Bramwell Brown Ltd

INVESTMENT ADVISERS – SHAREBROKERS

Director: Brett Dymond – BBS, GradDipBusStud (Personal Financial Planning)

Bramwell Brown Limited – Newsletter – February 2022

Brokers' Picks

Each year the New Zealand Herald publishes a table of brokers' recommendations for the five companies they think will be the best performers over the coming year. It's a no-win situation for the brokers, as they all know the share-market is not somewhere to invest for a short period. However, it provides interesting reading, and looking back on previous recommendations highlights the fundamental need to hold a diverse range of companies. Two years ago, A2 Milk was chosen by five out of six of the brokers. It has since fallen over 60% in value. Evolve Education, Tower, NZ Refining, Vista Group, Sky TV and Comvita have been chosen previously – none of which have performed well since. Plenty of very good choices have also been made of course, including Mainfreight, Freightways, Fisher & Paykel Healthcare, Ryman Healthcare, Xero and Restaurant Brands. Here are this year's choices:

Broker 1	**Broker 2**	**Broker 3**
Contact Energy	NZ Refining	A2 Milk
Summerset	Sky City Entertainment	Fletcher Building
Pushpay	Arvida	F&P Healthcare
Ebos	Ebos	Infratil
Fletcher Building	Vulcan Steel	Freightways

Broker 4	**Broker 5**	**Broker 6**
AFT Pharmaceuticals	Heartland Group	Contact Energy
Fletcher Building	Mainfreight	Infratil
Heartland Group	Sky TV	Heartland Group
NZ Rural Land Company	Trade Window	Skellerup
Promisia Healthcare	Trustpower	Comvita

I think it's important to stress that nobody should be picking stocks with a one-year time frame – shares should be treated as a long-term investment. If I had to pick a sector I see performing well into the future it would be the retirement-care industry. New Zealand's demographics see the sector well placed for significant growth, although rising interest rates could see their share-price performance curtailed in the short-term.

Sharemarket Volatility

The Financial Markets Authority (FMA) released research just before Christmas on investor capability in relation to market volatility. Their concern is that newer investors may not be prepared for a market downturn. In recent years many new investors have been attracted to the share market, with online platforms such as Sharesies and Hatch making it simple and cheap to buy shares. Of course, these platforms don't come with advice, so investors are often making choices that aren't backed by research, or taking into account the investor's tolerance for risk. The past decade has seen significant appreciation of assets (shares and property) due to the very low interest rates over that period. What happens when interest rates start increasing? The theory is no different, but in reverse – as interest rates increase, asset prices should decrease.

The FMA's concern is that many investors have had years of rising share prices, and are not prepared for a period of negative returns. They have made available a number of educational resources, including this article written by well-known financial commentator, Mary Holm.

"I'm worried. While it's great to see many new people getting into investing in shares, and others taking more interest in their KiwiSaver accounts as their balances grow, they could be riding for a fall. Share markets – and property and bond and cryptocurrency markets for that matter – fall as well as rise. And so do all but the very lowest-risk KiwiSaver funds. It happened not long ago. We saw an example of a share market downturn in February 2020, near the start of the Covid-19 pandemic, when both the New Zealand and world share indexes plunged. More than 200,000 New Zealanders – particularly young people - panicked and moved to lower-risk KiwiSaver funds, and others sold their share investments. However, the markets recovered remarkably quickly, before more people reduced their risk. That was great. The only trouble is that such a speedy turnaround may have given investors a false sense of security. The 2020 plunge was the first major downturn since the global financial crisis in 2007-09. In the decade in between, newcomers to shares and KiwiSaver enjoyed a pretty steady stream of market gains, no doubt boosting people's confidence in their investments.

We don't know, though, when the next downturn will happen. It could be tomorrow – literally. And it could take a few years to fully recover. What to do? How can you cope with volatile investments? One way is to avoid them, sticking with low-risk funds or bank term deposits. But in the long run your money will grow much more slowly. If you plan to stick with shares, higher-risk KiwiSaver funds or other share funds, ask yourself three questions:

- Is your investment spread across many different shares?

