

New Zealand Equity Monthly October 2021

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By Stuart Williams, Head of Equities

New Zealand equities have lagged developed peers in 2021

The New Zealand stock market has been flat in the calendar year to date, with companies working to adapt to a number of risk factors. This puts it in stark contrast with markets in the rest of the developed world, which have seen gains ranging from 10% to 25%. The Australian market, for example, has risen by approximately 12%. Furthermore, New Zealand equities struggled in October, with the market seeing a month-to-date drop of about 200 points towards the end of the month.

Companies adapting to policy developments and other risks

Of the risks New Zealand firms are currently responding to, the most significant are related to government policy. Recent developments in this area include the government's push to reform New Zealand's three water services (drinking water, waste water and storm water) by transferring control of them from local councils to four publicly owned entities, the phasing out of the right to deduct mortgage interest on rental properties from taxes, and the continuation of pay restraint for public sector workers such as healthcare professionals. The slow pace of the country's COVID-19 response has created further difficulties. Staffing shortages are also continuing to bite, particularly in sectors such as nursing, retirement, agriculture, construction, infrastructure and technology. Companies are handling these challenges by being adaptive and seeking further ways to generate high returns.

Inflation may be more persistent than previously thought

Transitory inflation may be more persistent than previously hoped for given continued supply chain issues and high raw material prices. Continuing wage inflation underpinned by an increase in beneficiary payments as well as pay equity and minimum wage mandates is also likely to feed into prices. The companies most likely to thrive in this environment, in our view, will be those with pricing power, solid operating margins and the pricing discipline to have captured and embedded inflationary gains in the past. Strong technology will also be important.

Housing market likely to prove resilient

Although the hike in New Zealand's Official Cash Rate by a quarter of a percentage point to 0.5% on 6 October has implications for housing and other such sectors, housing market growth looks likely to level off rather than collapse. One factor supporting the market is the government's granting of residency to migrants through the one-off 2021 Resident Visa scheme, which will provide a simplified pathway for eligible temporary visa holders to settle in New Zealand permanently. Furthermore, housing market resilience is particularly important for the retirement sector given that embedded House Price Index gains seen during 2021 have significantly enhanced retirement village unit affordability for the time being.

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