

New Zealand Equity Monthly October 2022

New Zealand equity market well positioned to withstand near-term challenges

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By Michael De Cesare, Portfolio Manager

New Zealand stock market has followed a different track in 2022

Major global equity indices have trended downward overall in 2022 so far, with significant volatility seen in almost every individual index. But in contrast to their year-to-date performance, most markets staged a strong bear market rally in October, with key markets rising by mid to high single digits. Another notable feature of global equities this year has been the significant divergence seen among indices. The S&P/NZX 50 Index of the 50 largest names on New Zealand's Exchange has provided an example of this by following a different track to the overall global trend so far. Having outperformed most other markets in the year to date, the S&P/NZX 50 then largely missed out on the rally seen elsewhere in October. This appears to be the result of the New Zealand market's tendency to miss out on spikes due to its relatively low beta as well as its comparatively strong performance in the preceding months.

Global and domestic factors both creating challenges for companies

Movement in the Cboe Volatility Index (VIX) of expected volatility in the US stock market suggests that anxiety has been driving equities so far in 2022. Given that a VIX value of greater than 30 is thought to signal panic in the market, it is interesting to note that the index only spiked above 30 twice in 2021 but has jumped into panic territory multiple times so far in 2022. It has also been much higher on average than it was in 2021. This is understandable in view of the global factors at play this year. Dramatic changes in messaging from central banks on inflation, the Omicron variant of COVID-19, the war in Ukraine and uncertainty over Taiwan all caused volatility to surge in 2022. In addition to these external headwinds, New Zealand's companies are facing higher costs from wage rises, continued supply chain disruptions, and rising borrowing costs due to higher interest rates. All of these factors are compressing companies' margins. New Zealand is also at risk of falling behind in the global battle for human resources as competing destinations make radical changes to their immigration policies. One example of this is Singapore's recent announcement of a new, five-year work visa effective from January 2023.

New Zealand market well placed to withstand near-term challenges

Despite the near-term challenges, we believe that New Zealand's equity market is still in a strong position overall. The country itself is a liberal democracy with a stable political system. In addition, many of New Zealand's companies operate in oligopolistic industry structures that provide favourable operating environments. In the wider economy, unemployment is low, the household savings rate is close to a record high, and the strong US dollar is benefitting exports. Furthermore, New Zealand's tourism sector, which was almost as large as the country's dairy sector before the COVID-19 pandemic, now looks set to bounce back from the effects of the pandemic. The key task now is to navigate a way through the near-term headwinds facing the market.

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