

# Fisher Funds Market Insights

March Quarter 2025



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# Volatility returns as markets grapple with tariff implications

Ashley Gardyne, Chief Investment Officer

Market performance in the first quarter of 2025 has been vastly different from 2024, as investor optimism gave way to anxiety over US-driven trade policy. The tariffs announced by Donald Trump on 'Liberation Day' were more punitive than expected, and impacts will be felt on economic growth and inflation. At the same time, the resulting market disruption is starting to create attractive opportunities for long-term investors.

## Trump bump becomes Trump slump

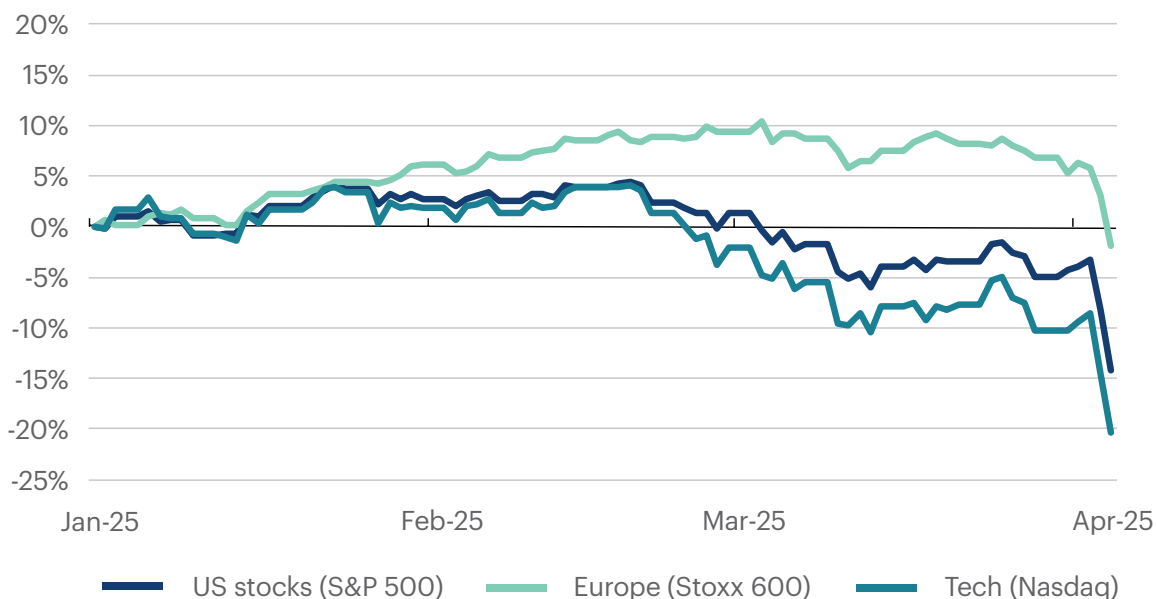
After two consecutive years of +20% gains for US equity markets, it has been a tumultuous start to 2025. The Trump administration has imposed higher-than-expected tariffs on many of its trading partners, while also beginning to implement a

restrictive immigration policy and fiscal austerity through Elon Musk's Department of Government Efficiency. Trade policy uncertainty has knocked consumer and business confidence – and left investors grappling with how this will impact the real economy.

As a result, the initial post-election surge in US equities has sharply reversed, and the S&P 500 Index fell 4.6% in the first quarter. Outside of the US, other markets have fared significantly better, with Europe and Emerging Markets gaining 5.2% and 2.4% respectively in the first quarter.

Combined with the market impact of Trump's 2 April Liberation Day announcements, the S&P 500 has fallen 12.2% from its highs. The US small cap Russell 2000 Index and tech-heavy Nasdaq Composite have fallen 21.8% and 18.0% respectively.

