

Yovich & Co. Market Update

10th April 2023

As at 6th April	NZX 50G	All Ords	Shanghai	FTSE	Dow	NASDAQ	NZDAUD	NZDUSD	OCR
Previous Week	11884.50	7373.34	3272.86	7631.74	33274.15	12221.91	0.9359	0.6261	4.75%
Week Close	11870.08	7412.01	3327.65	7741.56	33485.29	12087.96	0.9386	0.6268	5.25%
Change	-0.12%	0.52%	1.67%	1.44%	0.63%	-1.10%	0.29%	0.11%	0.50%

Last week saw mixed results in share markets, with the NZ market relatively flat, down 0.12%. In the US, the market was flat overall, with the S&P 500 Index down 0.10%, however the Dow Jones was up 0.63%, while the NASDAQ was down 1.10%. The Australian and UK markets were both in positive territory, up 0.52% and 1.44% respectively. The key market mover was the increase in oil prices, following the decision by OPEC to cut production by more than 1 million barrels a day, which pushed energy shares higher.

The Reserve Bank of NZ made a shock 50bps increase to the Official Cash Rate, where it was widely expected to increase by 25bps. The move takes the OCR from 4.75% to 5.25%, which is already at or above some economists' forecasts of the peak of the OCR during this tightening phase, but still 25bps away from the RBNZ's forecast peak of 5.50%. The Reserve Bank of Australia however have opted to go in a different direction, and have paused their interest rate hikes, leaving the cash rate at 3.60%.

Weak data from the US in relation to manufacturing, services, and jobs reports moved US interest rates lower. The 2-year Treasury rate declined by 31bps to 3.82% during the week, while the 10-year Treasury rate was down 27bps to 3.31%. In NZ, despite the shock OCR increase, rates actually fell, suggesting little buy-in from the market on the RBNZ's view that higher rates are needed, and showing the market's view of easier monetary policy in the second half of this year. The 2-year swap rate declined by 4bps to 4.99%, while the 5-year swap rate was down by 17bps to 4.25%.

The US Dollar Index was down by 0.55%, and the NZD appreciated slightly against the USD, moving to 0.6268. The Dow Jones Commodity Index was up 0.69%, and the price of Brent Crude oil was up 6.75% to just above US\$85 per barrel.

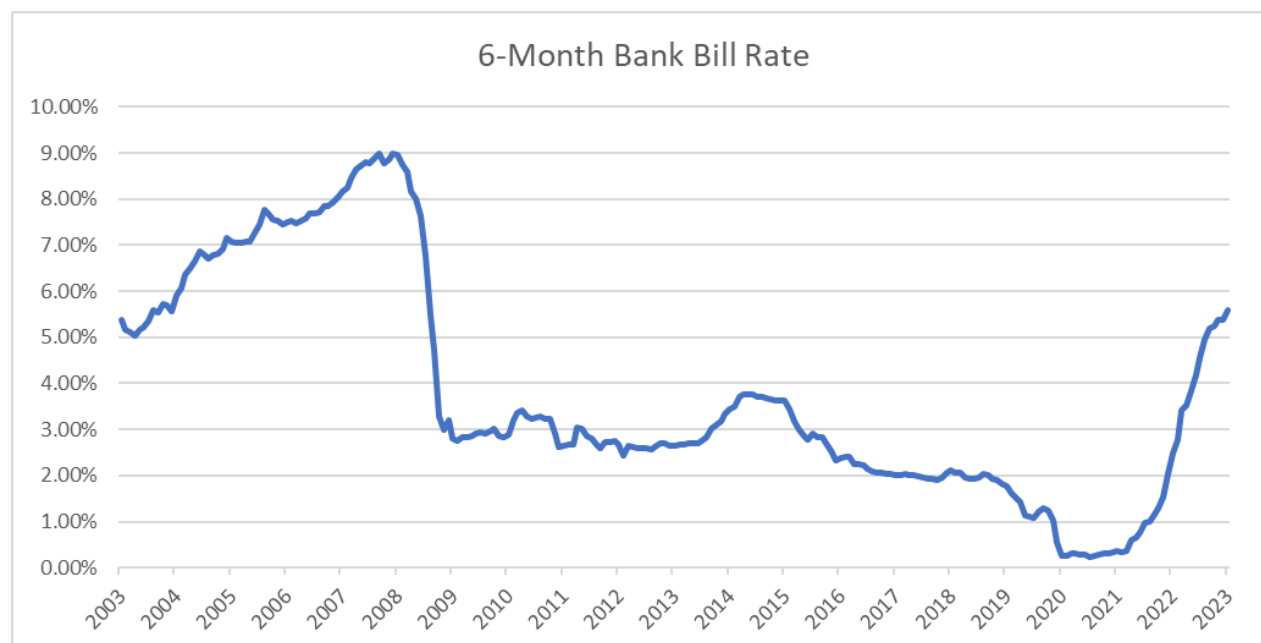
In local business news, One New Zealand (previously Vodafone) has signed a deal with Elon Musk's SpaceX, meaning its mobile network will work with Starlink satellites from late 2024. Meanwhile, 2degrees has announced a trial with satellite provider Lynk, allowing customers to connect from remote areas.

In housing, CoreLogic data shows NZ house prices fell a further 1.1% in March. Fletcher Building expects a 20% fall in demand for its homes, as soaring interest rates impact the cost of living. NZ banks are now stress testing mortgage applications at interest rates nearing 9%, with ANZ's test rate now 8.6%.

