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Yovich & Co WEALTH MANAGEMENT

Yovich & Co. Market Update

8th May 2022

As at 6th May	NZX 50G	All Ords	Shanghai	FTSE	Dow	NASDAQ	NZDAUD	NZDUSD	OCR
Previous Week	11884.30	7724.76	3047.06	7544.55	32977.21	12334.64	0.9143	0.6465	1.50%
Week Close	11609.38	7467.59	3001.56	7387.94	32899.37	12144.66	0.9054	0.6409	1.50%
Change	-2.31%	-3.33%	-1.49%	-2.08%	-0.24%	-1.54%	-0.98%	-0.86%	0.00%

Global equity markets fell last week due to global growth concerns surrounding the ongoing lockdowns in China and supply chain disruptions, with the NZ market falling 2.31%, and the Australian market falling 3.33%. The US market saw wide fluctuations, with the Dow eventually ending down 0.24% and the NASDAQ falling to further lows, down 1.54%.

The oil price climbed higher during the week, up 3.4% to US$113, with ongoing concerns around tight supply and the EU's proposed ban on Russian oil imports. Other commodities weakened however, with the prices of industrial metals such as aluminium and copper down heavily due to a softening demand outlook. Commodity currencies such as NZD, AUD and CAD were all down as a result, with the NZD falling 0.86% against the USD, which strengthened further as the DXY index reached a new high above 104.

Domestically, interest rates continued to rise rapidly, with the 3-month bank bill rate up 12.8% to close at 2.12%, and the 5-year swap rate increased by 3.24% to close at 4.06%.

The biggest movers of the week ending 6th May 2022				
Up			**Down**	
EROAD	8.28%		Air New Zealand	-10.17%
Manawa Energy (formerly Trustpower)	3.12%		Precinct Properties	-7.89%
Pushpay Holdings	3.03%		Stride Property Group	-7.07%

Economic News

In its latest monetary policy statement in February, the Reserve Bank of NZ spoke of NZ's robust economy during the lockdowns in 2021, supported by low interest rates and significant government support. Economic activity slowed during the second half of 2021, however not as much as anticipated, as people have adapted as best they can to ongoing disruptions. While conditions remain volatile, economic activity is expected the recover in the latter part of 2022 as borders re-open, however we are not expected to see tourists at pre-Covid levels for several years.

On the demand side, low unemployment and high prices for key exports (coupled with a lower NZD) will support both household consumption and business investment. However, the NZ economy is facing capacity constraints, with ongoing global supply chain issues coupled with scarce labour domestically, meaning this strong demand is leading to inflation rather than continued GDP (gross domestic product) growth. After annual inflation of 6.9% in the December quarter, inflation is expected to reach a peak in the March 2022 quarter, easing gradually from there towards the 2% target midpoint over the medium term. Overall, while monetary conditions are still supporting the economy, financial conditions are expected to tighten as the RBNZ lifts the OCR to deal with rising inflation, which will weigh on GDP growth.

Low Unemployment

The unemployment rate has declined to 3.2%, being its lowest-ever recorded level. Strong demand for labour has been partially unmet because of already low unemployment and ongoing border restrictions, limiting migrant workers. More firms are reporting labour as the factor most limiting production (other factors being capital, finance, materials, orders), and the reported difficulty in finding both skilled and unskilled labour remains near record highs. The effect of this tightness in the labour market is rising wage growth in nominal terms, however to date this has been outstripped by higher CPI inflation, meaning real wages have gone backwards.

House Price Inflation Starting to Ease

Nationwide house prices fell in December and January, with higher mortgage interest rates and tighter credit lending standards impacting housing demand. With high building consent numbers, the housing shortage is rapidly closing, especially with low migration. The expected influx of returning kiwis has not eventuated, and more likely we will see a brain drain to Australia, which offers higher wages and a lower cost of living. The RBNZ forecasts for house price growth to slow over the coming year, before declining about 9% over the next couple of years. This level of decline represents a minor reversal of large house price increases over recent years, and this view is consistent with market economists who expect a “soft landing”. A strong labour market is a key driver behind house prices not falling more dramatically, as potential house buyers feel more secure to buy with a stable income.

