

MARKET PERFORMANCE AND COMMENTARY – JANUARY 2021

MARKET PERFORMANCE

Index	Index Level/ Price	1 Month %	3 Month %	1 Year %
Global Equities				
MSCI Emerging Markets	772.74	3.8	18.7	27.9
S&P 500 (US)	3714.24	-1.1	13.6	15.2
Nikkei 225 (Japan)	27663.39	0.8	20.4	19.2
FTSE 100 (UK)	6407.46	-0.8	14.9	-12.1
DAX (Germany)	13432.87	-2.1	16.2	3.5
CAC 40 (France)	5399.21	-2.7	17.5	-7.0
Trans-Tasman Equities				
S&P/NZX 50	13127.29	0.3	8.6	12.0
S&P/ASX 300	73142.86	0.3	12.1	-2.7
Bonds				
S&P/NZX NZ Govt Stock	1923.88	-0.5	-3.1	2.8
S&P/NZX A Grade Corporate	5955.78	-0.3	-1.4	4.0
BBgBarc Global Aggregate Hdg NZD	428.79	-0.6	0.3	2.9
FTSE WGBI Hdg NZD	3718.35	-0.8	-0.5	3.0
Oil				
West Texas Intermediate Crude	52.20	7.6	45.9	1.2
Brent Crude	54.85	7.2	48.6	-2.6
NZD Foreign Exchange				
AUD	0.9393	0.7	-0.2	-2.8
EUR	0.5932	0.8	4.6	1.6
GBP	0.5248	-0.4	2.7	6.9
JPY	75.4537	1.5	9.2	7.6
CNY	4.6425	-0.8	4.9	2.4
USD	0.7207	0.1	9.0	11.4

Source: Nikko

Executive summary:

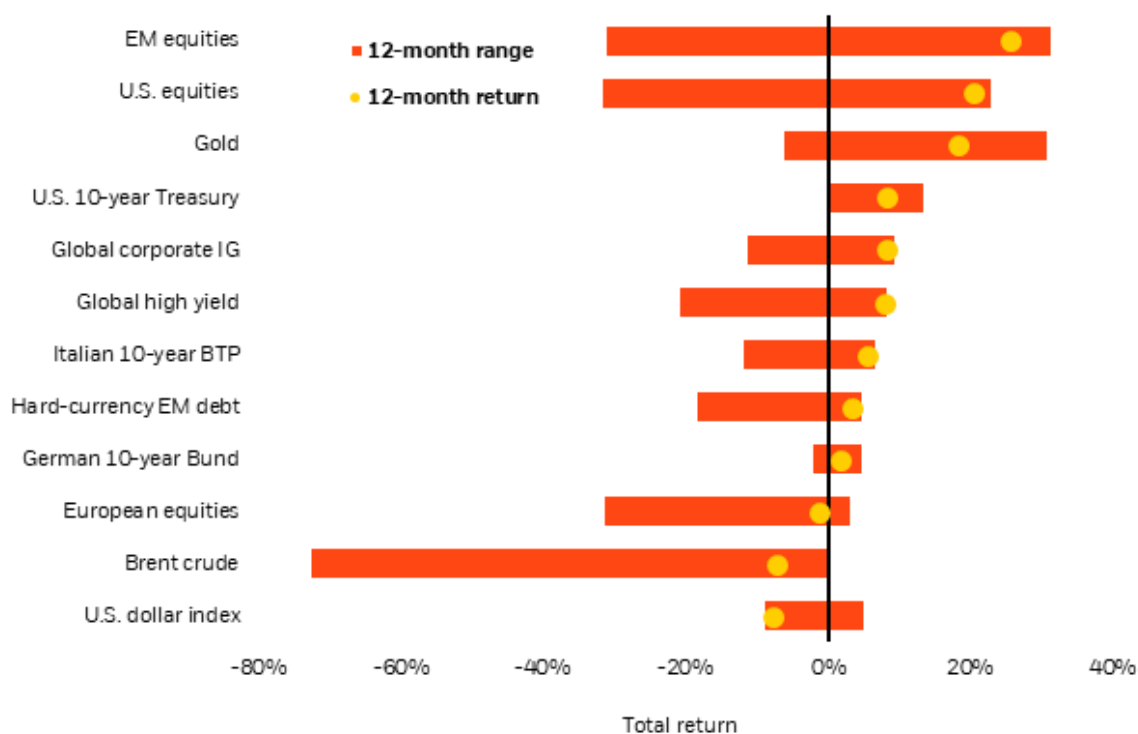
- Oil continues its trend higher
- Australasian markets slightly positive for the month; Europe and US negative; Japan and emerging markets positive
- Bond markets drop reflecting the rising interest rates
- Watch for increasing inflation

FINANCIAL MARKETS

In contrast to December, January has been volatile. It started with rapid growth, then slowed after Trump supporters stormed Congress, it then subsequently dropped due to a short squeeze caused by retail investors hitting back at hedge funds. The S&P500 index started rising towards the end of the month. One third of S&P 500 companies reported their last quarter earnings beat expectations by over 80%. The Fed improved their economic outlook and reaffirmed expectations for “low for long” rates. The ECB also has an optimistic outlook for 2021 and stated their willingness to continue quantitative easing.