## Market performance since 1 Jan 2025



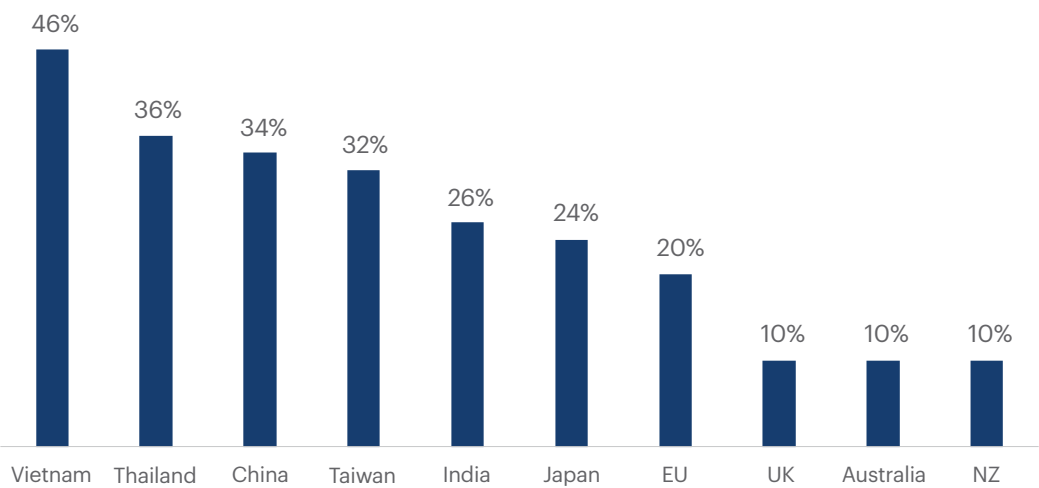
Source: Bloomberg

Trade policy has hit sentiment, and is starting to impact the real economy

In the lead-up to the 2 April tariff announcements, various indicators of business and consumer sentiment started to deteriorate. Trump’s stop-start policymaking also started to influence behaviour, with consumers pulling back on large purchases, management teams putting M&A activity on ice, and businesses delaying new investment projects.

With the 2 April announcement we now have more clarity – but at higher tariff rates than the market had expected (a further 34% tariff for China, 26% for India, 24% for Japan, and 30%+ for a number of Southeast Asian economies). This announcement resulted in a 4.8% one-day drop in the S&P 500 Index as investors tried to digest the potential impacts this would have on inflation and growth.

US Reciprocal Tariff Rates

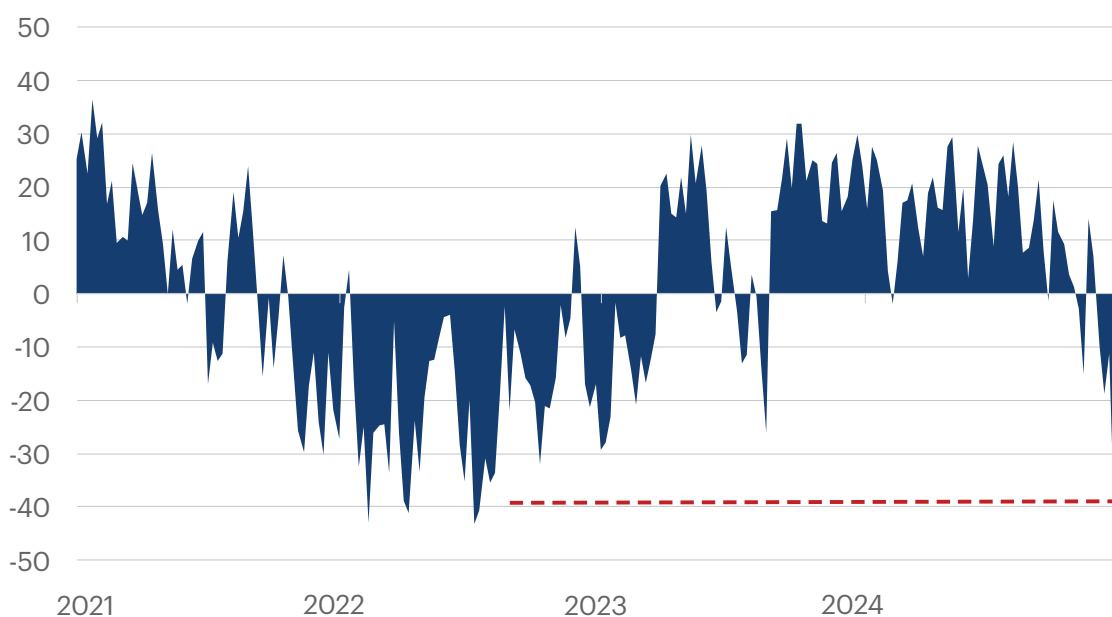


Source: Bloomberg

The hard economic data hasn’t been impacted by tariff uncertainty yet as unemployment is low and US growth has been resilient. However, initial assessments suggest that these new tariffs could lift US inflation by around 1.5% and reduce economic growth by 1.0-1.5% in 2025. While these impacts may seem small, particularly compared to what we saw post-Covid, they could increase if other countries retaliate. That said, there is more water to go under the bridge, and other countries’ co-operation could also see tariff rates and the economic impact reduced.

Opportunities to emerge from the sell-off

When things are moving quickly and uncertainty is high, markets can overreact to short-term news. Indiscriminate selling can often create buying opportunities. As the chart on the next page shows, US retail investor sentiment is already sharply negative, with bearishness approaching levels seen during the 2022 inflation spike. This dip suggests an element of panic in market prices.



Source: Bloomberg, American Association of Individual Investors

Widespread tariffs will have consequences for growth, inflation, and many global companies. Businesses will also take time to adjust their supply chains and pricing in response. On the other hand, as we have seen from history, high-quality businesses will typically find a way to adapt to external events like tariffs, inflation shocks, and pandemics.