The effect on the economy from high house price inflation has been to support household spending, especially on long-lasting goods, for example couches, spa pools and the like. We can expect to see that type of spending pull back from previous levels as a result of lower house price inflation, which will assist the RBNZ in dampening the demand side of the economy.

More Government Spending

While the RBNZ is trying to dampen demand to get inflation under control, the government has signalled another expanded budget, targeting infrastructure. Given the significant capacity pressures in the economy, it will be very difficult for the government to achieve its infrastructure goals without just crowding out the private sector and causing more inflation and higher interest rates.

Overall Outlook

With economic growth being limited by capacity constraints, the robust demand that was caused by low interest rates, government support, and continued high employment, has resulted in rising inflation. Now that the RBNZ has pivoted from loosening monetary policy to support the economy, to tightening by raising the OCR for the purpose of price stability, we are seeing higher interest rates. This, along with other factors, has meant that house price inflation has eased, and this will have a dampening effect on household spending, which in turn will slow economic activity, leading to inflation being reined in, and GDP growth slowing.

Continued low unemployment will underpin robust demand in the economy, allowing the RBNZ to focus on price stability, with most forecasts being that the OCR will end up at just over 3% over the next year or so (currently at 1.50%). However, continued fiscal expansion by the government may exacerbate price and capacity pressures, potentially pushing out the timeline for the RBNZ to pull inflation back to its target range.

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Investment News

Trustpower (TPW.NZ) Changes Name to Manawa Energy (MNW.NZ)

Trustpower has sold its gas, telecommunications, and retail electricity supply business to Mercury, excluding the supply of electricity to commercial and industrial customers. The company has now changed its name to Manawa Energy. Manawa Energy has 26 power schemes throughout NZ and a total capacity of 498MW. Its commercial and industrial electricity business supplies around 680 customers nationally.

Current Share Price: $6.95, **Consensus Target Price**: $6.87

Mercury (MCY.NZ) Launches $200m Capital Bond Offer

Mercury has launched a $200m capital bond offer. The bond has a term of 30 years, with interest reset dates every five years. The initial interest rate has been set at 5.73%pa. The proceeds of the bond issue are intended to be used to refinance drawn debt relating to the Trustpower retail acquisition and for general corporate purposes.

Current Share Price: $5.75, **Consensus Target Price**: $6.49

ANZ Bank (ANZ.ASX or ANZ.NZ) – First Half Profit Up 20%

ANZ has released its first half year results, revealing statutory profit up 20% on previous corresponding period (pcp). The dividend announced of 72c is up 2c on pcp. The CEO cited positive balance sheet growth in Australia driven by improvements in home loan capacity, and strong home loan momentum in NZ delivering market share growth.

Current Share Price: AUD$26.76, **Consensus Target Price**: AUD$29.39

Kiwi Property (KPG.NZ) Gets Approval for Drury Development

Auckland Council has announced the approval of Kiwi Property's Drury Private Plan Change application, paving the way for the development of the company's 53ha site, which will be the location for the new Drury Town Centre. The development is expected to unlock thousands of houses and new jobs, and generate significant value for the company for years to come.

Current Share Price: $1.025, **Consensus Target Price**: $1.20

Channel Infrastructure (CHI.NZ) Announces $100m Bond Offer

Channel Infrastructure, formerly NZ Refining, has announced the offer of unsecured, unsubordinated, fixed rate bonds. The offer is for up to $100m, plus oversubscriptions of up to $25m at the company's discretion. The net proceeds of the offer are to be applied towards repaying a portion of the company's existing bank debt, and will also provide diversification of funding that aligns with an infrastructure business. The bond will be for 5 years, and the interest rate will be the swap rate plus an indicative margin of 1.80%-2.10%, subject to a minimum interest rate of 5.80% per annum. The offer closes on Friday 13th May.

Current Share Price: $1.08, **Consensus Target Price**: $1.16