Equity markets (except Europe) are the main benefactors of the current situation, due to the flood of cheap money driving equities to record highs. It’s noteworthy that 20% of all US dollars in circulation have been printed within the last nine months, which gives an idea of the weight of the Fed’s support.

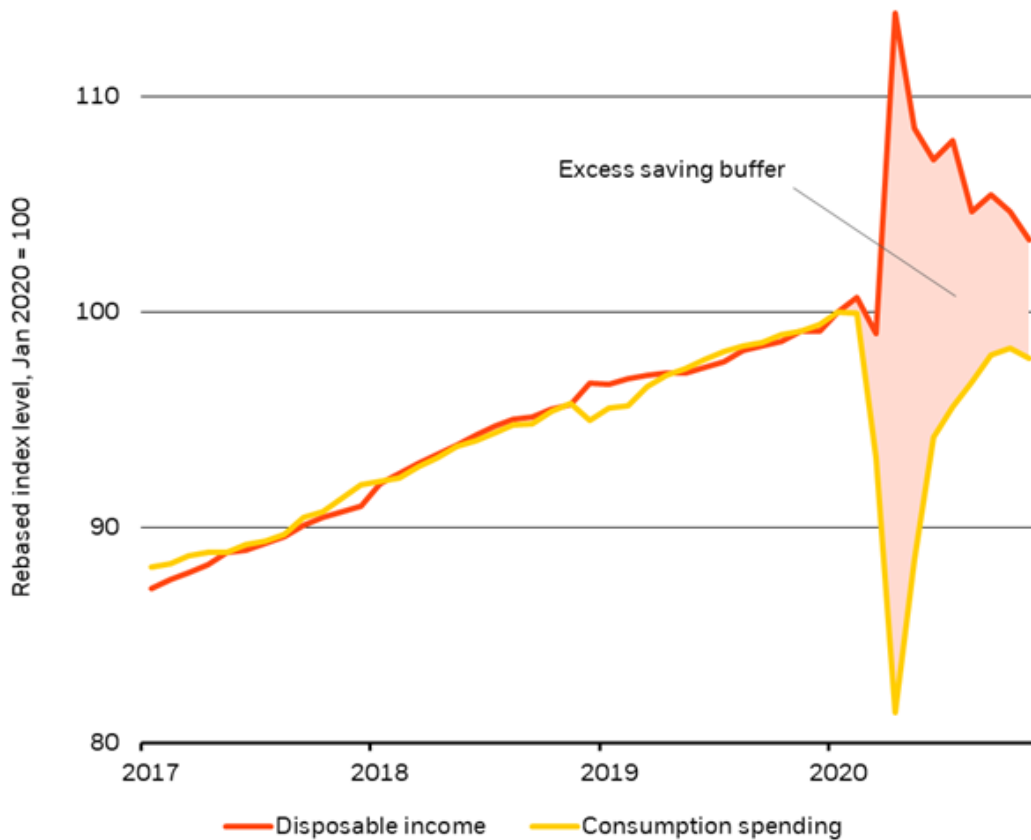
Selected asset performance in the past 12 months



Source: Blackrock

Many households in the US saved up a huge amount of US\$1.5 trillion so called “forced savings” during the pandemic. This money will go into the market once the restrictions ease. In combination with fiscal support announced by Biden of US\$1.9 trillion, we expect to see a continued appetite from both government and central banks to maintain support for as long as its needed.

