Fisher Funds Market Insights

March 2023 Quarter

Contents

Contributors this month

Ashley Gardyne
Chief Investment Officer

Matt Peek
Portfolio Manager

Robbie Urquhart
Senior Portfolio Manager

Sam Dickie
Senior Portfolio Manager

David McLeish
Senior Portfolio Manager

A buoyant start to the year for investors

Ashley Gardyne, Chief Investment Officer

Despite markets experiencing banking-sector-inspired drama last month, both equity and bond markets reported solid gains in Q1 of 2023. Performance across our strategies was strong after a challenging 2022.

So far in 2023 our theme of "a bumpy road, but a better destination" seems to be playing out, with both equity and bond markets rallying in Q1.

A better start in 2023

Equity markets had a buoyant start to the year despite ructions in the banking sector. The MSCI World Index gained 7.3% for the quarter – with most geographies higher (including the US, Europe, New Zealand, and Australia) and technology-heavy indices like the Nasdaq Composite (+16.8%) making the biggest moves.

Finally, some good news arrived for fixed-income investors. Last year's rapid rise in interest rates set investors up for a better start to 2023, and key bond market indices have gained around 3% so far this year.

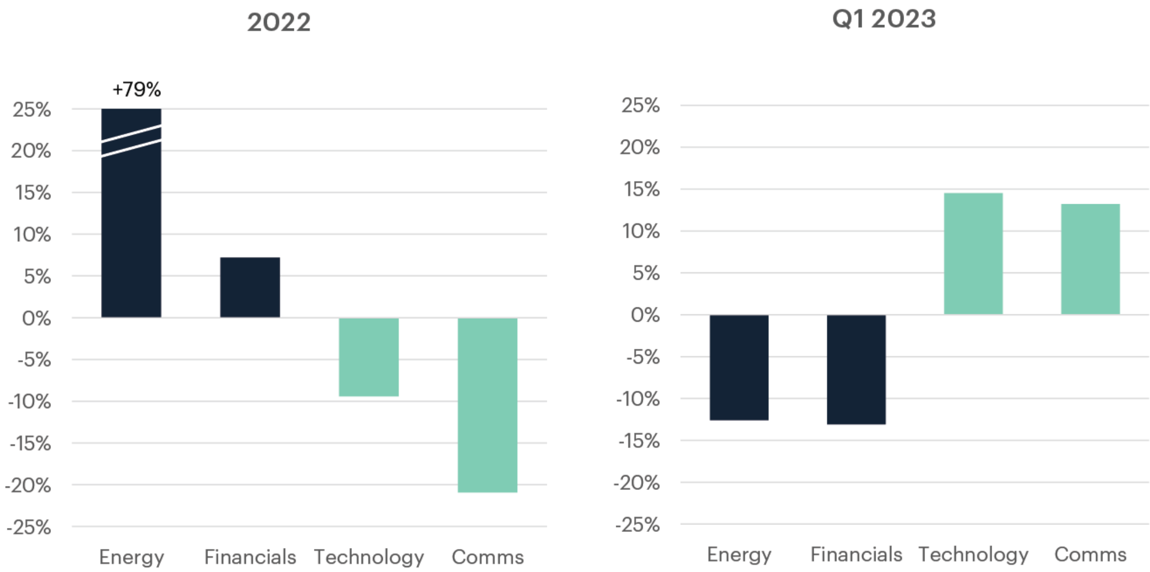
The failure of Silicon Valley Bank (SVB) provided an unwanted flashback to the US subprime crisis in 2008 and led to rapid deposit outflows at a number of otherwise sound banks – like Signature Bank and Credit Suisse. The failure of SVB and Signature Bank caused regulators to step in and protect depositors, while also providing substantial liquidity to the broader banking sector. These interventions seem to have mitigated the risk of contagion for the time being. Also providing comfort to both depositors and regulators is the fact that the banking sector is in significantly better shape compared to the Global Financial Crisis (from a credit quality, liquidity, and capital adequacy perspective). After initial banking-inspired declines in early March, markets closed the month back at their highs.

Q1 witnessed a reversal of many 2022 trends

A lot was going on beneath the headline moves in market indices this quarter – with the start of 2023 reminding us of the over-reaction and reflexivity often present in markets.

Last year, rising interest rates and inflation led to the outperformance of banks and energy companies, while technology and other growth companies generally underperformed. But the consequences of these rising interest rates, such as slowing growth and banking sector stress, have in turn caused interest rates and energy prices to reverse course and fall from their highs, hitting banks and energy companies in 2023.

