Walter Yovich (FSP 41025)
Jarrod Goodall (FSP 198885)
Nathanael McDonald (FSP 629229)
Brock Fannin (FSP 1002346)

Yovich & Co. Market Update

19th March 2023

As at 17th March	NZX 50G	All Ords	Shanghai	FTSE	Dow	NASDAQ	NZDAUD	NZDUSD	OCR
Previous Week	11727.04	7348.23	3230.08	7748.35	31909.64	11138.89	0.9319	0.6131	4.75%
Week Close	11725.62	7188.18	3250.55	7335.40	31861.98	11630.51	0.9356	0.6269	4.75%
Change	-0.01%	-2.18%	0.63%	-5.33%	-0.15%	4.41%	0.40%	2.25%	0.00%

Following a heavy decline last week, the US market recovered this week, up 1.43%, as fears of further bank-run contagion abated. However, heightened volatility remains, with Credit Suisse in Switzerland coming under pressure. The NASDAQ finished with a strong recovery, up 4.41%, while the Dow Jones was down slightly. The UK market however was down a heavy 5.33%, while European shares were also down. The NZ market was flat last week, while the Australian market was down 2.18%.

First Republic Bank in the US was the second bank to come under pressure after the collapse of SVB, however it has been given assistance by a number of major US banks contributing $30b worth of deposits. This is a signal of confidence in the bank, and support for the banking system.

Treasury yields in the US have seen very large falls, as investors move capital into safe assets. The 2-year Treasury rate was down a massive 65bps during the week, falling to 4.16%, having pushed above 5.00% only the week before. The 10-year Treasury rate was down 26bps to 3.55%. In NZ, the 2-year swap rate fell by 25bps to 5.14%, while the 5-year swap rate fell by 21bps to 4.56%.

The USD fell, with the US Dollar Index down 1.05%. The NZD recovered some ground against the USD, up 2.25% over the week to 0.6269. The Dow Jones Commodity Index was down again last week by 2.54%, while the price of Brent Crude oil fell heavily by 12.3% to finish the week at US$72 per barrel.

Stats NZ said food prices rose 1.5% in February to be up 12% year-on-year, the highest inflation rate since September 1989. The Stats NZ rental index fell in February to be only 2.1% higher year-on-year. The index is being dragged lower by weak Wellington rents, while most other regions are recording rental inflation over 4%, including Auckland.

The REINZ house price index for February fell a seasonally adjusted 13.9% year-on-year. Annual net migration gain has continued to surge back to historically normal levels, hitting 33,200 for the year to January. The NZ economy contracted by 0.6% in the final three months of 2022.

The biggest movers of the week ending 17th March 2023				
Up			**Down**	
Fonterra Shareholders' Fund	13.42%		Synlait Milk	-10.94%
Pushpay Holdings	11.29%		Heartland Group	-7.51%
Channel Infrastructure NZ	7.09%		Fletcher Building	-6.05%
Serko	6.67%		Pacific Edge	-5.43%
Infratil	4.81%		Scales Corporation	-4.89%

Walter Yovich (FSP 41025)
Jarrod Goodall (FSP 198885)
Nathanael McDonald (FSP 629229)
Brock Fannin (FSP 1002346)

Market Highlight – Silicon Valley Bank Collapse

As reported last week, US-based Silicon Valley Bank (SVB) collapsed on 10th March following a bank run. Prior to the collapse, SVB was worth more than US$200b, and was the 16th largest bank in the US. California regulators seized the bank and put it under the control of the Federal Deposit Insurance Corporation (FDIC).

What Caused the Collapse?

The cause of the collapse was the mismatch between the duration of the bank's assets and its liabilities. For a bank, assets are the loans it makes to customers, and other securities it invests in, while its liabilities are the customers' deposits. Because assets are normally long-dated (e.g. long-term mortgages), and deposits are short-term, there is a timing risk. Generally, this risk is mitigated by:

1. Having a large and diverse customer base to avoid large movements in deposits;
2. Hedging interest rate risk via derivatives;
3. Holding sufficient capital reserves.

