BC'S BUSINESS BRIEFS

Asset Values – making sense of today's values

As with many others that have tried to predict what would happen to asset values as the world works its way through the Covid-19 pandemic, I have been woefully wrong in my predictions. There appears to be a huge disconnect between values of growth assets such as shares all around the world and individual asset classes in different markets. Here in New Zealand we appear to be experiencing huge growth in residential housing prices that I certainly did not predict a few short months ago.

What have been the driving factors behind these trends? I certainly don't know for sure, but a small number of things in New Zealand's case appear to have contributed to this;

1. As economic activity has cratered, the government (as we all know) is borrowing hundreds of millions of dollars to pump into the economy to minimize the lasting social and human damage from the largest fall in economic activity since the Great depression;
2. The Reserve Bank is part way through easing interest rates to such a degree that it is distinctly possible we may hit negative rates territory in the next year;
3. While net immigration has almost come to a standstill, the thousands of New Zealanders living abroad who have flocked home to New Zealand on a permanent or semi-permanent basis have brought significant amounts of capital (both monetary and human) back in to the country;
4. Most people appreciate that Covid-19, while very serious in the short term, is likely to be around for a long time and we need to find a way to live with it until a vaccine is readily available that lowers the risk of catching it and mitigating its impact;
5. It appears that a combination of these and other factors has given the general public the confidence to invest in growth assets and in the case of residential housing, to accept that we still have a shortage of houses in this country and house ownership is as important now as it's ever been;
6. With regard to shares it's impossible not to come to the conclusion that the extremely low interest rates available to investors on fixed interest is contributing in a large way to the flight to equity markets as people search for ways to pad their investment income.

What about the future?

Good luck in predicting what will happen to asset values in the future. I'm sure nobody can be supremely confident they know the answer to that.

There are a few facts which could (should?) have an impact on asset values. These are a few things, that I sometimes wonder about;

1. Have we reached the bottom of the economic downturn yet? Conventional wisdom suggests that we may not have. The stimulus funding from government is basically finished and the lifeline these funds contributed to business' ability to stay afloat is complete. Are we going to see an increase in the numbers of business' closing down in the next 6-12 months?
2. Though New Zealand is widely acknowledged to have done a pretty good job of handling the pandemic, there is no guarantee that it won't come back. We would hope

that the border holes that allowed the recent flare up back in, won't be repeated, but we can't be sure;

3 A higher unemployment rate will inevitably lead to more stressed house sales as people are unable to handle the debt servicing associated with what are high average loan values, particularly in Auckland;

4 In the case of businesses that don't make it through the next 6-12 months, there will inevitably be fallout for business owners forced to dispose of second properties, perhaps holiday homes. If you're faced with the choice of closing your business (and therefore income generation capacity) or selling your holiday home, I believe most business people would choose to dispose of the holiday home in the first instance. There must be some likelihood of this impacting on the values of residential property in some of our favourite beach towns.

While I have been undoubtedly wrong in my views regarding asset prices in the last six months, I believe there is still reason to be cautious in suggesting the worst is behind us economically. I believe it is too soon to draw that conclusion. The fact that we are about to head in to summer in better shape than it appeared we would some months back is good. Here's hoping some warm sunny weather will assist us getting through what will likely be a tricky next six months, from an economic standpoint.

Election 2020

While it's still looking likely that the Labour party will continue to lead the government after our upcoming election, one can argue that the most important thing that business needs out of the election is certainty. Whatever your political persuasions, if you are in business and you are uncertain of the likely policy changes after the election, you will be far less likely to invest in growing your business than if you know what the roadmap looks like. While my inherent belief is for smaller government and smaller taxes, most of all I want to know the ground rules so I can have confidence that any decisions I make are soundly based within the rules framework and the rug won't be pulled from under my feet as a result of changes out of my control.

One of the interesting trends to me has been the rise of the Act party in this election campaign. One imagines that a significant part of their rise in the polls has been a result of their natural partner National's missteps leading in to the election. While the result is heavily biased towards a Labour led government, it is not outside the realms of possibility that a National/Act coalition is possible. If the Greens and NZ First fail to make it back into parliament (distinctly possible) and the right bloc were to consolidate their position by perhaps 5% in the last week of the election campaign (unlikely but possible?), we would be in a very tight race all of a sudden. If that happens, we can only hope that the final result is obtained for whomsoever can form a government quickly and we can all get back to work.

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