Chart 1: Sector performance goes into reverse



Source: Bloomberg
Note: Comms Services include large technology companies like Google, Meta, and Netflix.

The share prices of many technology companies were hit hard The share prices of many technology companies were hit hard in 2022, due in part to rampant expense growth and slowing revenue growth (after the COVID-driven surge in demand). Many of these companies have now rebounded strongly, responding to cost pressures and weak share prices by reducing headcount to lift earnings. Meta, Microsoft, and Salesforce are good examples of this.

Other tech companies have responded by pulling growth levers. Netflix, for example, reacted to the slowdown in subscriber growth by offering an ad-supported tier, which is now seeing new users join the platform for the first time. We prefer businesses with options – be it growth levers, pricing power, or high incremental profit margins – over those highly exposed to factors outside their control, like interest rates and commodity prices.

Chart 2: Big tech driving market gains in 2023

Source: Goldman Sachs

Looking forward, rather than reacting to last year's news

Rather than reacting to last year's trends, it's important to reflect on, and position for, potential consequences of the current environment and policy settings.

What could be the next domino to fall due to interest rate hikes by central banks? Could we see cracks in the commercial real estate market? Highly indebted listed companies having to refinance at much higher rates? Or tightening credit conditions hitting small businesses? Or perhaps we need to consider where to invest geographically: with the New Zealand domestic economy being more at risk than the US due to the nature of our housing and mortgage market.

In recent months we've been actively reviewing our exposure to these sorts of risks and repositioning our portfolios where appropriate. Focusing on high quality companies, with low leverage, and options at their disposal to manage costs and drive growth is always important – but especially so in an environment of heightened economic uncertainty.

While we're taking a cautious approach to which companies we select, when we look at the businesses we own, and the investment opportunity set more broadly, we're optimistic about the medium-term and long-term outlook for our portfolios. As we have recently witnessed, markets typically climb a wall of worry. And when the list of investor worries is long, potential returns are often at their highest.

Weathering the storm

Matt Peek, Portfolio Manager, New Zealand Equities

2023 began with unprecedented weather events in New Zealand, and turbulent markets globally, but our portfolio has weathered the storm relatively well.

Cyclone Gabrielle had little impact on companies in the portfolio

During the quarter, Cyclone Gabrielle tragically impacted the country, particularly the eastern North Island. But this had no major impact on companies in the portfolio.

Delegat experienced minor surface flooding at its Hawkes Bay winery and one of its vineyards. However, there was no silt residue, damage to vines, or impact on the coming harvest.

Meridian's Harapaki wind farm development is being impacted by damage to transmission lines and road access. The site itself is still being assessed but at this stage any damage appears manageable.

Freightways flagged a limited impact on its business due to lost revenue and additional costs from using alternate routes.

From Xero to hero

After a disappointing share price performance in 2022, Xero was the strongest performer in the portfolio with its share price up +27% over the quarter.

In late 2022, many global tech companies reduced their staffing numbers to focus on profitability, with high-profile workforce rationalisations at Amazon, Google, and Microsoft.

Xero followed suit in March after new CEO Sukhinder Singh Cassidy (only months into her role) outlined plans for how the company will reduce its global workforce of around 5,000 people by 15%.

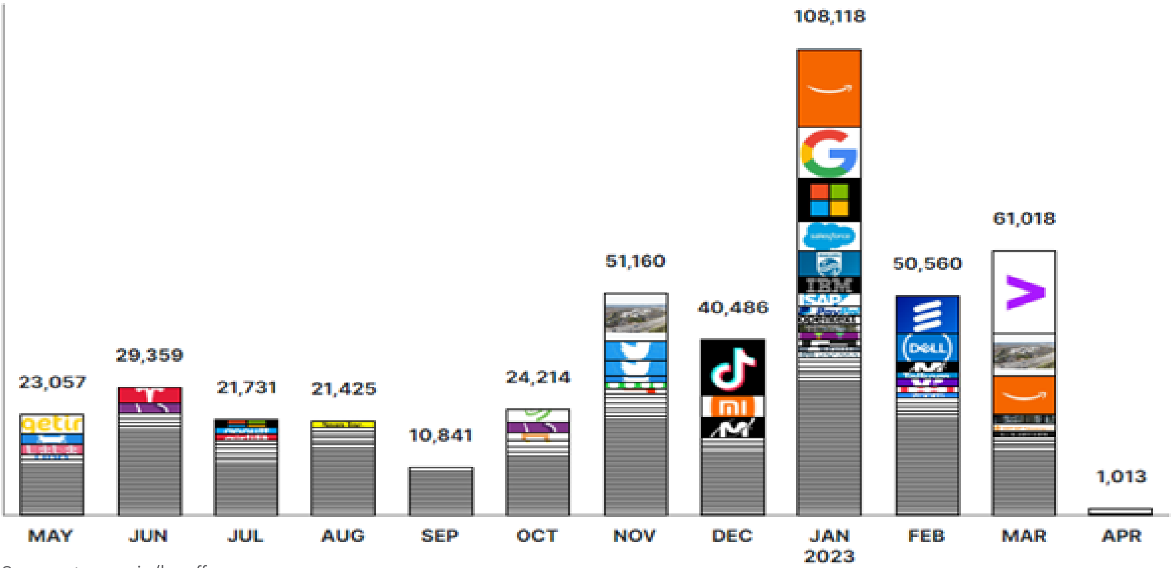
Like many tech companies that rode the wave of positive market conditions in the wake of COVID, Xero had recruited a large number of new people as it sought to enable future growth.

