

## Quarterly Market Comment

Despite a sharp pullback in September, most share markets delivered modest positive gains over the quarter. Weakness in September was notable – (after a bullocking run) the -4.1% decline in the MSCI All World Index was the worst month since the March 2020 COVID crash.

The New Zealand market was an outlier. As is often the case, it has been less volatile than international peers. After lagging year-to-date, the New Zealand market led the pack with healthy returns over the quarter.

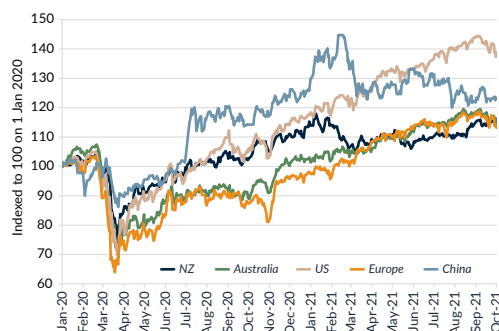
Volatile Chinese markets have continued to grab headlines retracing on concerns of (1) regulatory clampdowns on a range of industries such as technology and education, and (2) the troubles of highly indebted property developer Evergrande and risks to the broader housing market.

Bond returns were negative over the quarter with yields continuing to firm as economies recover and inflation tracks at the highest levels in decades. Central banks around the world are edging toward tightening. In New Zealand the lowest short-term interest rates in history have ended – on 6 October our Reserve Bank (RBNZ) hiked the official cash rate (OCR) for the first time since 2014.

### Global share markets hit a speedbump

Since the lows of the COVID crash in late March 2020 it has been an exceptional run for global share markets. That run hit a significant speedbump in September.

#### STOCK MARKET INDICES



Source: Thomson Reuters, Forsyth Barr analysis

With many markets near record highs and valuations generally lofty relative to history, they were susceptible to a pullback. To emphasise just how unusually calm it had been, until the last day of September (when the run was broken) it had been 236 trading days since the MSCI World Index had seen -5% drawdown. That's the second longest period in the past 25 years. Markets can sometimes be volatile, but for most of the past year (until recently) they haven't been.

Fears of "stagflation" (slow growth and higher inflation), are growing. Inflation measures around the world are the highest they've been for years. Soaring energy prices and persistent supply chain constraints are heightening concerns that will continue. Central banks are inching toward withdrawing crisis monetary policy settings, lifting ultra-low interest rates and ending "money printing" (quantitative easing).

The weakest of the major share markets over the quarter were China and Hong Kong. Initial concerns mounted after a clampdown by Chinese authorities on technology and education companies. Some worry these moves may be signs of broader pending regulatory tightening. More recently, markets have been focused on the troubles of property company Evergrande. The company, which builds around 4 – 5% of new homes in China, is the most indebted property developer in the world and has recently failed to meet some of its bond payments. The key concern for markets is contagion (the spread of problems from one company to another) given the company's long list of creditors including local banks, offshore bondholders, contractors, suppliers, and retail investors. We anticipate Chinese policymakers are likely to react quickly to ring-fence Evergrande, but concerns will likely persist until plans for managing the company's issues are known.

### New Zealand market bounces despite COVID lockdowns

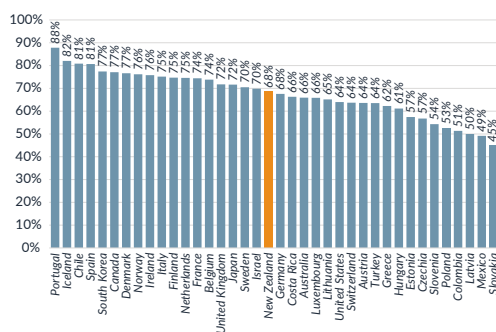
After being a laggard to global markets, the New Zealand share market had a strong quarter, boosted by companies reporting healthy results in August.

Some may be surprised the strong performance has come at a time when we've been hit with the first COVID-19 community outbreak in six months, and parts of the country remain in lockdown. Lockdowns will impact economically-exposed sectors and companies. The good news for investors, however, is the New Zealand market

is dominated by defensive companies in sectors like healthcare, utilities, telecommunications, and consumer staples. The earnings of these companies are less affected by the economic environment.

The silver lining of the outbreak is that it's been the wake-up call for many New Zealanders to get vaccinated. We no longer hold the inauspicious title of being the least vaccinated country in the OECD. This time round, New Zealand had little choice around how to respond to the COVID-19 outbreak. Widespread vaccinations are the only way to provide countries with broader choices about how to manage COVID-19 in the future.

