

Investment insight

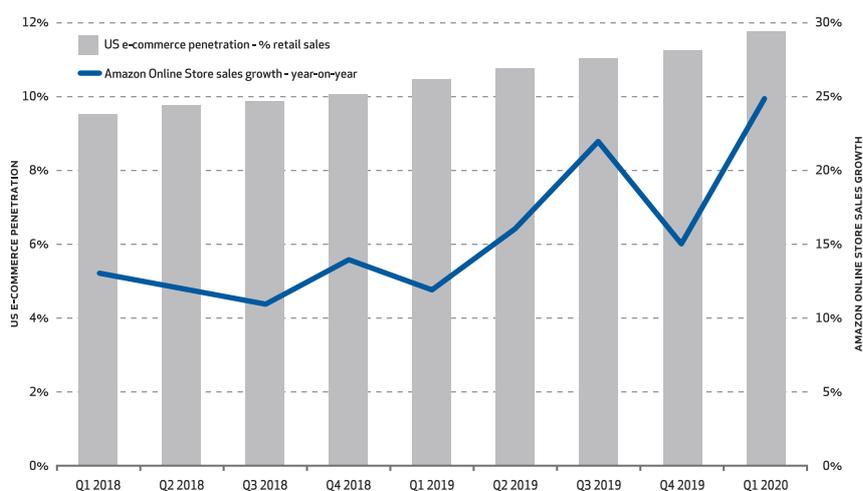
Digitising the global economy

Executive summary

- COVID-19 and three to four years of digitisation in six months.
- NZ Funds clients are invested in this once-in-a-generation digital transformation and we believe the changes we are witnessing are permanent.
- **The Tap. Touch. Speak. Grab and go.** Consumers and merchants are rapidly embracing a shift towards digital payments amid a surge in online purchases
- **Buy now, pay later.** New-age consumers, especially millennials, increasingly want simpler mobile-based financing solutions.
- **Communications.** People are creating digital habits that will last well beyond the current climate.
- **Digital currency.** Globally, digitisation of national currencies is already underway. Soon we may stop wondering whether crypto will ever catch on or why NZ Funds have invested in Bitcoin.
- **Rideshare.** Uber is well positioned, both during and post-COVID-19, to drive the ongoing shift to on-demand travel, mobility and food delivery.
- **Geopolitics.** The battle for technological supremacy between the United States and China will likely intensify.
- **Market volatility.** The powerful secular trends underpinning the technology sector's most appealing long-term growth stories remain intact.

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The rise of e-commerce



Source: FXC Intelligence Analysis, Company Financials, US Census Bureau.

“The way we make payments is changing faster than any other area of financial services. New technology and changing customer expectations are shattering the status quo and challenging the traditional role of banks.”

Interestingly, EY wrote this back in 2019, highlighting that the way we use technology and make payments was already changing rapidly. This is one of the many themes in the digital world where COVID-19 has brought three to four years of digitisation forward into a six month period. NZ Funds’ clients are invested in this once-in-a-generation digital transformation, and we believe the changes we are witnessing are permanent which allows us to look through any short-term market volatility.

The Tap. Touch. Speak. Grab and go

PayPal, the payments company, recently reported record earnings as consumers and merchants rapidly

embrace a shift towards digital payments amid a surge in online purchases. The California-based company reported a 137% year-over-year increase in new active accounts, to a record 21.3 million in the quarter, the most in its history.

It is well known that consumers have been doing more shopping online due to the coronavirus – and that means they must quickly adapt to technologies which are new to them. Companies have ramped up their digital commerce investment to meet consumers’ rapidly changing expectations. Amazon has benefited from COVID-19 - the company’s overall sales skyrocketed 40% year-over-year to US\$88.9 billion in the second quarter.

Despite appearing to be a highly established market, the United States offers significant opportunity for e-commerce growth, since e-commerce is still a minor channel there, accounting

for just 8.9% of retail sales. In China it accounts for 23.1%.

Research by NZ Post into how the COVID-19 response has impacted the way New Zealanders shop shows that online shopping increased 105% when the country moved into Alert Level 3. While this surge dropped off as life started to return to normal, online shopping remains around 30% up on this time last year, signalling that COVID-19 may have changed the way we shop forever.

NZ Funds' clients are invested in both Amazon and Paypal.

Buy now, pay later

If you have done any online shopping in the last few months, you have probably seen several interest-free, instalment payment offers from firms such as Afterpay, Laybuy, Zip and Oxipay. This is known as 'buy now, pay later' (BNPL). Approximately 20% of all clothing and footwear purchases in New Zealand were financed via BNPL in 2019. This has increased dramatically since COVID-19.

New-age consumers, especially millennials, increasingly want simpler mobile-based financing solutions. The chance to spread payments for a new pair of shoes or a kitchen appliance instead of paying the full amount upfront is appealing to many, and

especially to the younger generation who do not tend to use credit cards.

Splitit is a BNPL company in which NZ Funds' clients are invested. The company operates globally and is listed in Australia, the unofficial hub for BNPL companies globally. Splitit is an attractive way for New Zealand based investors to access the global payment theme.

Communications

Outside of payments, virtual communication is here to stay. For example, Zoom has record user numbers as work colleagues connect and friends and families catch up for virtual happy hours and birthdays. The trend is clear: People are creating new digital habits that will last.

Furthermore, some generations who had been avoiding online interactions are now attending virtual doctor's appointments, video chatting with the grandkids, and ordering supermarket shopping online. As digital technologies become more embedded in culture, new markets could open in unexpected demographics.