The biggest movers of the week ending 7 th April 2023			
Up		Down	
Arvida Group	5.38%	Serko	-8.37%
Sky Network Television	3.17%	Vista Group International	-7.91%
The Warehouse Group	2.16%	Pacific Edge	-5.81%
SKYCITY Entertainment Group	2.09%	KMD Brands	-2.73%
Vulcan Steel	2.07%	The a2 Milk Company	-2.40%

Investment Topic – How Bonds Work

While the current rising interest rate environment is not welcome news for borrowers, it does present an opportunity for savers to attract a higher return. In particular, those investors whose portfolios have become weighted too far towards shares, have an opportunity now to re-balance back to a level that more accurately reflects their risk profiles, without having to accept low returns on term deposits and bonds. The chart below shows the 6-month bank bill rate over the last 20 years, revealing the steep rise since late 2021.



Mechanics of a Bond

The key components of a bond are as follows:

1. The issuer: The entity that issues the bond, being a company or government.
2. The bondholder: The investor buying the bond.
3. The face value: The amount that the issuer pays the bondholder on maturity. This is also called the par value, principal, or nominal value.
4. The coupon rate: The interest rate that the issuer agrees to pay the bondholder, expressed as a percentage of the face value. The coupon rate is typically fixed, but it can be variable in some cases.
5. The maturity date: The end date of the bond, when the issuer must pay back the full face value to the bondholder.

When an investor buys a bond, they essentially lend money to the issuer in exchange for regular interest payments, called coupon payments, and the return of the principal amount on maturity. For example, suppose you buy a bond with a face value of \$10,000 and a coupon rate of 5%. This means that the issuer will pay you \$500 per year in interest until the bond matures. As the bondholder, you will receive coupon payments, typically semi-annually or quarterly, and then the \$10,000 principal amount on maturity.

Price of a Bond vs Interest Rates

If you buy a new bond, you pay \$1.00 per bond. Using the above example, you buy 10,000 bonds for \$10,000, and receive the face value of \$10,000 on maturity. However, you may sell your bond before maturity, and the price received will be influenced by current interest rates.

The price of a bond and interest rates have an inverse relationship, meaning that as interest rates rise, the price of existing bonds tends to fall, and as interest rates fall, the price of existing bonds tends to rise. For example, 2 years after you have purchased your \$10,000 bond paying 5%, you want to sell it before maturity. If interest rates in the market rise to 6% for similar bonds, then investors will be more attracted to new bonds paying 6%. In order to sell your bond, you will have to accept a lower price for the bond. For example, you might sell the bonds for \$0.97 per bond, meaning you receive \$9,700 for your bonds.

Yield to Maturity

For the purchaser of the existing bonds, they receive an effective rate of 6% on their investment, called the yield to maturity. The yield to maturity is the total return when taking into account the price paid. Importantly, the coupon payments and face value remain the same. The new purchaser will continue to receive \$500 per year, however on maturity they will receive the full face value of \$10,000. Because they only paid \$9,700 for the bonds, this \$300 capital gain pushes the total return of the investment up to 6%.

Investment News

Mercury (MCY.NZ) – Agreement with Amazon for Renewable Energy

Mercury has reached an agreement with Amazon for renewable energy for their Auckland data centres, planned for launch in 2024. Amazon will purchase around half the output of Turitea South, being the southern section of the Turitea wind farm, to support Amazon Web Services's (AWS) data centres. Having a guaranteed consumer buying a significant amount of the generation means that Mercury remains well positioned to continue developing renewable projects at pace.

Current Share Price: \$6.25, **Consensus Target Price:** \$6.25

Stride Property Group (SPG.NZ) – Update on Portfolio Valuation

Stride expects a gross revaluation movement for its directly held office and town centre portfolio of (\$39.1m), being a 3.4% decrease. The portfolio has a draft valuation as at 31st March of \$1.1b, with an expected average capitalisation rate of 6.0%, up 43bps from 30th September. The expected loan to value ratio is approximately 36%.

Current Share Price: \$1.29, **Consensus Target Price:** \$1.62

Spark (SPK.NZ) Releases Three-Year Strategy

Spark released its three-year strategy to FY26, which will focus on data centres, and new technologies to fuel growth in Spark's core markets and across its growing high-tech portfolio. The CEO cited tailwinds that include the continued exponential growth in data, acceleration of technology convergence, the return of international travel, and rising levels of immigration. The company will invest \$250m-\$300m in the high-growth data centre market and \$40m-\$60m in 5G Standalone. In mobile and broadband, Spark will leverage its data capability and 5G investment to deliver the latest digital experiences, personalised for its customers.

Current Share Price: \$5.04, **Consensus Target Price:** \$5.11

Scales Corporation (SCL.NZ) – Update and Revised Guidance for FY23

Scales advises that guidance for FY23 underlying net profit has been reinstated at \$14.0m-\$19.0m, following an assessment of the impact of Cyclone Gabrielle. Regarding the cyclone's impact on Mr Apple's crop and orchards, the current indications are that the FY23 crop will be down approximately 25% on the initial forecast for the year, and total tree losses are estimated at approximately 5% of the total planted orchard area, however due to expiring leases, only

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



50% will need to be replaced. The total cost of replanting should be no higher than the usual redevelopment capex programme.

Current Share Price: \$3.25, Consensus Target Price: \$3.90