Recent share price movements may be justified in certain parts of the market, but in some cases we believe the market is overreacting. While the US market is down around 12% from its high, selected high quality businesses have seen their share prices fall 25 – 30% or more.

### If in doubt, zoom out

It is easy to focus on the 'risk-du-jour', but these risks don't stay front and centre forever. The 2022 inflation spike seemed dramatic at the time, as did the global economy grinding to a halt during COVID lockdowns. Both events are now well in the rearview mirror and markets have continued to move higher.

# Volatility returned to the New Zealand market in 2025, creating opportunities

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**Matt Peek, Portfolio Manager, New Zealand Shares**

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Global markets have been volatile with the US S&P 500 seeing a 'correction' (more than 10% fall from highs) during the quarter. The fall is due to key influences from Trump's second term: the potential impact of tariffs on the global economy, whether cutbacks in spending at DOGE (Department of Government Efficiency) will induce a consumer downturn, and concern around further geopolitical tensions. The volatility has spilled into April with most markets down sharply in the first week as a result of the US 'Liberation Day' tariff announcements.

While volatility sees portfolio values drop from time to time, this comes as part and parcel of being invested in shares, and so we should expect it every so often. We use these opportunities to actively adjust the portfolio (as we did this quarter), putting more money into opportunities where we think better value is emerging and often funding that with cash or by selling down positions where our expected reward-to-risk ratio has not improved.

## A backwards step for the New Zealand market this quarter

The poor performance of the New Zealand market was led by company-specific dynamics for some of the larger companies in the market. Notably, these included Fisher & Paykel Healthcare (-13%), Infratil (-18%), Ryman (-37% to \$2.76), and Spark (-25%, not owned by the fund), which together contributed to most of the New Zealand market decline.

Fisher & Paykel Healthcare saw its share price slump with the company warning that it could face higher costs following President Trump's announced 25% tariffs on products imported from Mexico. Approximately 43% of the company's revenue came from the US, with approximately 60% of US volumes supplied from its Mexican manufacturing campus. We expect the company will be able to mitigate the tariffs over time (should they eventually be implemented).

Infratil provided two key updates about CDC Data Centres. Early in January, CDC also announced it has completed contracting for 230MW of capacity

by year end versus expectations earlier in 2024 that this would reach 400MW. Looking at the big picture, this rate of contracting is still much higher than was anticipated a year ago. However, it was disappointing to see expectations for a higher level of contracting not met.

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## Infratil announced an investment of A\$216 million.

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In February, Infratil announced an investment of A\$216 million into existing CDC Data Centres, increasing its stake by 1.6 percentage points to 49.8%, alongside fellow shareholder, the Future Fund, which bought another 10.5% of CDC. The overall deal was conducted between existing shareholders (Commonwealth Superannuation Corporation (CSC), selling to Infratil and the Future Fund). CSC ran an external process to establish valuation, but existing shareholders had pre-emptive rights allowing them to purchase the shares on offer at the same price offered by third parties. The transaction implies an equity value for CDC of A\$13.7 billion, a 34% uplift on the most recent valuation.

Despite this, Infratil's share price declined after the deal. We attribute this to market concerns around CDC's recent delayed contract wins and skittish sentiment about datacentres generally, including concerns Microsoft is pulling back on demand. Some concerns also point to the transaction occurring among existing shareholders, versus a third-party transacting, given the opacity of the pre-emptive process.

During March, Infratil released a newsletter, which noted its portfolio company One NZ remains on track to meet the mid-point of its earnings guidance range of \$580-620 million (set in May 2024). This range contrasts with heavyweight competitor, Spark, which made the fourth downgrade to its current year earnings guidance, citing 'spending cuts and mobile fleet reductions across Government

and businesses, changes in product mix, and aggressive price competition in mobile'. We note that the mobile share tracking we follow indicates One NZ (along with rival 2degrees) has progressively been taking market share from Spark and had also moved more proactively to position for a consumer slowdown.

During the quarter, we saw several key Infratil executives step up and buy a significant number of shares on market with their own money, which is the ultimate vote of confidence in the longer-term prospects for Infratil and the value on offer. We also bought additional shares during the period.

The quarter was not all bad news – the portfolio's companies as a group delivered credible results in a difficult market environment during February reporting season, particularly a2 Milk (+40%) and Vista (+22%).

### **We exited the Fund's position in Ryman during the quarter**

Ryman unexpectedly announced that it had raised \$1 billion of new equity to pay down debt. This was disappointing, given the balance sheet has been a focus area for us and the management team had assured us all was in order at its late November result. The company concurrently provided a weak trading update with December quarter sales applications down around 40% on the year before, citing challenging market conditions and heightened competitive activity. Ryman also cited impact from 'changes to Ryman's ORA (Occupancy Right Agreement) pricing model, organisational restructure, and reduced incentives in market'. Again, this was not on management's radar. The company flagged yet more potential impairments to its assets despite recent write-downs. Ryman also announced that it will halt more future developments and has roughly halved its combined build rate for the 2026 and 2027 financial years, which will curtail future growth.