However, the company had grown faster than its business. It had also diluted its focus by casting the net too wide instead of focusing on strategic priorities. The new CEO plans to "streamline and simplify" the company's teams and she cited several roles that have duplicate responsibility. The company will be more efficient and effective with leaner teams.

Xero is seeking a "better balance of growth and profitability" moving forwards and has already indicated its earnings for the new financial year will be a greater portion of its revenue.

Globally, tech layoffs that began in late 2022 have accelerated in 2023 (see the graph below).

Chart 1: # of Tech Employees Let Go (as at 4 April, 2023)



Source: trueup.io/layoffs

Ryman Healthcare strengthened its balance sheet

In February, Ryman Healthcare raised $902 million of new equity at $5.00 per share to reduce its debt levels. After Ryman revealed an unexpectedly large step-up in debt in its half-year result in November, we had anticipated the equity raising and reduced our shareholding at higher prices.

We took up our entitlement to buy new shares at $5.00, as the company has taken the first steps to set itself on a more sustainable growth trajectory. The long-term economics of the business model remain compelling, although our position size remains smaller than previous years until we get more confidence in management's execution.

Ryman provided an update on its development plans, with progress slowed or halted on high intensity sites such as the one in Takapuna. Development will slow in the near-term to ensure a sustainable growth path and lower peak debt levels. Ryman announced a medium-term gearing (debt to assets) target of 30–35%, with the new equity reducing gearing from 43% to 34%.

We fought for a better outcome in the Pushpay takeover battle

In April 2022, Pushpay's board had received approaches from several parties interested in potentially acquiring the company. From the outset, cornerstone shareholder Sixth Street and private equity firm BGH held around 20% of the company and were clearly in the box seat as they could effectively block any other party from doing a deal.

Unfortunately, Pushpay's board recommended the initial $1.34 per share low-ball offer by way of scheme of arrangement in October 2022. Generally, we remain dubious about schemes of arrangement, where, due to the 75% threshold, a substantial minority can be forced to part with a company despite rejecting an offer. The 90% takeover threshold is there for a reason – to ensure companies are only taken private at compelling valuations – and we would prefer to see directors avoid lowering the bar by readily agreeing to go down the scheme path.

At this point, they had already sought feedback from institutional shareholders around where they viewed fair value. So, it should not have been a surprise that many shareholders (us included) would have not entertained an offer that low.

Pushpay shareholders voted in March to see whether the company would be taken private at that price. We voted against the offer, against the directors' recommendation, because we thought it did not sufficiently compensate shareholders. This would also pressure the bidder to dig for a better offer. Fortunately, enough other shareholders did the same that the scheme vote failed.

To its credit, the bidder then made a revised offer of $1.42 per share. Fisher Funds and several other key institutional investors enabled the higher offer to be brought forward by agreeing to vote in favour of the scheme at the new price.

Pushpay is the leader in its sector and has an appealing runway for future growth, but several questions remain for investors. Growth has slowed and it has changed its 'go-to-market strategy' repeatedly without a satisfying explanation for why it hasn't worked.

Overall, Pushpay still has a bright future, but it is not without risks. Through this process, we have new doubts about whether the board have the appetite to work hard to get the best out of management and drive value creation for shareholders over time.

For these reasons, we have agreed to accept the $1.42 offer: the certainty of a bird in the hand.

A good start to the year – clouds on the horizon for consumers

Robbie Urquhart, Senior Portfolio Manager, Australian Equities

The Australian Equity Fund has had a strong start to the year, helped by lower interest rates, rebounding economic activity in China, and a resilient earnings season.