NZ Funds' clients are invested in Zoom.

Governments and central banks backing digital currencies

Globally, digitisation of national currencies is already underway. Sweden is well on the road to phasing

out conventional cash. New Zealand has been a world leader in paying with alternatives like chip cards. China, with its powerful, centrally controlled state, is ideally placed to push through a digital coin that will help it keep track of the money flows of everyone who uses it.

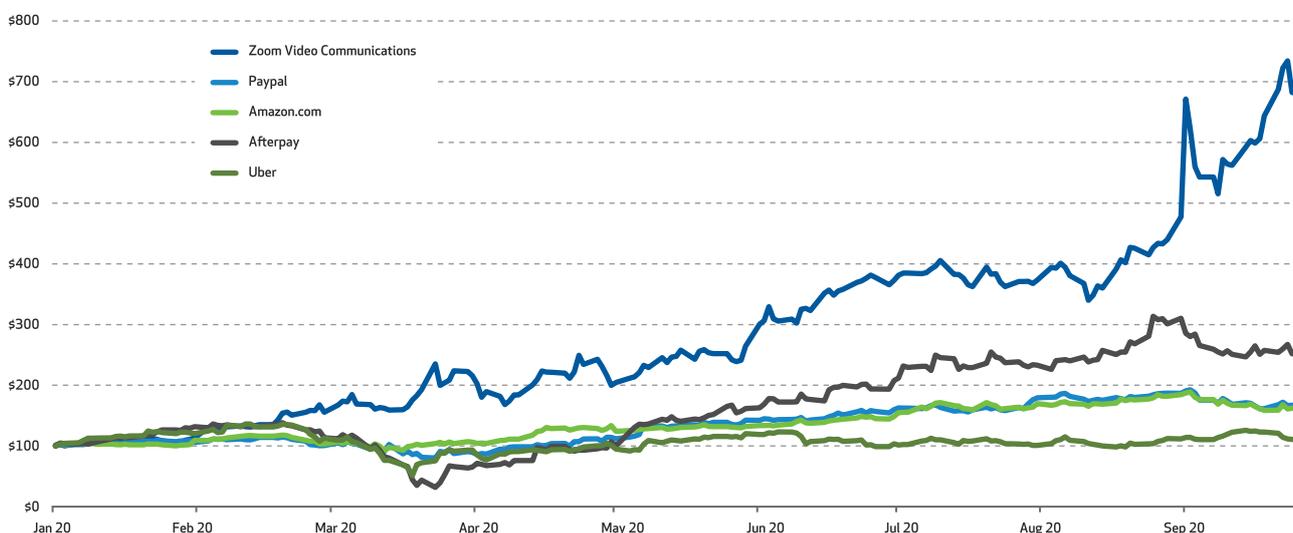
If central banks give their stamp of approval, we might see a lower reliance on fiat (government-issued) currency and actual paper money in our day-to-day lives. If more and more of our purchases are made online and cashless shops become more popular, why the need to exchange digital currency into paper money? Large retailers like Amazon might launch their own digital coins. Facebook are already doing so.

Soon, we may stop wondering whether crypto will ever catch on and why NZ Funds have invested in Bitcoin via Galaxy, whose mission is to institutionalise and promote the growth and advancement of the underlying ecosystem and technology behind digital assets and blockchain.

Ride share

Given Uber's global scale advantages in its core Rides business, we believe Uber is well positioned during and post-COVID-19 to drive the ongoing shift to on-demand travel, mobility and food delivery. While we expect business trends will worsen in a second wave of

Share performance



Source: Bloomberg.

COVID-19, we expect Uber will be able to leverage its scale globally to capture incremental market share and improve its competitive position into the eventual recovery. Rideshare has been a long-term theme of NZ Funds growth portfolios since the sector listed in 2019.

Geopolitics and technology

The battle for technological supremacy between the United States and China will likely intensify in a new world accustomed to online entertainment and shopping, and where the need for tracking data to avert future health crises is greater than ever.

United States policy toward China now rests on restricting the flow of technology to China, restructuring global supply chains, and investing in emerging technologies at home. Even a new United States administration is unlikely to stray from these fundamentals.

At the same time, China is racing to develop semiconductors and other core technologies to reduce its vulnerability to supply chains that pass through the United States. In pursuit of that goal, its leaders are mobilising tech companies to become national 'winners'.

Market volatility and technology

The sharp pullback in technology stocks this month strikes us as a normal bout of profit taking after the sector's strong run. Although a broad-based sell-off can be unsettling for investors, we believe that the powerful secular trends underpinning the technology sector's most appealing long-term growth stories remain intact.

The digitalisation of the economy has shown signs of accelerating, from growing adoption of e-commerce, payments, communication, and mobility. We understand concerns about the near-term outlook for tech stocks. However, we focus on the secular trends that we believe can create value over the long term.

Especially during periods of volatility, as an active manager we believe that our knowledge of individual companies and business models gives us an edge in identifying and taking advantage of compelling opportunities. In fact, we have never been more excited about the upside prospects of clients portfolios given the long-term trends identified.



James Grigor, CFA
Chief Investment Officer

James began his career at NZ Funds in 2000 as an intern, becoming an Equity Analyst in 2004.

Following a deployment with the New Zealand Defence Force to the Middle East in 2009, James relocated to London where he worked in management consultancy and private equity.

James returned to New Zealand in 2015, and following a senior role at Macquarie Bank, returned to NZ Funds in 2017.

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