In SVB's case, their customer base was very concentrated in the tech space, which saw a surge in investment due to low interest rates. SVB saw large growth in deposits as a result, and invested a lot of these funds into a long-term Treasury bond portfolio, without sufficiently hedging their interest rate risk.

As interest rates rose, SVB's Treasuries fell in value, which normally wouldn't matter if the assets are held to maturity, but it becomes an issue if the bank is forced to sell Treasuries to fund withdrawals. The tech sector is particularly sensitive to interest rates, and as interest rates rose, tech companies found it tougher to raise capital, prompting them to draw on their deposits. With SVB's customer base being highly concentrated in the tech sector, this meant a significant surge in withdrawals that needed to be funded by selling assets at a loss.

To shore up its balance sheet, SVB announced a capital raise, which then triggered a panic among venture capital firms who advised companies to withdraw their money from the bank, causing a bank run.

Is the Bank Being Bailed Out?

The FDIC is acting as receiver, which typically means it will liquidate the bank's assets to pay back its customers, including depositors and creditors. The FDIC typically sells a failed bank's assets to other banks, using the proceeds to repay depositors whose funds weren't insured. So the answer is no, the investors of the bank are not being bailed out; the FDIC is insuring that depositors receive their money, avoiding a loss of confidence in the banking sector as a whole.

What is the Contagion Risk?

On top of the actions of the FDIC, the Federal Reserve has established a new program, Bank Term Funding Program (BTFP), which will provide banks with an additional source of liquidity, secured against high-quality securities, eliminating the need to quickly sell those securities in times of stress.

These measures mean that the systemic risk from the SVB failure are low, and it is unlikely to set off the kind of domino effect seen in the banking industry during the GFC in 2008. However, while a broader contagion is unlikely, smaller regional banks may be in for challenging times ahead, as they are disproportionately tied to cash-strapped industries like tech and crypto.

The collapse may have an ongoing effect on the economy in the US, as investors become more risk averse and capital becomes harder to attract, further adding to the risk of an economic slowdown.

Walter Yovich (FSP 41025)
Jarrod Goodall (FSP 198885)
Nathanael McDonald (FSP 629229)
Brock Fannin (FSP 1002346)

Investment News

Fletcher Building (FBU.NZ) Receives Shareholder Class Action

Fletcher Building has been served with a class action lawsuit filed in the Supreme Court of Victoria. The claim is brought by those who acquires shares between 17th August 2016 and 23rd October 2017 and relates to the company's disclosures regarding its Building + Interiors business in that period. The company said it would defend the claim.
Shareholders learned the construction division was experiencing heavy losses on a major project when its half-year results were announced in February 2017, however the scale of the problem emerged only gradually.
Current Share Price: $4.35, **Consensus Target Price**: $6.24

Fonterra (FCG.NZ/FSF.NZ) – Half-Year Profit Up 50%

Fonterra has announced its half-year results, with profit after tax of $546m, up 50% from the first half of 2022. The earnings per share were 33cps. The lift in earnings comes from the company being able to shift the milk supply into products and markets which are seeing favourable prices. The interim dividend is 10cps, up from 5cps last year. The forecast milk price range is $8.20-%8.80 per kgMS, and the full year forecast is for normalised earnings of 55-75cps.
Current Share Price (FSF.NZ): $3.38, **Consensus Target Price (FSF.NZ)**: $3.67

Auckland International Airport (AIA.NZ) Announces Multi-Billion Dollar Redevelopment

Auckland Airport has announced the replacement of the old domestic terminal, with a brand new domestic terminal to be fully integrated into the international terminal. The domestic terminal is almost 60 years old and is nearing capacity. The board has given approval for the project to move into the final stages of design as part of a circa $3.9b construction programme to take place over the next 5-6 years.
Current Share Price: $8.86, **Consensus Target Price**: $8.14