If you're in a KiwiSaver fund or another fund, this is taken care of for you. All the funds I know of invest in a wide range of shares. If you're investing directly in shares, it's wise to spread your money over at

least ten companies, and twenty or thirty is better still. Shares in a single company can become worthless, but that doesn't happen to multiple companies all at once. What's more, the companies should be in a broad range of industries. A single industry can hit hard times. It's also wise to invest in many different countries. The easy way to do this is through a New Zealand-run managed fund that holds international shares. Many KiwiSaver funds invest internationally. Ask your provider about your fund's mix.

- When do you plan to spend the money – perhaps on a first home, or in retirement?

You don't want to ever be forced to sell an investment when it's down. So you need to think about your spending plans. If you expect to spend the money within ten years, I suggest you move to a medium-risk KiwiSaver or other managed fund. If you stay at the higher risk level, there's a chance the markets will fall and won't recover in time. Then, when you get to within two or three years of spending, move to a low-risk fund or bank term deposits. Even medium-risk investments can be pretty volatile. You want to be sure that every last cent will be there when it's time to withdraw the money.

- How would you feel if your investment balance halved in a downturn?

It's happened before. Starting on BlackTuesday, 20 October 1987, the value of all the shares listed on the New Zealand stock market halved in less than four months. The market continued on down to a 60% drop, and took several years to recover. Around the world, the crash was similar, although the recovery was faster. When the market crashes, many people sell their shares or move their savings to lower-risk investments. This is a bad move. If your $10,000 balance becomes $5,000 and you sell or switch, you've made that $5.000 loss real. But if you wait – and your investment is well diversified - your balance will grow back again.

How do I know? Share markets have always recovered in the past. And when you think about it, they always will. Companies continue to provide goods and services, and people continue to buy them. Many of those companies will make profits, and investors will want to participate by buying shares in the companies. That demand will push prices back up. Put it this way: if that process doesn't continue, we've got more to worry about than our investments! In the long run, people with diversified higher-risk investments, who don't plan to spend that money within ten years and who stay put during market downturns, come out as winners.

Despite these assurances, though, some people can't cope with seeing their balance fall. If that would be you, it's really important that you reduce your risk now, before a downturn, so you don't find yourself turning a loss on paper into a real loss."

I share the FMA's concerns. We have new investors, some with large sums of money to be allocated to shares. Our medium-term prediction is that interest rates are likely to increase, and share prices therefore should decrease. You could argue that if this is your expectation, then it's best to keep your funds in cash and wait until the market reaches the bottom. I'd make the following points:

- History tells us we are not very good at predicting the future accurately
- The majority of investors seek income, and shares provide that income
- Sitting on cash will provide the lowest level of income
- Cash provides no opportunity for growth

Nobody likes to see their assets reduce in value, particularly those new to investing. Long-term, experienced investors have been through a number of cycles, and have seen the share values go through peaks and troughs. The Global Financial Crisis in 2008 had a big impact on share values, however eventually saw a very impressive recovery. The Covid 19 outbreak saw a dramatic drop in values, however was short-lived. My advice to investors during volatile periods is to invest in stages, rather than trying to time the markets and invest all at once. If you consider a wage-earner enrolled in a Balanced KiwiSaver fund, every fortnight their KiwiSaver provider is purchasing shares for them to add to their portfolio. Over one or two years you could say that some shares were purchased cheaply, and some were expensive. Over a long period however, it is more likely that the value of those shares has increased.

Mary Holm makes a good point when she asks "How would you feel if your investment balance halved in a downturn?" This would be an extreme downturn, but it is not out of the question. What I have discovered over my years as an adviser is that investors will have a certain risk tolerance, however when risk turns into loss, they realise that they weren't prepared to take the risk after all. I may sound like a broken record, but I'll say it again – our best defence against market volatility is:

- Understand the risks you take with investments, and stay within the risk you can tolerate
- Hold a wide variety of asset classes
- Buy good companies and hold them for long periods
- Hold overseas investments as insurance against a shock to the New Zealand economy
- Limit your exposure to individual companies
- Be aware that a market correction will occur at some point
- Don’t attempt to time the market – invest in stages
- Don’t be tempted to sell if the market does fall

DISCLOSURE STATEMENT AVAILABLE ON REQUEST AND FREE OF CHARGE