Along with share markets around the world, the benchmark ASX200 index (70% hedged into NZ$) has started the year positively, rising +3.6% in Q1. The unexpectedly speedy re-opening of China's economy post-COVID buoyed commodity markets and supported a broad increase in mining company share prices in Q1 (a large constituent of the Australian share market).

Additionally, further signs suggest that the post-pandemic increase in inflation may have reached its zenith and is beginning to subside. Australia's inflation rate fell from a peak of 8.4% in December 2022 to 6.8% in March 2023. Coupled with turmoil in parts of the global banking sector (sparked by rapidly rising interest rates), the market has sharply reduced its expectations about how much further central banks can go in hiking interest rates this cycle. This has seen interest rates fall from recent highs. The Australian 10-year Government bond yield fell from 4.05% to 3.3% over Q1.

Resilient results in Q1

This supportive backdrop, along with resilient earnings results from a number of our portfolio companies in February, drove a broad-based rally across our portfolio during Q1.

Profitability of oOH!media has rebounded strongly

oOH!media's (+28.8% in A$) profitability has rebounded strongly over the last year. It has benefitted from the recovery of out-of-home advertising audiences as the impacts of COVID-related restrictions fade. oOh!media's key Road, Street Furniture and Retail advertising assets delivered revenue for the 2022 year above pre-COVID levels. Given oOh!media has a high proportion of fixed costs (mainly site rentals for its advertising billboards), a large proportion of the 18% increase in revenue for 2022 came down to underlying earnings which more than quadrupled from their depressed 2021 level.

Cochlear rebounded across many regions with greater growth expected

Cochlear (+16.8%) similarly noted a rebound in new cochlear implants across multiple geographies in recent months. This was helped by improving staff absenteeism and falling COVID hospitalisations (both of which had negatively impacted surgery capacity).

Additionally, Cochlear released its next generation of units. This product release is expected to underpin further growth in new cochlear installations as well as upgrades to the newer unit across the existing customer base in 2023.

Our faster growing tech and internet companies benefited from falling interest rates

Falling interest rates during Q1 benefited our faster growing technology and internet companies. This is because the bulk of their cash flows are realised many years into the future, so changing interest rates can have an amplified effect on the discounted value of those cash flows.

> Falling interest rates during Q1 have benefited our faster growing technology and internet companies.

Two positive factors were also evident in resilient financial results and trading updates for Wisetech (+28.5%), Xero (+27.3%), and online classified advertising businesses REA Group (+25.4%), SEEK (+15.4%), and Carsales (+8.9%). Firstly, these companies have been largely successful in increasing the prices of their services, offsetting inflationary pressures. Secondly, their management teams have focused on cost discipline, which has also improved profitability.

That said, not all of our companies have been successful in combating rising cost pressures in recent months.

Domino's profitability has dropped but is expected to recover

Pizza franchise owner Domino's (-23.7%) was caught by surprise by the full brunt of inflationary cost pressures across food, energy, and labour. These results are a function of a very unusual operating environment. The management team are addressing their errors around pricing, and we think they will resolve this weak performance in time.

Domino's aimed to cover their cost increases and protect franchisee profitability by changing prices and adjusting the menu. Unfortunately, with consumers already facing cost-of-living pressures, the eventual price level saw order volumes slip. This slip particularly affected delivery orders, which had previously been boosted by COVID. Together, these factors adversely affected Domino's sales and profit margins in its recently released financial results.

Australian banks reap the benefit of 'unquestionably strong' banking regulation

The major Australian banks have been viewed as a relatively safe haven compared to international banks, so they've outperformed compared to their peers. This is because they have benefitted from having strong oversight from APRA, the bank regulator in Australia.

Two US banks were seized by regulators during Q1 due to their inadequate managing of the sharply rising interest rate environment over the last year, and a loss of confidence from their customers. This led to increased volatility and share price weakness across global banks and financial markets. A key US bank index of share prices fell -17.3% in Q1.

Our shareholdings in four major banks fell, but they still outperformed many global banks

Partly reflecting this negative sentiment towards financials, the share prices of our four major Australian bank shareholdings fell in Q1. However, they outperformed many global banks.

CBA (2.1%), ANZ (-3.0%), Westpac (-7.2%) and NAB's (-7.8%) share prices were negatively impacted by the release of CBA's financial result in February, in which it intimated that its net interest margin (a sign of profitability) may have peaked in October.

Investors seemed to conclude that future profit growth for Australian banks will be harder to achieve in a softening economic environment. This was a key driver of some of the weakness in the Australian bank share prices and not because of any meaningful concerns from investors about the companies themselves.

