Greytown Trustlands Trust

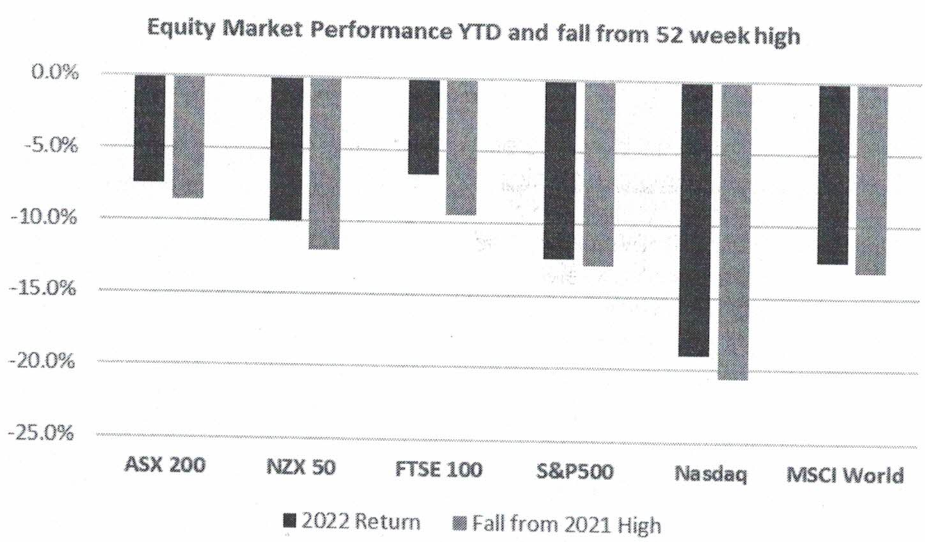
From: Jake Olsen <jake.olsen@craigsip.com>
Sent: Wednesday, 9 March 2022 12:49 PM
Subject: Investment update and market comments

Good afternoon

Markets remain on edge as Russia's invasion of Ukraine combined with ongoing concerns around inflation and the path of interest rates continue to create volatile conditions. It is extremely difficult (if not impossible) to predict how the war in Ukraine will develop from here, or the flow-on effects of the associated sanctions and shortages.