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## **The company flagged yet more potential impairments.**

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Despite being long-term investors in Ryman, our thesis has shifted negatively over recent years. While we reduced the position size significantly over the last five or so years, reflecting various issues, we ultimately thought the company still had a strong brand and business model and would regain success with a capable management team and Board in place. The surprise equity raise and change in narrative from the new management

team materially impaired our investment thesis: (1) we have lower confidence in the management and Board; (2) greatly reduced sales after making necessary changes suggest a weaker brand and poor execution, in contrast to Summerset; (3) the growth profile is now lower than we expected; and (4) the potential for greater value over time has decreased due to a large equity raise, asset values unexpectedly being lower, and a slower growth forecast.

We did not participate in the equity raising at \$3.05 per share and fully exited our existing holding in Ryman at above that price. We will take lessons forward in our efforts to continuously improve.

The situation at Ryman contrasts starkly with Summerset (-13%), which delivered a strong 2024 result in February. Importantly, the company also provided an upbeat, albeit cautious, trading update for the first eight weeks of 2025, citing 'market conditions are stable with some early signs of improvement', with the rate of contracting up around 30%. The shadow cast by the situation at Ryman nonetheless weighed on the Summerset share price, but this created an opportunity to add to our position.

Like the divergence between One NZ and Spark, it is comforting to see Summerset out-executing its competitors in a tough market. We continue to see the same happening with other portfolio companies, including Vulcan Steel (+14%) versus Steel & Tube (-8%), Freightways versus NZ Post, and a2 Milk offshore versus its competitors.

### **Volatility can create opportunities, such as Mercury**

We built a position in Mercury (-2%) during the quarter. Mercury is one of the five key New Zealand electricity generator-retailers ('gentailers'). Fundamentally, Mercury's core economic 'moat' is its irreplaceable low-cost hydro assets, with nine power plants on the Waikato River. This North Island hydro system provides a differentiated generation mix to Meridian and Contact. Mercury also has a significant proportion of wind versus other gentailers and a modest amount of geothermal, which nicely balance its generation portfolio. Another attractive attribute is its well-progressed future development pipeline, mostly wind but also geothermal expansion, with a solid balance sheet to support this. We think the recent share price represents an attractive entry point, similar to our initial purchase of Contact in August 2020, which has significantly outperformed other gentailers and the New Zealand market since.



# Strategic portfolio adjustments amid market uncertainty

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**Robbie Urquhart**, Senior Portfolio Manager, Australian Shares

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The focus of our Q1 commentary is to explain how we have sought to sensibly take advantage of the significant share price volatility experienced in the period. Where companies are performing well operationally but share prices have fallen (related to broader market reasons), we have added to our positions. Where companies have performed poorly, we have been circumspect. In some cases we have reduced our weighting, with others we have sold our shareholding.

We have also been measured in responding to controversy that has embroiled Wisetech, a key investment for us. Here, we have engaged with what we regard as a high-quality business rather than following the knee-jerk market response by selling our shares.

We think we will be well served by these decisions.

Building on this approach, it is early days following the US tariff announcements, and the tariff landscape outlook is fluid. We think the sharp market sell-off that accompanied this added uncertainty in early April, will continue to present us with opportunities to re-shape the portfolio to deliver superior performance for our investors over the next few years.

Despite the disappointing start to the year, our portfolio companies are well positioned to grow their profits over the medium term. They benefit from economic moats that we think will stand the test of time, notwithstanding how the US tariff regime might evolve.

It is these business fundamentals that will ultimately be reflected in their share price returns.

## Significant dispersion of equity returns across different geographies in Q1

US foreign and trade policy uncertainty saw European indices outperforming the US share market during Q1. Within the US, the technology heavy Nasdaq index fell 10%, underperforming many other sectors of the market.

As we go to press with the Quarterly Review, we also note that the wide-ranging tariff announcements

in the US on 2 April have caused a sharp sell-off in global share markets with share prices of global technology companies consequently falling further.

The Australian share market fell in line with the S&P 500 index in Q1. However, like the S&P, returns were significantly dispersed across industries and companies. Industrials (+1.5%) and Materials (-1%) buoyed by gold miners were two of the better sectors in Q1. And, as seen in the US, information technology (-18%) was the worst performing sector and helped drag the Australian share market lower.

Part of the return dispersion across the ASX was driven by the rising global economic (and tariff related) uncertainty. Some of this uncertainty was also driven by company specific announcements during the semi-annual financial reporting season in February. Companies that disappointed market expectations, irrespective of whether this was due to temporary or more structural reasons, saw their share prices fall sharply.

## Opportunity knocks when market wobbles collide with high-performing companies

Skittish and volatile markets, such as those experienced in Q1, present investors with opportunity.

