Market and Economic Review
November 2021

Divergence

October performance saw largely positive returns but with significant divergences. Higher risk growth funds saw some strong returns whilst lower risk funds fell in the month. This is all down to the rebound in share markets that came alongside some sharp falls in bond markets, particularly in Australia and New Zealand.

Investors started the month nervously awaiting US company 3rd quarter profit announcements. The outcomes were better than expected with aggregate profit margins largely immune to rising input costs. Large technology companies were standout performers, particularly Microsoft and Alphabet (Google's parent) whose stocks rose 17.6% and 11.3% respectively. Broadly strong profit announcements helped propel global shares up 5.5% in October.

Local Australian and New Zealand share markets were more muted, ending the month down 0.1% and 1.3% respectively. The prospect of higher interest rates is weighing on these markets but there are still opportunities for outperformance through stock selection. We had reduced exposure to the weaker iron ore space whilst bank stocks are one sector that can benefit from a rising interest rate environment.

It was bonds that saw outsize moves in October. Investors are questioning the need for low interest rate settings as global inflation surges. This has led to large moves in investor pricing of interest rate hikes over the next couple of years and bond prices have suffered accordingly. Investors currently expect NZ interest rates to rise by almost 2% over the next 12 months. We think interest hikes of this magnitude are unlikely and for the first time in several years, some bond investments are now starting to look a little more attractive.

Strong global share markets are masking what is a very complicated outlook. If central banks do indeed hike rates like markets expect (which is not a given) then this will be a significant headwind for the global economy and share markets. On the other hand, if central banks do not raise rates then the global economy could boom, leading to more bond market volatility. Milford funds have plenty of flexibility to allow us to try and navigate this environment and we continue to find attractive investment opportunities.

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