The strengths of Australian banks

In the years following the 2008 financial crisis, APRA tightened bank regulation in Australia. New regulation required Australian banks to hold significantly more capital buffers than international banks, and to have significant liquidity buffers. Banks also had to effectively hedge their interest rate risk, protecting them from being caught out by rapidly rising interest rates. Importantly, APRA's regulation also applies to all banks – no exemptions or different rules exist for large or small banks. 'Unquestionably strong' is APRA's mantra.

Additionally, Australian banks also benefit from having very broad, stable deposit bases across millions of customers. Again, this provides a good bulwark against a potential loss of confidence across their customer bases.

Our portfolio companies have done well to navigate a complex economic environment

Management teams have typically struck a cautious tone when discussing their earnings outlook for the rest of 2023.

Cost pressures will continue to weigh on profitability for a while. Consumers have yet to feel the full impact of central bank interest rate hikes in recent months. Many Australian households roll off (low) fixed rate mortgages onto significantly higher mortgage rates over the rest of 2023. This is likely to impact spending and consumption. How much, remains to be seen.

On the positive side, employment levels remain close to record highs. Rising inbound migration into Australia and rebounding international tourism will support the domestic economy. And the rebound in China's economic activity is also likely to help global growth.

Overall, we think our portfolio companies remain well positioned to navigate this environment. Many of our companies provide goods and services that businesses or consumers need rather than discretionary items. They are also run by high quality management teams. We think these companies are well placed to keep growing their earnings over coming years, as the remaining disruption from the pandemic is wrung out of the global economy.

A strong rebound in quarter one

Sam Dickie, Senior Portfolio Manager, Select International Equities

There was a lot going on in global markets in the first quarter. A key indicator of market volatility and fear, the VIX index, spiked to 6-month highs in early March and ended the month near 12-month lows. The concerns around the US banking sector were a major contributor to this spike in investor concern.

This elevated uncertainty and banking sector concern caused investors to lower their expectations for further interest rate hikes by the US Federal Reserve. At the start of the month, the market was expecting four more rate hikes, with the Fed Funds Rate expected to peak at 5.5%. By the end of the month, the market was expecting a peak of more than 5% in the Fed Funds Rate, with sharp rate cuts to begin in the second half of 2023.

Alongside these interest rate moves, companies with strong balance sheets (i.e. no or low levels of debt) began to outperform companies with low quality balance sheets by as much as 10% in a month. This has happened as investors became concerned about a possible credit crunch and the resultant growth slowdown.

US big-tech companies were a major driver of market performance in the first quarter – partly due to their strong balance sheets, but also due to falling interest rates (which favour growth companies) and some positive corporate updates.

Portfolio update

The biggest contributors to the Fund's outperformance for the quarter were our positions in Chinese technology holdings, Alibaba and Tencent, combined with some of the US technology names and Floor & Décor. Offsetting these performance drivers were losses on our banking holdings.

> US big-tech companies were a major driver of market performance in the first quarter.

Alibaba and Tencent positioning for the future

Alibaba (+16%) announced it would be restructuring its business into six separate business units and will explore listings or fundraisings for all of them apart from the core e-commerce platform. This was received positively by the market as the value of businesses such as Alibaba Cloud and Cainiao Logistics were not being reflected in the current share price. This should also allow these smaller businesses to be more focused and nimbler outside of the larger corporate structure.

Meanwhile, our other Chinese holding Tencent (+22%) reported strong results as it benefited from a recovery in the Chinese economy following the end of lockdowns, coupled with continued execution in its strategic growth areas such as short video advertising and global gaming.

AI drives interest in Alphabet and Microsoft

Alphabet (+17%) and Microsoft (+17%): while the gains in these companies share prices are largely attributable to gains in the broader tech sector, public interest in AI has been supercharged recently by ChatGPT, an AI-powered chatbot, which has generated a lot of press for these companies.

We increased our position in Floor & Décor late last year

We bought more Floor & Décor (+41%) late last year despite the housing downturn. Three things gave us confidence to buy into a cyclical business in a housing downturn: a long runway for growth, an overly negative consensus, and the ability to prosper at the expense of competitors.

Floor & Décor (FND) is a leading specialty retailer in the hard surface flooring market, with a focus on offering high-quality products at affordable prices. FND operates in a fragmented and large market for hard surface flooring, estimated to be around $40 to $50 billion.