We capitalised on this by adding to high-quality positions including software company Atlassian (-13% in A\$), online classified advertising businesses CAR Group (-12%) and SEEK (-4%), and the global leader in treating profound hearing loss, Cochlear (-9%).

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## We capitalised on this by adding to high-quality positions.

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These companies are leaders in their fields, with broad economic moats around their core divisions. The management teams are performing strongly in this economic climate.

Atlassian, for example, delivered revenue growth of over 30% in its key divisions. It lifted earnings guidance for the full year. Critically, it achieved key US government security and regulatory approvals



in Q1, enabling further use of its software by government agencies. Cochlear received regulatory approvals in Australia and Canada for its newest sound processor, also laying the foundation for future growth.

SEEK and CAR Group similarly demonstrated tangible progress in delivering on key profit metrics in what has been a tricky global economic environment. As a job advertising platform, SEEK has little control over the economy and appetite for businesses to hire employees. But SEEK did well in what it could control, taking market share in advertising, lifting prices, controlling costs, and investing in new products. In Australia, SEEK's share of advertising placements now sits at 35%, over 4x that of its nearest competitor.

CAR Group has successfully expanded into international markets over the last 15 years. Apart from Australia, CAR now counts South Korea, the US, and Brazil amongst key markets that help drive and diversify its earnings growth. Each of these markets is structurally growing. Like SEEK, CAR's management team is juggling its levers of price, cost, and product investment for durable growth.

We were happy to buy more shares in each of these companies, which are selling for less than they were at the start of the year. We have funded these purchases from a combination of positions that look relatively more expensive, as well as from positions we have exited (see below).

### Balanced approach as we engage with Wisetech over governance

In responding to the 33% share price drop in software company Wisetech's case, our calculus is different. This difference is reflected in our measured decision to remain invested but at a lower target weight than we have invested in historically.

Wisetech is one of the highest quality companies on the Australian share market. Its software solves critical challenges for large logistics companies. Wisetech is becoming more important to its customer base as it increases the number of bottlenecks that it solves for its customers. It is the clear market leader and has decades of growth ahead of it.

Personal controversy related to the founder (and Wisetech's largest shareholder) Richard White, led to tensions with the Board. This ended with four independent Board members resigning abruptly in February. This governance turmoil saw several large shareholders exit their positions and was the primary driver of recent share price weakness.

We are deeply unhappy with the governance turmoil. But rather than sell our position at what we think is now a compellingly cheap valuation, we elected to engage with the company. Alongside other institutional shareholders who also see merit

in this approach, we have actively encouraged the company to take expeditious, yet orderly, steps to refresh the Board. We also pushed for the company to embark on a clear succession plan to ensure a smooth transition to a new CEO, one capable of achieving Wisetech's significant potential in the future. If the company delivers on these steps, alongside the clearly articulated software product development plan, we think shareholders will do very well in time.

It is early days in this governance reset. But we have been satisfied with the company's efforts so far in responding to this engagement. This response includes appointing two new directors to the Board in late March. If the company continues to improve its governance structure, our position sizing could be reviewed again in time.

### Exercising caution where an investment thesis has been dented

In a handful of cases we saw the market react sharply to financial updates from our companies where management execution lay at the core of the poor financial results. Insurance construction and support services company Johns Lyng (-42%), pizza franchise operator Domino's (-11%) and supermarket operator Woolworths (-2%) all fit into this category.

We have sold and exited our position in Woolworths. While we like the non-discretionary nature of Woolworths Australian food business and the scale moat afforded to it by being the largest supermarket operator with over 30% marketshare of the supermarket industry. However, management has consistently underperformed its key competitors in both Australia and New Zealand for almost two years. In addition, competition has intensified with the likes of Amazon, Bunnings, and Chemist Warehouse chipping away at supermarket profitability.

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## We have reduced our portfolio weighting in Johns Lyng.

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We have reduced our portfolio weighting in Johns Lyng after poor execution within its Australian business saw a key insurance customer re-allocate work to their competitors. This departure put a deep dent in its profitability, which was further exacerbated by benign weather (fewer insurance claims were made). We're comfortable that inclement weather will return to damage properties, driving an increase in insurance claims in the future. However, we are less enamoured with how easily an insurer was able to take work away from Johns Lyng. This suggests its moat may be narrower than we first thought. It is an issue we're working through with

management (including monitoring whether Johns Lyng can recoup that lost share – something management remains confident in doing).

Domino's fits into a similar category. Domino's replaced its CEO in late 2024. The new CEO has taken some significant steps to remedy poor decisions made, particularly in Japan, under the prior CEO's tenure. These steps, which include shutting down a raft of unprofitable stores across the Domino's network, seem sensible. However, we are looking for more evidence of management execution and an improvement in overall operations before we are prepared to add to shares that, at face value, look relatively cheap.