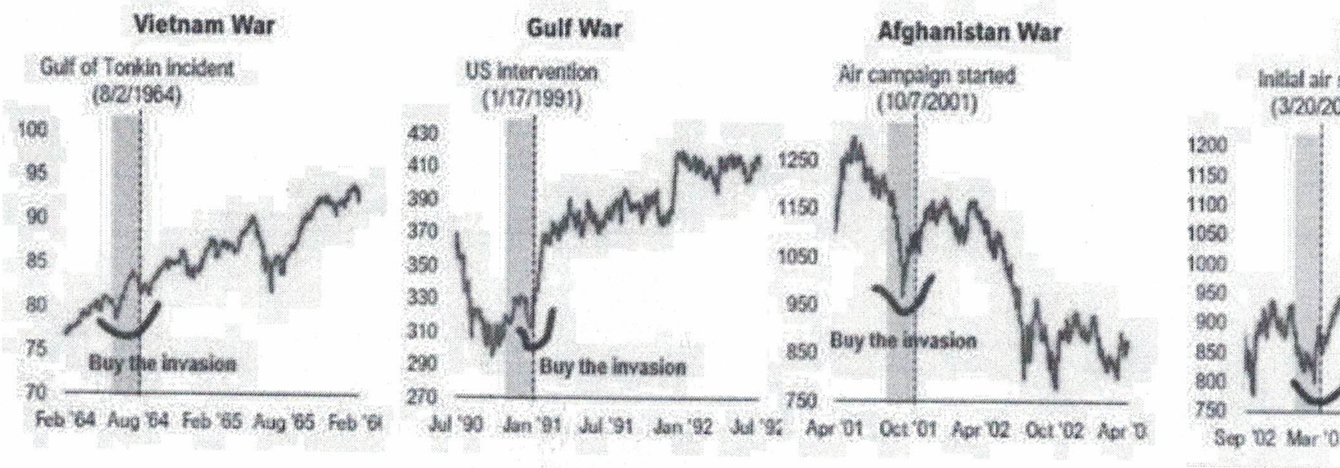
Market comments

- We expect continued volatility and downside risk to equity markets if the Ukraine invasion continue or escalates further.
- Assuming an eventual resolution of some sort and an end to the military conflict, this could prove an attractive buying opportunity at some point. Most geopolitical events don't have long-lasting effects on financial markets, although it is extremely difficult to judge how this might end
- While we have some short-term caution, we retain our constructive 12-month outlook for domestic and global equities. Our positive 12-month view is premised on the prospect of an extension of the current phase of above-average growth for both the global and domestic economy. This should continue to support the global and domestic earnings cycle, which was emphasised in the recent US earnings season as well as the NZ/AU earnings season results.
- In addition, global monetary policy remains highly accommodative. Policy is set to tighten but is far from neutral, let alone approaching restrictive levels. We see this as a supportive base for risk assets
- Most markets have reached 'correction' territory (figure below) – meaning they have fallen 10% from their 52-week highs. In a lot of instances, certain high-quality stocks are further off than the index, which is creating some attractive entry points for long term investors.



Russia/Ukraine – *unlikely to derail the global expansion*

- We expect the war in Ukraine to stay within its borders and therefore not have a significant impact on global growth or a major incremental impact on market risk premia.
- The US and UK/EU have levied significant sanctions centred on the Russian banking/financial system. Although they have not halted Russian energy exports, which would risk a recession in the highly dependent European economy. Europe receives close to 40% of its gas supplies and 25% of its oil supplies from Russia – so Western leaders are unlikely to pull the energy sanctions lever
- The historical precedent stemming from most major conflicts is they typically do not have a long-lasting impact on asset market performance (see chart below). On this basis, we may already have seen the lows in risk assets; however, a quick resolution in respect of this conflict appears unlikely



Inflation / Interest rates

- The outlook for inflation and interest rates still appears to be the main risk factor for equities at this juncture. While the inflation pulse is global, pressures appear most acute in the US. The response of the US Federal reserve will be critical for global asset markets
- The Russian invasion of Ukraine has seen the US rates market reduce the expected pace of Fed rate hikes and take the chance of a 50bps start to the tightening cycle in March to virtually zero. This was ratified by comments by Fed Chairman Jerome Powell this past week. We believe the projected interest rate path is reflected in current prices.
- Our read on the US economy at present is that it is expanding at a very robust clip, and we expect it can withstand multiple rate hikes over the coming year. Market pricing of 6-7 rate hikes in the space of the next 12 months is now looking too aggressive in our view.
- The US reporting season was strong with the majority of companies beating earnings estimates with positive outlook commentary. Corporate America is expected to take advantage of volatility by increasing buybacks by 12% to $1 trillion in 2022 according to a recent forecast by Goldman Sachs – this is a positive signal to the market.
- We expect there will be enough fading in inflation pressures over the coming year to keep the Fed on a moderate tightening path. Equities should be able to move higher into a gradual tightening cycle over the next 12 months as they have in many previous cycles

Key Takeaways

- Investors have a significant wall of worry to confront at present. This is nothing new in the grand scheme of market dynamics, although uncertainty is undoubtedly higher than average at present
- Importantly, equities are still supported by a strong global and domestic economy. The Russia Ukraine conflict has not as yet caused enough economic and financial stress to sway us from an upbeat view on global growth
- Inflation and the path of the Fed is still the key risk factor, though for now, monetary policy remains in a very supportive position. Our assessment is that the Fed will proceed relatively gradually, and the US economy is more than strong enough to cope
- We remain alert to the risk that inflation proves stickier than we and the markets currently anticipate
- We construct portfolios to optimise the downside protection from periods of volatility like these
- Many economies have removed Covid restrictions including the US, Australia and UK which provides a strong positive outlook for the recovery in 2022 and beyond
- NZ continues to have restrictions which is causing short term issues around services; in particular couriers, food supply, building products etc
- We believe the lowering restrictions caused by covid measures may lead to less supply chain disruption later in 2022 and therefore may see the path of inflation pull back to a more normal level

Given the recent volatility and fall/correction in equity markets, we reiterate our position that we believe equities will deliver superior returns over the medium term, however it is important at this juncture to ensure your asset allocation is appropriate and we will be in touch if any adjustments are necessary.

As always, if you have any questions specific to your portfolio or markets in general, do not hesitate to let me know

Regards