Compared to $4.3 billion of FND revenue the company's current market share is only about 10% to 11%, providing significant opportunities for the company to capture additional market share. To do this, FND is expanding its store base in the US, with a goal of opening around 30+ new stores per year. At the end of 2022, FND operated 191 stores in the US, and we see room for at least 400 stores in the long term. The company's expansion plans are supported by favourable store economics, strong store-level performance, and a long-term trend of consumers preferring hard flooring over carpet.

We exited First Republic Bank and Signature Bank

We exited First Republic Bank and Signature Bank during the quarter. Following the collapse of Silicon Valley Bank on the afternoon of Friday 10 March, fears of further bank failures saw depositors exit other regional banks, resulting in one of our portfolio holdings (Signature Bank) being closed by regulators on Sunday 12 March, and another portfolio holding (First Republic) left on the verge of failure.

The closure of Signature Bank was driven by a combination of the fastest Fed hiking cycle in history, the collapse of Silicon Valley Bank, and a subsequent loss of confidence in regional banks. The pace of the deposit outflows was also extreme, in this modern era of near-instant bank transfers.

This was very hard to predict in advance. Unlike many other bank failures – this wasn't primarily a lending or credit issue. It was instead a crisis of confidence underpinned by Silicon Valley Bank's customer base and a mismanagement of investment assets. As fear spread, following the collapse of Silicon Valley Bank, people got scared and looked for other possible areas of risk in the banking system – especially banks with high levels of uninsured deposits (including Signature Bank and First Republic).

Signature Bank and First Republic had the attributes of the high-quality businesses we look for. These were well-managed banks, with differentiated business models that allowed them to take market share over the last twenty years. On a fundamental basis, Signature Bank and First Republic were different businesses than Silicon Valley Bank. They did not have the same customer concentration, nor the mismanagement of the duration on investment securities.

In a banking crisis, fundamentals take a back seat to emotions and sentiment. While we can assess fundamentals; it is much more difficult to forecast sentiment.

We have no remaining bank positions.

Gartner has lagged, but we've added to the position

(Gartner (-3%) has lagged behind the market after strong outperformance last year. The core research and conference segments continue to grow, so we took advantage of the weakness in March and added to the position.

More recently the market has been concerned about a macro slow-down impacting Gartner's more cyclical businesses. These concerns cover two businesses: their IT consulting, and their research for small start-up software companies where concerns exist around the wider start-up funding environment. These two segments make up around 15% of revenues and, following recent underperformance, a slow-down in these businesses is largely reflected in Gartner's share price.

We exited StoneCo because lower returns are expected

We exited StoneCo (+1%) during the quarter. In line with our investment thesis, the company has successfully reached a double-digit market share in the Brazilian payments market. We believe StoneCo has made the easy market share gains, with competitors now matching their pricing advantage and distribution strategy.

From here it will be increasingly difficult for the company to gain market share. This is likely to result in greater capital intensity and therefore lower returns on capital.

Investing in quality opportunities key to riding out recession

David McLeish, Senior Portfolio Manager, New Zealand Cash & Fixed Interest

The domestic bond market, while still volatile week to week, was much better behaved this quarter. The stubbornness of domestic inflation, despite its normalisation in many other regions, continues to drive tighter Reserve Bank policy for now. However, longer-term fixed interest assets, as they tend to do, took their cue from offshore markets and performed strongly.

Have we reached a tipping point in interest rates?

Jenga is a family favourite game of ours. While I was locked in a tense battle of nerves with my daughters last week, I noted parallels with the current interest rate cycle. In Jenga, players take turns removing one block at a time from a tower, then placing the block on top, making the tower progressively more unstable. The same can be said for the impact of each incremental interest rate hike on the New Zealand economy.

Monetary policy works with long and variable lags

Interest rates at these levels, both in New Zealand and across much of the developed world, are beginning to bite. We expect previous interest rate hikes to have an increasingly negative impact on growth and inflation for at least another year.

But the recent spate of bank failures in the US and Europe suggests the pressure of high and rising interest rates has a new and potent transmission mechanism.

> Interest rates at these levels, across much of the developed world, are beginning to bite.

Tighter bank lending standards raise the risk of a hard landing

The failures of Silicon Valley Bank, Signature Bank, and Credit Suisse are unlikely a sign of bigger things to come – given the unique and extreme factors which caused their demise.

But banks' appetite to lend will likely be curtailed, for a few reasons. First, lower bank profitability (stemming from deeply inverted yield curves). Second, increasingly scarce deposits (admittedly much more an issue in the US and Canada). And third, deteriorating quality of assets (as borrowers fall behind on their payments).