U.S. income vs. consumption, 2017-2020



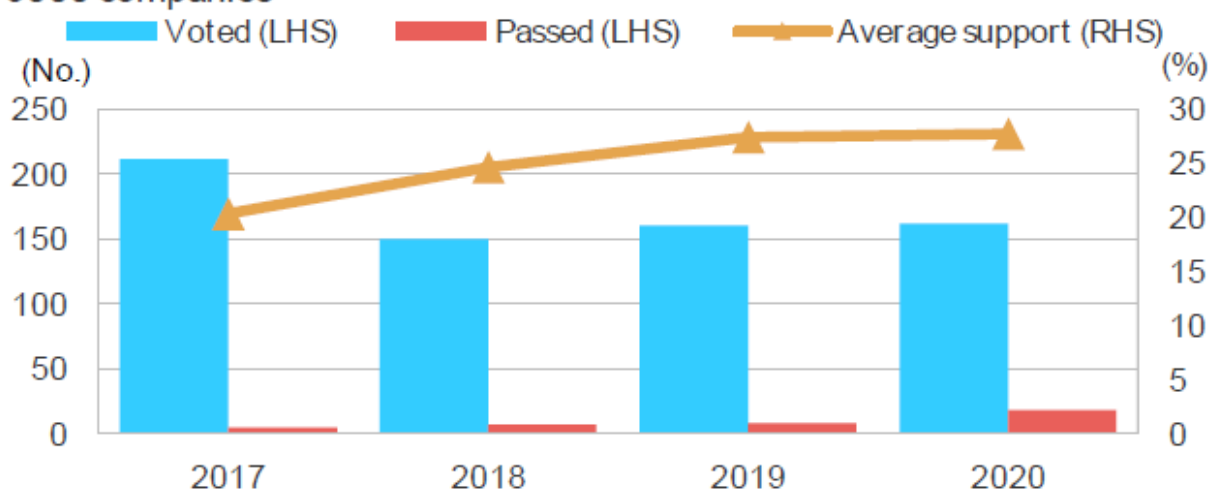
Source: Blackrock

The importance of Environmental, Social and Governance imperatives have been realised by governmental bodies. The European Commission has aimed to enhance the quality of ESG data as a result of the harmonisation processes and directed the need for sustainability reporting. The ECB is planning to implement climate change and environmental factors as part of their assessment followed by similar action from the central banks of France, England and others. More than one third of a €750 billion recovery package will be directed to green projects.

Environmental and sustainability considerations are already part of the strategic framework for many companies. The Georgeson 2020 annual governance review of Russell 3000 companies highlighted there were double the number of environment and social proposals supported by shareholders which is pleasing to see. Similar popular views are also reflected in New Zealand where the government recently started putting into action the need to become carbon neutral by 2050.

More Support for E&S Shareholder Proposals

Number of environmental and social shareholder proposals for Russell 3000 companies



Source: FitchRatings

NEW ZEALAND ECONOMY

There are signs of a global recovery in demand for consumer goods which is being led by China. Global trade volumes are now near pre-Covid levels.

The rebound in trade has been sudden and has caused a number of issues. Some supply chains are struggling to meet demand and global logistics have been strained, leading to container shortages in a number of ports. The impact of this has been felt by some importers who have faced an elevated price in order to secure some supplies.

This has boosted prices for commodity prices like dairy, forestry, and fruit. The predicted milk price forecast is now \$7.50/kg of milk solids, the highest level since the 2013/2014 season. Meat has not fared as well, as three of our main markets are Europe, UK, and the US - all of which are struggling to contain Covid.

The CPI surprised on the upside with an annual rate of 1.4%. However, this was due in part to some effects of Covid in certain areas. Whilst the market is predicting higher levels of inflation during 2021, these are likely to be seen as temporary by the RBNZ, so we probably won't see a hike in the OCR anytime soon.

Whilst NZ has come through the Covid outbreak better than most countries, the market (and RBNZ) was predicting an uptick in the unemployment rate to 5.6% from the current 5.3%. However, the real numbers showed a drop to 4.9%.

A surging housing market, increasing inflation and falling unemployment proved the actions of the Government and RBNZ were the right ones and will raise the question of whether any ongoing stimulus is needed.

GEOPOLITICAL

Geopolitical risks increased with US-China tensions around Taiwan and South China Sea. China made several steps towards claiming their sphere of influence. Chinese air forces including nuclear-capable bombers entered Taiwan air defence zone twice during late January. On 26 January China passed the legislation which allowed the coastguard to open fire on foreign vessels to stop or prevent threats. South Korea approved and budgeted the construction of homegrown aircraft carriers to attempt to gain leverage against China.

The Biden administration re-established its interest in Libya and Syria where main players were previously Russia and Turkey. Also, Biden has been a strong supporter of intervention in Afghanistan and Iraq which may indicate a high possibility of new military operations, particularly in the Middle East.

Turkey is increasing their weight on the global arena with recent success in the Nagorny Karabakh conflict where they supported Azerbaijan against Armenia and Russia. Azerbaijan finally got control over the Nagorny Karabakh region which had been occupied by Armenians since the early 1990s. They used Turkish air drones, the Bayraktar TB2 UAV which was effective against the Russian Orlan-10 UAV. Turkey was able to help resolve this conflict by providing these powerful drones to Azerbaijan. Interestingly, Ukraine also increased the number of Turkish drones it holds, likely as a result of Azerbaijan's success, which may provide leverage against the Russians as they continue to occupy territory in the Ukraine.

