

# Snapshot

Market insights for investment professionals from  
Fisher Institutional — August 2018

## Trump + Twitter + Tariffs + Trade Talk = Tremors



**Frank Jasper**  
Chief Investment Officer

The relationship between the United States and the rest of the World is at the core of Donald Trump's political movement. While this was focussed more on immigration, walls and vague comments about Nafta Trump has pivoted this year to an explicit focus on the US's economic relationship with its trading partners. This has caught the market's attention and tremors in stock prices have been the result.

Ever since the establishment of the General Agreement on Tariffs and Trade (GATT) was established in 1947 the western world has embraced liberal trade policies. This has meant that countries focus productive resources on areas of comparative advantage and increase trade in goods and services to fill in the gaps. Trade has been generally beneficial, resulting in higher levels of economic growth and more competitively priced goods and services.

Companies have taken advantage of free trade to build complex global supply chains enabling significant production efficiencies. This has been hugely beneficial to the emerging economies enabling a period of rapid growth.

While trade has enriched most of us not everyone has been a winner. Similarly, not every country has strictly adhered to the free trade playbook. It is these two themes that Trump has tapped into in his twitter storms.

He is somewhat justified in his rants. The US imposes lower average import tariffs than China does. Similarly US tariffs are lower than those that apply in most of the European Union. Tariffs are only part of the story. China has played loose and fast with intellectual property rights and has constructed an array of non-tariff trade barriers making it challenging for US companies to do business there.

In April Trump added teeth to his twitter rants kicking off a trade war with China. The first announcement was a 25% tariff on US\$50b of imports from China. These were imposed on the basis of protecting US intellectual property. China proportionately responded with its own round of tariffs on US imports.

In July a new tariff of 10% was introduced on a further \$200b of Chinese products. President Trump, when he announced this, noted "these tariffs will go into effect if China refuses to change its practices, and also if it insists on going forward with the new tariffs that it has recently announced. If China increases its tariffs yet again, we will meet that action by pursuing additional tariffs on another \$200 billion of goods." All up then, Trump is considering imposing tariffs on \$450b of Chinese imports. That is close to the total value of imports into the United States from China.

Predicting how trade battles play out is very challenging. The players have different objectives, none of which are clear, and the complex politics add a further layer of uncertainty. Trump can't back down now without a tangible victory and similarly President Xi of China can hardly roll over and let the US publically embarrass China. The stakes are high and the rhetoric adds fuel to a dangerous fire.



It is these high stakes that make predicting the impact of this trade bout difficult. Looking back at past trade wars would suggest that if things don't get worse from here the impact to global growth is likely to be minor and easily absorbed by markets. Goldman Sachs, the global investment bank, estimates an "increase in the average tariff rate similar to our expectation for the current episode usually lowers output by 0.2%. The trade balance typically improves — as trading partners usually only retaliate partially — but the effect is small."

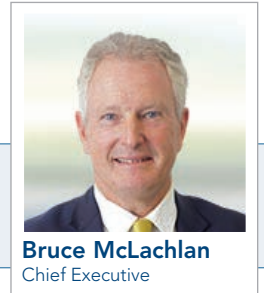
So if this plays out in line with history we don't have a lot to worry about. Of course the words "in line with history" and "Donald Trump" are not normally uttered in the same sentence. There is still a risk that this war gets out of control with a much greater impact on global growth and asset prices.

While we are not explicitly positioned for this outcome our portfolios have a cautious tone. We have a lower exposure to global shares than is normal. We expect inflation to rise — rising tariffs add to this risk — so have less invested in long-term fixed income investments than we would normally have. We have more cash than usual which provides both protection and liquidity if markets do come under pressure.

What's not talked about as much in the media is the effect on individual companies. Companies have got used to liberal trade policy. Supply chains are global and inventory levels of unsold intermediate and finished goods are typically low.

Take Apple for example. iPhones are assembled in China by Foxconn with sub-assemblies from throughout Asia all delivered just in time for a phone to be built and shipped to customers. Tariffs and more onerous non-tariff barriers will be a real problem for this business model. Apple is not alone in facing this risk. A trade war is likely to add cost to the supply chains reducing corporate profitability. We have little exposure to manufacturing but it's a dynamic we are watching closely.

All up there is some logic to this trade war. A reduction in intellectual property theft and a lowering of non-trade barriers would be good for the United States and good for the global economy. I for one do not expect China to so meekly roll over and suspect that tariffs around the current levels will be with us for a while.