As lending becomes more constrained, less investment and spending are likely. In turn, this could slow economic growth and cause a further, reflexive deterioration in the quality of bank assets. Although this is mostly an offshore dynamic, due to the unique characteristics of each country's banking system, it has the potential to slow growth globally, even more quickly than it was doing a fortnight ago.

A more defensive posture remains prudent

As such, for both our cash and fixed interest portfolios we continue to maintain a mild overweight duration position (that is, more interest rate sensitivity than their respective benchmarks). We have also lowered our corporate bond exposure in both portfolios somewhat, instead favouring higher-grade government and quasi-government securities at this stage.

Portfolio well positioned despite growing concerns around commercial real estate

Sam Dickie, Senior Portfolio Manager, Property & Infrastructure Fund

After providing good ballast to diversified portfolios last year given its more defensive positioning, the Property & Infrastructure fund has lagged growth portfolios slightly so far in 2023.

Separately, the market is concerned about commercial real estate globally. More specifically, the concern is that office vacancy continues to rise globally as people continue to work from home and companies downsize. Investors are also concerned about retail property in an ongoing macro slowdown. Plus, there are concerns about high borrowing rates, large amounts of debt maturities coming due over next few years, and a possible credit crunch due to deposit flight in the US and Europe.

Portfolio update

We have an intentionally large underweight position in Australasian property (18% of the portfolio invested in Australasian property instead of the 35% weighting in our benchmark). This is primarily because property companies typically have narrow moats (low barriers to entry, and commoditised rents and pricing) and short growth runways. Also, since the pandemic, we have become more concerned about the structural oversupply of office space.

> We have an intentionally large underweight position in Australasian property.

Airports fared well in Q1

Global airports had a strong Q1 for three key reasons. First, traffic continues to rise as demand has been artificially suppressed in recent years by travel restrictions, and more recently airline capacity restrictions. The fact the industry is below pre-pandemic capacity somewhat insulates it from the wider economic slowdown. Second, while cost inflation is being observed, the strong operating leverage in airports and pandemic-era cost-cuts mean that earnings per share growth is strong. Finally, the regulatory framework for airports mean that capex inflation benefits medium and long-term earnings as airports can charge higher prices. This is particularly true for Auckland Airport.

Auckland Airport (+11%) had a stronger than expected first-half result. International traffic reached 59% of 2019 levels. Spend rates in the retail business improved and rental growth in the property business was strong. Most significantly, the company will spend approximately NZ$3.9 billion over the next five to six years on aeronautical projects.

Zurich Airport (+17%) and Groupe ADP (+5%) reported its second-half 2022 results, both ahead of expectations. Retail spend per passenger in Zurich is normalising to pre-pandemic levels, whereas Groupe ADP is seeing a structural increase due to an overhaul of its retail operations. Earnings expectations for both airports increased post-results as airline capacity shows resilience.

Vienna Airport (+22%) reported its second half 2022 result. EBITDA was above most recent company guidance and slightly below market expectations. Management guided to traffic at 82% to 85% of 2019 levels, whilst EBITDA guidance was 10 to 15% below market expectations. We sold half our stake into the IFM tender offer in February 2023 as we expected liquidity to decrease, and the offer price was reasonable. The stock has performed strongly in March; however, this price action is out of step with the muted outlook provided by the company and the absence of other material developments.

We've lifted our position in Equinix

Equinix (+11%) had a solid quarter and we upgraded our position in March. This was based on increasing comfort that Equinix can pass on cost inflation, through several price increases and surcharges. Importantly, Equinix's interconnection moat and high value locations allow it to pass on costs to an extent that other datacentre operators cannot achieve.

We have also seen Equinix experiencing robust demand, despite the price increases, and backlogs remain at record levels. Equinix has also reduced leverage levels recently, reducing the near-term refinancing burden. Taken together, Equinix expects to see cash flow per share grow in the high single-digits over the next few years. This compares well against a datacentre and tower peer group that see cash flow per share growth in the mid-single digits or, in some cases, negative.

American Tower outperformed expectations but faces headwinds

American Tower (-4%) announced earnings ahead of expectations but the outlook was underwhelming. Initial guidance for 2023 implies -2% negative growth in cash flow per share, as American Tower faces headwinds from increased financing costs (8% growth impact), foreign exchange rates, and potential bad debts in India (combined 3% growth impact).

We reduced our position in December 2022 as we were concerned about high borrowing costs and a questionable decision to enter the Indian market in 2017. While we were disappointed with the headwinds on India and refinancing, we remain encouraged by the progress on US macro tower leasing.

