

Market and Economic Review

December 2021



Omicron the headline, interest rates remain the real story

November returns were impacted by the emergence of a new Covid variant, 'Omicron', which derailed global markets in the last few days of the month. Funds ended the month modestly lower. While the market response to this known risk was relatively short lived, this has nonetheless been a poignant reminder that new variants will be a feature of the investment landscape for some years to come.

The key to the outlook for financial markets is how central banks will respond to elevated inflation. Sharp rises in interest rates have the potential to upset share markets, bonds and a host of other assets. Fortunately, central banks seem to be in little hurry to meaningfully tighten policy, although there are signs the mood is shifting. The RBNZ raised rates by 0.25% in the month but some investors had expected even more. Whilst Australian and US central banks are being more patient, inflation is not going away, and this will keep the pressure on these central banks to hike.

November delivered a wide range of outcomes for our stocks, but healthcare companies were a standout. Fisher & Paykel Healthcare continues to be a significant Milford holding; last month they

announced good results and foresee ongoing strong demand for their products. The result sent the shares up 6.8%. In Australia, property companies Goodman and Charter Hall Group had a strong month, up 12.7% and 11.5% respectively. NZ shares were broadly weaker with the NZX 50 Index down 2.9% as investors anticipated higher interest rates.

Even with the emergence of Omicron, the global growth outlook likely remains strong as economies continue to rebound after last year's sharp recession. But moderately high valuations of shares and rising interest rates temper our expectations for returns. The next 12 months are likely to see higher levels of volatility in share markets even if broad returns are expected to be positive.

Given the complex outlook, Milford funds have pared back some share market exposure whilst adding back some bond exposure in NZ and Australia. This takes our exposures back towards a more neutral setting whilst we await clearer opportunities and greater certainty about the outlook.

Milford Asset Management

Level 28, 48 Shortland Street, Auckland, 1010
Phone: 0800 662 345
Email: Info@milfordasset.com
milfordasset.com



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