## The compulsory financial lesson every teenager should receive

There is no manual for being a good parent. Most of us wing it on natural instinct, and the vast majority of children end up as good citizens. We also know many are financially challenged. Why is it that parents are generally good at teaching basic survival skills like personal safety and nutrition, but fall so materially short when it comes to monetary survival skills? The basics can be easily understood.

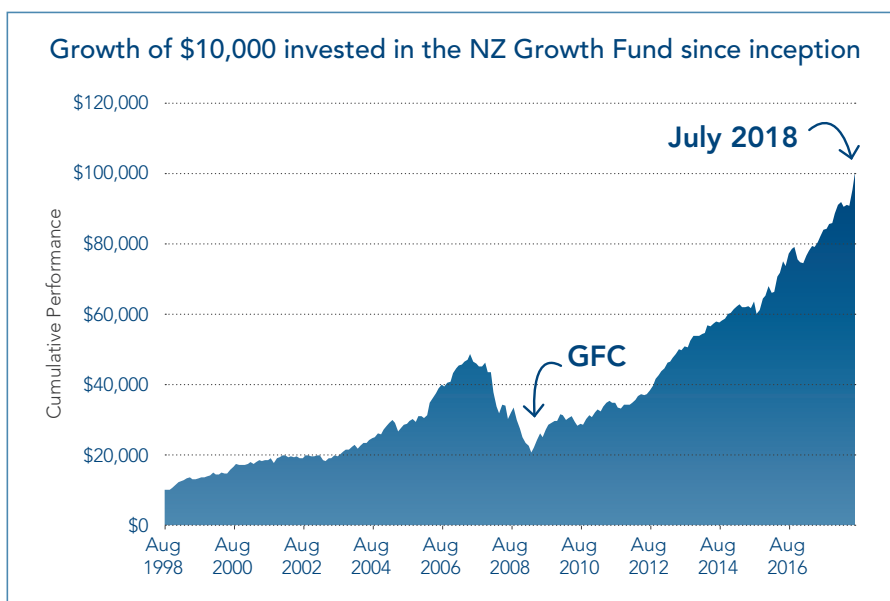
Fisher Funds will celebrate its 20th birthday in August 2018, and provide evidence of the most basic lesson that every teenager should learn. On August 1998 Carmel and Hugh Fisher launched the Fisher Funds New Zealand Growth Fund and the performance of this fund over the last 20 years is shown on the graph on this page.

This has been an eventful two decades. It started with the Asian crisis, endured the worst of the global financial crisis, multiple changes of government, new regulations, major natural disasters like earthquakes, company failures and so on. Despite all of this, \$10,000 invested in this fund in 1998 is still worth

around \$100,000 today. That is a compound return of 12.2%. Who would have thought this was possible with all of this negativity? This is no fluke and no get rich quick scheme. It is the disciplined following of basic monetary principles. Long term compounding, investing not gambling, diversification and holding the course with quality companies.

Why is it that the basics of long term investment in equities is not something that is shared with our younger generations? Teenagers are more likely to hear that shares are risky and “watch out for the next crash”, rather than the basics of equity investment. In today's new world where home ownership is dropping because of the excessive price levels, we need our younger generations to understand the value of equities as an alternative asset class to property and bank deposits.

Of course the Fisher Fund New Zealand Growth Fund has benefitted from the Carmel Fisher signature through most of the above period. The investment philosophy and process has been ingrained within the



business and is today continued on by a new wave of investment professionals in our investment team who are continuing and enhancing these philosophies and investment processes. This fund is truly a success story. It is also a demonstration of other New Zealand success stories. Companies like Freightways, Delegat Wines, Mainfreight and Ryman Healthcare have been long term investments of the fund and investors have profited from them.

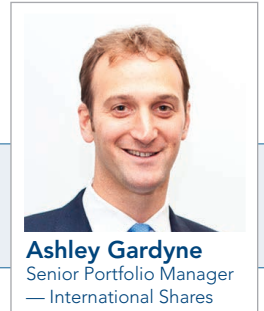
We at Fisher Funds will celebrate the 20 year milestone and marvel at the long term performance of one of our signature funds. Thank you to those of you who have stayed the course and reaped the benefit. Our prize is to endeavour to do this all over again in the next 20 years.

### Governance Changes

In late July we welcomed two new Directors to the Board, Guy Roper and Jennifer Moxon.