We lifted our position in Arena REIT

We upgraded our position in Arena REIT (-4%) late in the quarter as its relative valuation became more attractive after the recent sell-off. Arena is one of the highest quality Australian property stocks, with inflation-linked revenues, strong underlying demand dynamics that are resilient through economic cycles, and low leverage allowing for continued earnings growth at a challenging time for REITs.

North American railroads underperformed this quarter

Our North American railroad investments Norfolk Southern (-14%) and Union Pacific (-2%) underperformed. Volumes declined, the intermodal pricing outlook weakened, and investors became concerned about regulatory intervention.

We downgraded our positions in both railroads in December, as some long-term efficiency gains were unwinding, and earnings risk became elevated. We conducted research into Norfolk Southern's recent derailment in East Palestine, Ohio, which involved the discharge of toxic chemicals into the atmosphere. Our initial conclusion is that the company followed safety protocols, and we haven't substantiated union claims that under-staffing caused the accident.

New safety regulations are likely to be passed, increasing the level of investment needed by the railroads. We further downgraded our target weightings in March on the back of this rising regulatory uncertainty and ongoing macro uncertainty.

Market Movements

as at 31 March 2022

Bond Indices	Closing Values	Changes over: 3 Mths %	6 Mths %	12 Mths %
S&P Global LargeMidCap ($NZ)	N/A	8.6	6.6	3.1
USA - S & P 500	8791	7.5	15.6	-7.7
USA - Nasdaq	14735	17.0	16.1	-13.3
Japan - Topix	3325	7.2	10.7	5.8
UK - FTSE100	7930	3.6	12.5	5.4
Germany - DAX	15629	12.2	29.0	8.4
France - CAC40	21543	13.4	27.6	13.4
HK - Hang Seng	64985	3.5	19.1	-4.1
Australia - S & P 200	88138	3.5	13.2	0.1
NZ-S&P/NZX 50 Gross Index (inc imp credits)	14802	3.9	7.8	-1.0
Market Volatility - VIX	18.7	-13.7	-40.9	-9.0

Property		%	%	%
S&P/NZX All Real Estate (inc imp credits)	1641.3	2.0	-1.5	-15.1
S&P Global Infrastructure Index (70% Hedged NZD)	6757.0	N/A	9.8	-0.8

Ten Year Bonds	%	Yield Changes		
USA	3.48	-0.40	-0.35	1.16
Japan	0.32	-0.10	0.08	0.11
United Kingdom	3.52	-0.14	-0.62	1.89
Australia	3.30	-0.75	-0.59	0.47
New Zealand	4.20	-0.26	-0.10	0.98

90-Day Interest Rates	%	Yield Changes		
USA	4.85	0.43	1.52	4.33
Japan	0.07	0.01	0.02	0.01
United Kingdom	4.42	0.54	1.07	3.38
Australia	3.71	0.43	0.65	3.49
New Zealand	5.23	0.58	1.38	3.62

Market Movements
as at 31 March 2023

Bond Indices	Closing Values	Changes over: 3 Mths %	6 Mths %	12 Mths %
S&P/NZX Bank Bills 90-Day	761.93	1.11	2.09	3.15
Bloomberg Global Aggregate Index (Hedged NZD)	N/A	2.67	3.49	-4.79
Bloomberg NZBond Infl 0+ Yr Index	5656.88	N/A	7.55	-0.30
Bloomberg NZBond Composite 0+ Yr Index	1484.66	N/A	2.50	-1.34

Hedge Funds & Commodities		%	%	%
HFRX Global Hedge Fund Index (USD)	1368	N/A	0.2	-3.1
DJ-UBS Commodity Index Total Return	233	-5.4	-3.3	-12.5
Gold (US$/ounce)	1969.00	8.2	18.4	1.0
Oil (US$/barrel)	79.77	-3.7	-10.3	-25.7

Currencies		%	%	%
NZD / USD	0.6257	-1.1	10.6	-10.0
NZD / EUR	0.5759	-2.8	-0.3	-7.9
NZD / GBP	0.5060	-3.8	-0.1	-4.2
NZD / AUD	0.9342	0.2	6.2	0.9
NZD / YEN	83.27	-0.2	1.7	-1.4
Trade Weighted Index	71.28	-1.6	4.2	-4.6

*Total Return Indices. Indices are net of offshore tax.
Source: Thomson Reuters Datastream

fisherfunds

Contact: Private Bag 93502,
Takapuna, Auckland 0740
0508 347 437
enquiries@fisherfunds.co.nz