# Macro crosswinds drive sharp moves in markets and growth expectations

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**Sam Dickie, Senior Portfolio Manager, Select International Shares**

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Global stock markets, and in particular US stock markets, were impacted by multiple macro crosswinds during the March 2025 quarter.

First, exceptional US policy uncertainty around trade and federal Government spending sent policy uncertainty surveys to their highest level in 50 years. While this uncertainty unsettles share markets, it also disrupts corporate planning, contributing to a sharp downward re-pricing of US economic growth expectations. For example, the real time Atlanta Fed 'GDPNow' tracker shows the US already in recession. While attempting to track daily GDP is inherently volatile, in the past 25 years we have only seen real-time growth indicators drop this sharply during the COVID lockdowns.

In addition, the Department of Government Efficiency (DOGE), run by Elon Musk is in 'slash and burn' mode and that has impacted several sectors (healthcare and IT) that have the US Government as a customer.

On top of this, the ongoing China versus US AI arms race has caused the market to question the return on the rapid investment in US AI tech companies.

This questioning caused global growth stocks (and especially US growth stocks) to underperform global value stocks by 12%, the sharpest quarterly move in 25 years.

Against this backdrop - and given the conditions were particularly challenging for our investment style - the underperformance for the quarter can be attributed to the relative weakness in growth stocks.

While we had taken some profits in our US growth stocks, and big tech names in recent months, the stark underperformance into quarter end was throwing up interesting opportunities. For example, very recently, we have been taking profit in our China tech exposure Tencent and shifting that back into US tech - Tencent outperformed US big tech names by 50% in six weeks, an extraordinary move.

After month end and after the significant stock market weakness post-Liberation Day, we took advantage of the weakness in three ways:

1. buying high quality companies that are partially impacted by tariffs that have fallen sharply (Intuitive Surgical, Meta, Gartner);
2. buying companies

that are exceptionally high quality and are a little less expensive now (Costco, Hermes);- 3. taking profits in our defensives (United Healthcare, Boston Scientific), and buying high quality companies that are more directly impacted by tariffs and the related macroeconomic gyrations (Amazon, KKR, Nvidia).

We have been very under-exposed to the AI thematic because we were concerned about the amount of hype around. As the AI hype has been toned down over the quarter, we have been slowly increasing our exposure there.

Overall, this extreme lack of clarity on US and therefore global policy, exacerbated by the "Liberation Day" reciprocal tariffs, plus the speed of the global sector rotations, is throwing up opportunities. However, it is also causing us to be extra vigilant.

## Portfolio update

Tencent's (+19%) sharp rally was kick-started by Chinese AI startup DeepSeek's release of an AI model in January that performed on par with leading US AI models. This release ignited investor enthusiasm for the sector, and the Chinese tech companies launched their own AI models shortly after.

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## Tencent is executing well.

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While there was some concern in the quarter around Tencent ramping investment in AI, we view it as a positive. With over one billion users on its Weixin social media app, Tencent is arguably one of the best positioned companies in China to benefit from AI. This massive user base offers unmatched potential to monetise AI through multiple avenues including improved user engagement and increased advertising revenue in its social media and video products; consumer-facing AI applications; and AI search. Coupled with strong growth in the core gaming and advertising segments, Tencent is executing well, despite a softer economic backdrop in China.

Sentiment was further boosted by a more supportive stance from the Chinese government, with President Xi Jinping meeting tech leaders during the month.

This follows several years of intense regulatory oversight on the private tech sector.

Boston Scientific (+13%) came out of the quarter relatively unscathed against a backdrop of potential tariffs and proposed cuts to US healthcare spend. While tariffs have raised concerns for medical device companies that manufacture offshore, Boston did not expect any material impact to the business, but that may change with the 2 April tariff announcements. The Trump administration is also looking to take over \$1 trillion of costs out of the Government budget over the next 10 years. At nearly 30% of Government spend, healthcare is in the crosshairs, particularly the Government-funded Medicaid program. If these cuts are made, expectations are that hospitals may reduce large capital expenditures, however BSX has little to no exposure here. Boston's devices are typically used for non-elective procedures that are less likely to be deferred.

Netflix (+5%) had a strong start to 2025, building on record-breaking performance in late 2024. The company reported impressive subscriber growth in Q4 2024, adding nearly 19 million new members to surpass the 300 million subscriber mark. Notably, this growth was robust even in highly saturated markets like the US and Canada, underscoring the enduring appeal of the platform. In January, Netflix increased prices for all three plans, which

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## Netflix (+5%) had a strong start to 2025.

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is expected to grow operating profitability by 24% in 2025. Netflix's robust lineup of new content releases, coupled with its significant increase in the content budget to \$18 billion for 2025, solidifies its industry-leading content offerings and reinforces its strong competitive position in the streaming market.

