VIP Fixed Interest Portfolio



Monthly Review

January 2015

Investment Objective

The **VIP Fixed Interest Portfolio** aims to provide a high level of income over the medium to long term through investment in a diversified portfolio of Australian fixed income securities including Government and Semi Government Bonds, Managed Funds, Term Deposits and Cash.

The portfolio invests in 4 to 10 fixed income securities including Government and Semi Government Bonds, Managed Funds, Term Deposits and Cash that are managed with a bottom up approach while taking top down economic considerations into consideration.

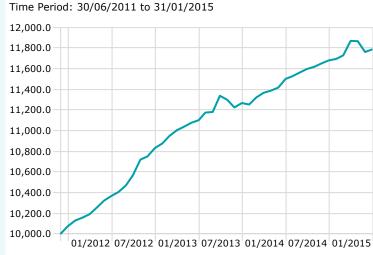
Performance Review

The Fixed Interest portfolio generated a 0.22% return for the month and -0.68% over the last 3 months.

This was against the Bloomberg AusBond Composite 0+Yr index return of 1.61% and 4.63% over the month and last 3 months respectively.

The post-fees returns for the *Investment* and *Superannuation* & 11,000.0 *Pension* portfolios are shown in the table below.

Investment Growth



-VIP Fixed Interest

Trailing Returns

As of Date: 31/01/2015

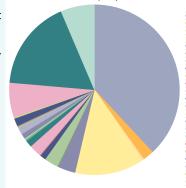
	1 Month	3 Month	6 Month	1 Year	2 Years	Since Inception
VIP Fixed Interest	0.23	-0.68	0.92	2.49	3.04	4.68
VIP Fixed Interest Investment	0.11	-1.01	0.24	1.12	1.66	3.28
VIP Fixed Interest Super-Pension	0.16	-0.88	0.52	1.68	2.22	3.85
Bloomberg AusBond Bank 0+Y TR AUD	0.25	0.71	1.38	2.72	2.77	6.92

Portfolio Exposure

The portfolio is mainly allocated across Australian fixed interest securities with the next dominant region being the US.

Across these regional markets the portfolio holds approximately 73.4% Government bonds, 18.1% Corporate bonds, and 5.6% Cash and Cash Equivalents.

VIP Fixed Interest - Fixed-Inc Country Exposure



Portfolio Date: 31/01/2015

Source: Morningstar Direct

Month in Review - Economic & Market Commentary

What's in store for 2015?

2014 saw an interesting period for global economies and markets, and at this point it seems that 2015 will be serving up a similar menu. And it seems that this menu is going to continue to be defined by low interest rates and rising growth asset prices as investors search for yield and income growth.

The size of the money printing programs in the US, Japan, and stimulus measures in China not only indicated the continuation of low interest rates for some time to come, but also acted to drive up growth asset prices (shares and property) forcing investors to take greater risk to achieve returns in excess of low cash and short-term bond returns.

These growth asset prices are the main focus now as investors ask whether the underlying economies are strong enough to sustain these prices and help these companies (in the case of shares) achieve greater profits and dividend growth.

Market shocks as we experienced last September and October were due to these types of questions as commodity and oil price falls signalled weak global growth that was not sufficient to support share prices at those levels.

In reply to this, developed economies have confirmed there commitment to keep interest rates low as a means to drive economic growth, and there is no better example of this than the Reserve Bank of Australia (RBA) cutting rates in February and talk of more cuts to come. Even the US Federal Reserve (US Fed) has signalled to the market that although rates are expected to rise in 2015 these rises will be small and will take some time.

In theory lower interest rates in Australia will help consumers spend as their confidence levels rise with the rise of their house prices and surplus cash flows. This increased confidence and demand will help business drive revenue growth and profitability in an environment where the interest bill on their loans is at very low levels. And, Australian companies that export goods or generate profits in US dollars will also see a rise in profits as low interest rates are expected to lower the value of the Australian Dollar (AUD) making exports more competitive.

The problem is that this theory does depend on where we're starting from, and the current position of the Australian economy is that of low economic growth (actually close to zero growth when you factor in inflation), low consumer demand, almost no wage growth, and rising unemployment. Luckily we have great political leaders from all sides that divert our attention from reality with leadership spills, a focus on international affairs that we all agree on (such as our non-approval of the death penalty) and searching for political point scoring when a potentially important report (such as the inter-generational report this week) is presented by the opposing side.

The reality is that some sectors will perform well in this environment and others will not, and therefore companies in those sectors will find it a little easier, than their peers, to generate profits. These would include companies with US dollar earnings, defensive companies that sell necessities and not discretionary items, and companies in sectors where global demand is depleting global supply such as Energy.

The US also has pressures even though the US economy is performing well with rising economic growth, stronger business investment, and falling unemployment. From a US perspective investors must consider the effect of increasing interest rates and a higher US dollar (making US exports less-competitive) on US consumers, businesses, and ultimately the US economy. This would also have an effect on the prices of US companies.

And finally, there is China and its impact on global asset prices. China, as in all economies, has its own pressures with one of the main being the large amount of reported un-used construction stock that will likely see a continuation of soft construction activity in China in 2015. Chinese authorities are expected to set fiscal and monetary policy to help ensure the economy can growth with an uplift in exports and consumer driven consumption with growth from consumption outpacing growth from investment and development. Commentators are projecting 7.1% GDP growth in 2015 for China, which will help support asset prices into the year.

The continuation of this expansionary interest policy from the world's major economies in 2015, in an attempt to lead to an increase in economic growth, is expected to sustain growth asset prices by driving company profit growth, driving export activity, and (as seen on the east coast of Australia) maintaining strong housing market activity. However, with the current stagnant position (weak in Europe) of most economies this profit growth will most likely be enjoyed by some and not all sectors of the economy.

Source: This article has been written with the help of our research partners Morningstar.

Source: Morningstar Direct

Portfolio Holdings & Adjustments

Trailing Returns

As of Date: 31/01/2015	Data Point: Return	Source Data: Total Return						
		YTD	1 Month	3 Month	6 Month	1 Year		
Realm High Income		0.22	0.22	1.26	1.85	5.80		
Bentham Wholesale Globa	l Income	0.02	0.02	0.24	-0.03	3.81		
Franklin Templeton Multise	ector Bond I	0.43	0.43	-2.25	-0.55	6.26		
Bloomberg AusBond Bank 0+Y TR AUD		0.25	0.25	0.71	1.38	2.72		

Performance Contributors & Detractors, and Portfolio Adjustments

The were no **Contributors** that achieved an excess return over the index for the month; and the **Top Detractors** for the month were the Bentham Global Income Fund +0.02%, Realm High Income Fund +0.22%, and the Franklin Templeton Multi-Sector Bond Fund +0.43%.

The VIP Investment Committee did not make any changes to the Fixed Interest portfolio in January.

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Source: Morningstar Direct