the investment strategies will be successful and investors should be aware that they can lose money investing assets in accordance with the strategies.

## Endnotes

1 All returns as at 31 March 2022. Index returns reflect capital gains and losses, income, and the reinvestment of dividends. Index returns are unmanaged and do not reflect the deduction of any fees or expenses. The index returns reflect all items of income, gain and loss and the reinvestment of dividends and other income. Past performance is not a reliable indicator of future performance.

2 Source: Bloomberg, AUD USD FX rate.

3 Source: MSCI All Country World Net Total Return AUD Index.

4 Source: MSCI World Net Total Return AUD Index.

5 Source: MSCI World Factor Mix A- Series (AUD). Pacific Net Total Return Index in AUD.

6 According to MSCI World Value Weighted Net Total Return Index in AUD.

7 Source: MSCI World Quality Net Total Return Index in AUD.

8 Source: MSCI World Minimum Volatility (AUD) Net Total Return Index.

9 Source: S&P/ASX 200 Total Return Index.

10 Source: FTSE Emerging Markets All Cap China A Inclusion Net Tax Index (AUD).

11 Source: Bloomberg Barclays Global Aggregate Total Return Hedged AUD Index.

12 Source: Bloomberg AusBonds Credit 0+ YR Index.

13 Source: Bloomberg Global High Yield Total Return Index Hedged AUD.

14 Source: Bloomberg AusBond Bank Bill Index.

15 Source: Bloomberg, Australia Govt Bond 10 Year Yield.

16 Source: Bloomberg, US Generic Govt 10 Yr.

17 Source: Bloomberg, US Generic Govt 2 Yr.

18 Source: Bloomberg, UK Gilts 10 Yr.

19 Source: FactSet, MSCI Australia/Metals & Mining.

20 Source: Bloomberg.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An investment in the model portfolio carries a number of standard investment risks; these risks are outlined in each Provider's PDS which should be read in full and understood by the potential investors.

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- the Provider's decision to exercise its discretion to implement a given strategy in a way that differs from the information provided by State Street;
- the timing of the Provider's implementation of strategy updates; and
- investor imposed investment restrictions; and the timing and nature of investor initiated cash flow activity in the account.

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