Alphabet (-18%) and Amazon (-13%) shares were weak, driven by softer than expected reported growth in cloud datacentres coupled with larger than expected capital expenditure. While the weaker cloud datacentre revenue was caused by capacity

constraints due to excess AI demand, sentiment generally soured on AI later in the quarter, kick-started by the release of China-based DeepSeek's efficient AI models. The market is also questioning the potential return on this elevated capital expenditure.

Floor & Decor (-19%) shares were weak during the quarter as it was caught up in President Trump's tariff announcement (it imports 70% of its flooring) and potential demand weakness as a result. Floor & Decor's superior value proposition (cheapest price, widest selection, direct sourcing) has driven ongoing market share gains in a weak housing market and should ensure it is in a better position than most of its competitors.

Greggs (-38%) shares fell sharply in the quarter reflecting broader weakness in the UK consumer sector, as falling consumer confidence and a deteriorating economic outlook weighed on sentiment. While Greggs has been taking market share in the UK food-to-go sector, it is struggling to pass on higher costs driven by the expansion of its food manufacturing plants and distribution in a weak consumption environment.

# Steady returns amid market volatility

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**Quin Casey, Senior Portfolio Manager, New Zealand Cash & Fixed Interest**

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Global bond markets had a relatively steady quarter amid rising uncertainty about the outlook for economic activity caused by US 'on-off' tariff policy announcements. Our preference for high-quality fixed-income assets, backed by companies with robust underlying fundamentals, proved beneficial. We will proceed with caution while also hunting for new investment opportunities that often surface during periods of market volatility.

## **Bonds offer ballast in stormy waters**

It is timely to recall that bonds are essentially an 'IOU'. A lender provides a borrower with a lump sum of money and the borrower agrees to pay the lender a schedule of interest payments and return the lump sum at an agreed date in the future.

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**Bonds can be a safe harbour when the waters become a little stormy.**

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When the borrower has significant financial strength, the flow of interest payments can increase in value during times of market uncertainty. That is, bonds can be a safe harbour when the waters become a little stormy.

In general, high grade fixed-income assets such as government bonds and debt securities issued by investment grade rated companies were a haven for investors during the first quarter of 2025.

For example, the NZX 50 Index returned -6.41% while an index of NZ government and investment grade bonds returned +0.69%.

In this way, unlike 2022, when bonds and equities delivered negative returns because of central banks hiking rates in response to the inflation shock, fixed income assets reverted to the traditional role of

providing ballast for multi-asset portfolios during market volatility.

And because the fund has been invested into higher quality fixed-income assets backed by high quality businesses, the fund generated a steady return for the first 3 months of the year.

## **Bargain buys on the horizon?**

As mentioned in recent quarterly reports, companies with more debt relative to cash flow are less resilient to slowing economic activity or periods of uncertainty. Such companies tend to find it difficult to grow sales as cashflow is diverted from new product initiatives to servicing debt.

Further, we have noted that credit spreads – the extra yield over and above a government bond – on lower-rated bonds have been below long-run historical averages in recent times.

However, during Q1, credit spreads on lower-rated companies moved higher due mainly to the US 'on-off' tariff policy announcements noted earlier.

While we have yet to identify attractive opportunities within the lower rated investment universe, we are rolling up our sleeves and applying our long-standing credit analysis process to bonds where the risk-reward balance has materially improved.

We will keep you posted on any bargain buys over the coming quarters.



# Tariffs, datacentres, and central banks were the key drivers of performance

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**Sam Dickie, Senior Portfolio Manager, Property & Infrastructure Shares**

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Three key things moved markets over the past quarter: President Trump's policy agenda (pro-growth excitement giving way to tariff-induced slowdown fears); demand questions in the datacentre and power markets; and a more hawkish stance from the US Federal Reserve and RBA.

## Potential US tariffs drove market volatility

Markets were volatile as investors tried to price uncertainty surrounding President Donald Trump's tariff policies, ahead of 'Liberation Day' on 2 April. Uncertainty impacted business and consumer confidence in the US, leading to negative economic surprise data. The S&P 500 recorded its worst first-quarter performance since 2022. Most relevant for our Fund are tariffs on Canadian and Mexican goods, potentially impacting trade for US freight railroads and travel demand for our Mexican airport investments.

## Datacentre demand has been intensely debated

The emergence of DeepSeek, a low-cost AI model from a Chinese start-up had a material impact on artificial-intelligence (AI) related stocks. The success of this low-cost AI model from China raised questions around the commoditisation of AI large-language models and the sustainability of the tens of billions of dollars being spent by large US tech companies on their AI ambitions. Should less compute power be needed, demand for electricity and natural gas (to fuel electricity generation) will also be lower.

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**These developments are negative for datacentre demand.**

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Reports also emerged of Microsoft cancelling datacentre leases. Microsoft has been the biggest datacentre lessor globally over the past two years. CEO Satya Nadella appeared on a podcast suggesting the global datacentre market could be oversupplied in 2027–2028, and that datacentre

lease pricing may come down (compared to expectations for rising lease rates). These developments are negative for datacentre demand.

