Dear Client

The Half Time Score

Investment Markets

The last two years have been very difficult for investors. Covid struck and caused a severe downturn, then Governments overreacted by flooding economies with money to reduce the chance of recession. This caused inflation which in turn required central banks to dramatically raise interest rates, which has reduced growth.

Last calendar year, New Zealand shares were down 12.0% and world shares declined 18.0% - the biggest falls since 2008, while house prices slumped 14.2%.

Conservative assets investments also had a tough time, with New Zealand corporate bonds falling 5.1%.

Normally we are at least partially insulated by falls in share markets in that bonds will off-set much of the decline. We need to go back to 1994 to find a time that shares and bonds were both down in a calendar year.

Against that backdrop, this year had looked set to be another challenging one, with slower economic growth and more interest rate hikes expected to pressure markets.

However, it hasn’t been too bad at all.

At the halfway point, world shares are up 10.6% in 2023, having rebounded 21.7% from the lows of October last year. New Zealand investors have seen their returns from overseas shares boosted further by a falling NZ dollar.

The NZ share market has been more subdued than most, but the NZX 50 index is up slightly this year and up almost 10% above its low point from mid- 2022.

Bonds, have also been positive, with the NZX corporate bond index rising solidly.

A lesson we can take from the last six months is to stay invested, even when there’s reason to be nervous. It would’ve been tempting to head for the hills after a year like 2022, but those who’ve stayed the course have enjoyed a healthy rebound.

Outlook

We can look ahead with optimism.

Inflation is coming down; supply chains have improved and labour shortages are reducing. Central banks in New Zealand and the US have almost done enough to tame inflation, even though they have more to do in the UK, Australia and Europe.

This bodes well for bonds, which prosper when interest rates stop rising, as well as during periods of economic uncertainty.

For share markets, it's more difficult to predict whether the buoyancy of the first half will continue. Leading economic indicators suggest weaker activity ahead. Some would argue that markets are forward looking and this uncertainty is already in the price, while others will point to the fact that we haven't felt the full effects of the steep rise in interest rates.

On the positive side, US shares have been up in 52 of the 73 years since 1950, which makes for a hit rate of about seven out of ten. Again, since 1950, there have been just three occasions where we've seen two negative years in a row, the last being in the early 2000s.

What's more, a positive first half of the year for the share market has been followed by a positive second half on 76% of occasions.

These facts mean that a cautious approach shouldn't mean staying on the sidelines completely.

History shows that there is a good chance of the recent trend continuing in the second half of the year– and the case for bonds is particularly strong.

As always please let me know if you want to discuss your investments or want to review your portfolio.

Best regards

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