#### SHARE OF PEOPLE WHO HAVE RECEIVED AT LEAST ONE DOSE OF COVID-19 VACCINE (OECD)



Source: Our World in Data, Forsyth Barr analysis

#### Interest rate rises are coming

New Zealand has been one of the first countries in the developed world to raise interest rates in a post-COVID world. On 6 October it lifted the official cash rate (OCR) by 25 basis points to 0.5%. Our economy is facing pent-up demand and capacity constraints — the housing shortage being the most obvious example — from the tidal wave of migrants over the last eight years. In recent years, that same migration kept a lid on wages. But now, with borders shut, capacity pressures are biting and inflation risks are rising. Closed borders are also driving up import costs. New Zealand is distanced from key trading partners and, as such, global supply chain constraints and rising freight costs have had an even greater impact here than abroad. Furthermore, unlike other countries New Zealanders have been breaking out the credit cards. Much of our strong economy is being funded by rising household debt for which we'll eventually face a cost. The market is pricing that by May next year, we will see three more rate hikes lifting the OCR to 1.25%, but the environment remains fluid and subject to change. The creep of the COVID-19 delta variant south of Auckland, uncertainty over how long level 3 lockdowns will be imposed, and growing questions around the pace of the global economic recovery will all influence the RBNZ's trajectory from here.

#### HIGHER INTEREST RATES AHEAD:

##### NZ OFFICIAL CASH RATE (OCR)



Source: RBNZ, Forsyth Barr analysis

#### A return to (normal) volatility

Recent volatility has broken a period of unusual calm in markets. Whilst we remain comfortable retaining a healthy weighting of risk assets (shares, property) in portfolios, we also believe the easiest gains in this cycle are likely behind us and that future returns will be lower than what we've seen over recent time.

Additionally, with share valuations at elevated levels vs. any historical reference, economic growth slowing, and central banks withdrawing stimulus, nervousness amongst some investors is heightened. We also expect that more bouts of market volatility are likely.

Volatility is a normal part of investing in equity markets. It's why investors earn an "equity risk premium" – a higher expected return over time from investing in the share market vs. lower risk assets like bonds. But all investors need to understand and be comfortable with the risk they are bearing. At any time if you have any queries about recent market events or wish to discuss the nature and composition of your portfolio please don't hesitate to contact your Forsyth Barr Investment Adviser. They're happy and available to discuss your investment plans at any time.

Matt Henry  
Head of Wealth Management Research

	30 September 2021	30 June 2021	% Change	30 September 2020	% Change	Year Ended 30 September 2021 Low	High
<b>Sharemarkets</b>							
S&P/NZX 50 G Index	13,276	12,655	+4.9%	11,747	+13.0%	11,539	13,276
Australian Accum index	84,352	82,932	+1.7%	64,608	+30.6%	64,244	84,352
S&P500 Accum (USA)	8,995	8,943	+0.6%	6,919	+30.0%	6,658	8,995
FTSE 100 Accum index	6,982	6,848	+2.0%	5,570	+25.4%	5,305	6,982
CAC40 Accum (France)	18,531	18,450	+0.4%	13,335	+39.0%	12,686	18,531
DAX (Germany)	15,261	15,531	-1.7%	12,761	+19.6%	11,556	15,261
Nikkei 225 (Japan)	49,402	47,970	+3.0%	38,259	+29.1%	37,869	49,402
Hang Seng (Hong Kong)	75,321	87,461	-13.9%	70,042	+7.5%	69,357	75,321
China 300	6,448	6,859	-6.0%	5,972	+8.0%	5,941	6,448
MSCI World (USD)	9,053	9,053	-0.0%	7,027	+28.8%	6,812	9,053
MSCI World (NZD)	9,053	12,957	+1.3%	10,631	+23.4%	6,812	9,053
<b>Money Markets*</b>							
NZ 90 Day Bill	0.46%	0.32%	+14 bp	0.29%	-0 bp	.25%	.48%
NZ 10 Year Bond	1.72%	1.80%	-8 bp	.63%	+62 bp	.51%	1.90%
AUD 10 Year Bond	1.16%	1.64%	-48 bp	.99%	+97 bp	.83%	1.83%
US 10 Year Bond	1.31%	1.58%	-27 bp	.71%	+69 bp	.68%	1.74%
<b>Returns</b>							
NZ Bank Bills			+0.1%		+0.3%		
NZ Corporate (Inv. Grade)			-1.2%		-3.8%		
NZ Government Bonds			-1.2%		-7.1%		
<b>Foreign Exchange</b>							
NZD/AUD	0.9537	0.9307	+2.5%	0.9258	+3.0%	0.9152	0.9537
NZD/USD	0.6898	0.6986	-1.3%	0.6610	+4.4%	0.7437	0.6898
NZD/GBP	0.5121	0.5051	+1.4%	0.5121	nc	0.5000	0.5361
NZD/EUR	0.5959	0.5890	+1.2%	0.5645	+5.6%	0.5565	0.6114
NZD/JPY	76.78	77.61	-1.1%	69.80	+10.0%	62.04	73.32

Source: Forsyth Barr Research, Bloomberg  
 \* 25 bp (basis points) is equivalent to 0.25%

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