## Key central banks adopted a more hawkish stance

The US Federal Reserve and the Reserve Bank of Australia struck slightly more hawkish stances over the quarter, mindful of labour-market risks and the potential impact of tariffs. Despite an elevated track for short-term interest rates, 10-year government bond yields fell in the US (-32 bps) as economic growth expectations fell. Similar bond yields in Australia and New Zealand were broadly flat.

## US tower operators benefited from lower interest rates and stabilising operating conditions

Crown Castle (+13%) announced the sale of its fibre and small cells business unit for US \$8.5 billion, with the proceeds to be used to retire debt (\$6 billion) and fund a share buyback (\$3 billion). The proceeds are disappointing relative to capital invested (\$19 billion), but we welcome Crown Castle's transformation into a pure-play US tower company. We consider its moat to be wider after the transaction and increased our position by +0.5% during the quarter.

American Tower (+15%) reported fourth-quarter earnings. Management indicated overall leasing activity may accelerate in the second half of 2025. Emerging markets, which have been problematic in recent years, are showing improving growth overall.

## Utilities saw divergent performance over the quarter

Utilities overall contributed 2% to fund return and 3% to benchmark return over the quarter. Stocks that provide power to AI datacentres declined -10% to -15%, whereas 'safe haven' utilities like American Water Works gained 16%. European Utilities gained 13% as global investors rotated out of USD-assets and the datacentre trade.

Within our portfolio, CMS (+10%) and American Water (+16%) performed well. However, our New Zealand 'gentailer' assets led to underperformance relative to the benchmark. Earnings expectations for Meridian (-4%) and Contact Energy (-1%) fell as they are forced to buy expensive thermal generation

while hydro lakes (a source of fuel for electricity generation) are low. We consider this to be a short-term issue for the sector.

We added Mercury Energy (-2%) to the portfolio during the quarter. We view Mercury as a quality-on-sale opportunity, with compelling valuation due in part to being deleted from a widely followed index. Mercury has the second-best asset base in New Zealand (behind Meridian), supported by valuable North Island hydro assets. We previously exited Mercury from the portfolio in 2016.

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**We see potentially attractive value in utilities and independent power producers.**

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For new opportunities outside our portfolio, we see potentially attractive value in utilities and independent power producers. Share prices for many such stocks have retreated significantly from their highs on concerns over renewable energy policy and datacentre demand concerns.

### **Datacentre stocks had a tough quarter**

Datacentre-related stocks were the worst performers in the portfolio this quarter: Infratil (-18%), Equinix (-13%), and GMG (-20%). We reduced our position by -1.5% in both Infratil and GMG during the quarter. Some of this capital was re-deployed into defensive names Mercury Energy (-3%) and Waste Connections (+13%).

Infratil (-18%) announced an investment of AUD\$216 million into existing investment CDC Data Centres, increasing its stake by 1.6% to 49.8%. The seller was fellow shareholder CSC. The transaction implies a 34% uplift on the most recent independent valuation. We estimate the deal implies \$1.15 per share of value creation for Infratil shareholders. Despite this, Infratil's share price declined after the

deal. We attribute this to market concerns on CDC's recent delayed contract wins (noting Microsoft is a major customer) and concerns regarding datacentres generally. We decreased our position in Infratil at the end of January (before the CSC deal) given CDC had missed contracting expectations and required more equity to deliver growth.

Goodman Group (-20%) reported first-half 2025 results alongside an AUD\$4.4 billion capital raise. Full-year 2025 guidance was maintained, which disappointed a market accustomed to earnings upgrades at half-year results. The capital raise was conducted to support growth in new datacentre projects, which carry 3–5 times the capital intensity of Goodman's traditional logistics property projects. Goodman will fund most of the initial investment from its own balance sheet and without customer leases in place (a tactic to maximise eventual lease economics). A restructure of a North American partnership also led to Goodman buying back \$3.5 billion of assets, further stretching Goodman's balance sheet. Overall, we were disappointed with the capital raise and restructure of the North American partnership. Goodman is a relative newcomer to datacentres, and it risks raising capital and building speculatively at the wrong point in the data centre supply and demand cycle. We did not participate in the capital raise and reduced our position by 1.5% during the quarter.

### **Tariffs impacted rail companies, despite solid fundamentals**

North American rail CPKC had a tough quarter (-3%, despite +10% performance in January) as tariff threats escalated. CPKC operates a network across Canada, the US, and Mexico. CPKC's fourth-quarter 2024 earnings beat expectations by 5% and beat overall 2024 earnings guidance, despite facing challenging weather and port disruptions. Management provided a wide range for 2025 earnings guidance (12–18% growth), incorporating tariff risk at the low end of guidance.



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