GAMESTONKED

Until recently most people had not heard of GameStop (in NZ, EB Games is owned by GameStop). However, unusual moves in the stock market have made headlines beyond the world of finance, particularly in respect of GameStop Corp., which at one point was up 2,000% in less than a month. This was driven by retail investors, who used online forums like Reddit's WallStreetBets to organize a concerted push at the expense of hedge funds who had shorted the stock.

While short squeezes are not new, these recent moves have captured the popular imagination, as a number of hedge funds who had placed significant bets against these companies were forced to close out their short positions or secure injections from other funds to avoid closing shop. With GameStop, the hedge funds may have miscalculated (or mis-timed their shorts) as the online forums had been discussing how they felt the stock was underpriced before Xmas when trading at \$5 per share. Hedge fund losses ran into the billions.

As John Maynard Keynes famously said, "The market can stay irrational longer than you can stay solvent."

But no matter how this finishes (likely with some retail winners but also a large number of losers), the market is forever changed. At any point, a large flash group of retail investors can throw the market out of kilter for days if not weeks on end.

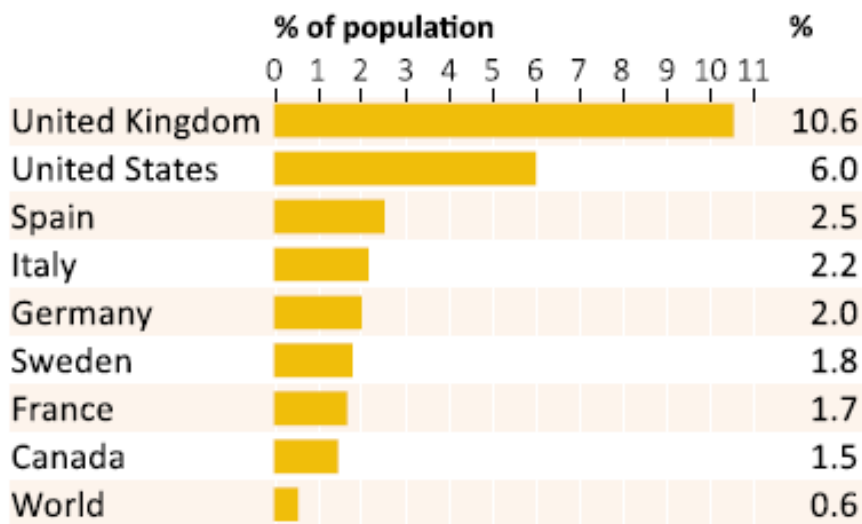
COVID-19 PROGRESS?

A couple of months have been passed since the first vaccines were approved for use. We know that less than 1% of the world's population has received one dose (noting, some vaccines requires two doses). However, it is pleasing to see the UK making the most progress with approximately 10% of vaccines administered. We

understand there would need to be at least 60% of the population receive the vaccine to potentially start having any herd immunity impact, which would indicate we are a long way off at this point.

New Zealand secured enough doses for vaccination of 5 million people, however, roll out will start not until mid-2021. The lion's share of secured deals is with AstraZeneca, while Pfizer received conditional approval so far.

COVID-19 Vaccination - received one dose



Source: ourworldindata.org

To play devil's advocate, we should consider the situation where, either:

- The current vaccines become less effective against new strains of the virus; or
- The vaccines that require two doses are not administered in the appropriate timeframe, minimising the efficacy of immunity protection.

The impact of such a scenario would be significant on the markets because much of the current optimism propelling them forward is based off an eventual vaccine rollout. We must prepare for the possibility this might not happen as we expect it to and how the markets would react when there is widespread realisation of this fact. Prime Minister Jacinda Arden stated we may not be travelling outside NZ, Australia and the Pacific until 2023. Our view is that this could be longer and a 3-year horizon more realistic.

SOCIAL UNREST

Social inequality is shifted from just poor and rich levels to having access to vaccines and not, and included in supply chain and not. The pandemic accelerated the transformation of the world to bipolar US-China order and disrupted supply chains. The political aspect ruled out the economical in rebuilding supply chain that negatively affected all resource suppliers over the world.

We are concerned the Game Stop saga is a reflection of inequality and division in the United States. It could be viewed as another proxy example for the growing split in the haves and have nots in America, which is

another piece of evidence pointing to the fact, America is severely divided on wealth inequality, values and political views, maybe more so than any other point in history. As such, tracking these micro examples should continue because if discontent with the current capitalist and political paradigm continues to spiral, there will be a civil unrest.

MARKETS OUTLOOK