Guy is currently CEO of Port Taranaki since 2015 and also a Trustee of the TSB Community Trust while Jennifer is a professional Director having previously had a career for over 30 years at IBM.

Concurrently with these appointments there was also an end of an era. Carmel Fisher retired as a Director and that brought an end to the amazing 20-year ownership, executive and governance time at Fisher Funds since founding the business in 1998. Carmel sold her remaining shares in Fisher Funds in 2017, but had stayed on as a Director to ensure a successful transition of the business to the new controlling shareholder, the TSB Community Trust. Carmel's legacy will live on at Fisher Funds long into the future, as is evidenced by her launch fund, the New Zealand Growth Fund.



## Time to unfriend Facebook?

Facebook or Faceplant? Following weaker than expected earnings guidance on a recent investor conference call Facebook's share price tanked 20%.

On its recent results call, CFO Dave Wehner communicated that Facebook's revenue growth is expected to slow, and that, combined with higher expense growth, the company will have declining profit margins over the next three years. While a slowdown in revenue growth was expected (no company Facebook's size can grow revenue at 40% per annum for very long), the magnitude of expense growth caught the market off-guard and wiped \$120 billion off Facebook's market cap in one day. Facebook's intention to hire more staff and increase spending on security, data protection and content moderation is driving expense growth. They are doubling the number of staff in these areas to more than 20,000 people. These investments are aimed at reducing the spread of fake news, eliminating election interference and protecting personal data.

The question for investors is if this investment will impact the long-term profitability of the business, or if it will strengthen and future-proof Facebook. .

To briefly put this news in context, on the same conference call Facebook announced that advertising revenues grew over 40%, global users increased 11%, and earnings jumped 31% on the prior year. That is stunning performance for a company of this size.

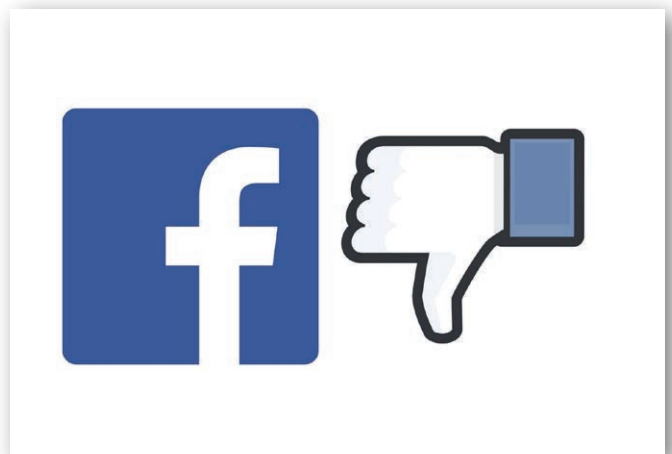
Occasionally management teams need to make difficult decisions that reduce the short-term earnings growth in order to strengthen the business and to grow more sustainably over the long term.

Facebook owns two of the world's largest media assets (Facebook and Instagram) and the two largest messaging platforms in WhatsApp and Messenger. Across these platforms they reach over 2.5 billion users who use them to engage with friends and

family, keep up with news and follow their interests. Advertisers are steadily increasing the proportion of advertising allocated to digital platforms, and therefore Facebook's ability to maintain and grow engagement across its community is central to its ability to take a large share of these ad dollars.

This recent step up in investment in security and content moderation, along with more transparency around data privacy, will increase trust and engagement by Facebook's community. This will ensure the company's longevity. Not only is this increased spend necessary, but by investing heavily in security and content moderation they are effectively raising the bar for any new entrants to the social media space — putting even further distance between Facebook and would-be competitors.

Ultimately these investments will help maximise the long-term value of Facebook. Some short-term pain, but for long-term gain.



### Facebook is becoming more valuable by the day

Most people and businesses get a lot of value out of Facebook's platforms — and they are gradually becoming more dependent on them.

Businesses that are embracing Facebook and Instagram are seeing great results. A furniture store near our office in Takapuna recently terminated its lease to sell its furniture online — mainly via Instagram. In doing so they saved considerable rent and staff cost. Social media can really help small businesses level the playing field against larger competitors. Small businesses (cafes, gyms, local retailers) no longer need to run expensive radio or newspaper adverts if they want to promote their businesses. For less than \$50 they could target 5,000 potential customers that fit the right demographic profile from an ad on Instagram. This is becoming ever important in a world where we are spending an increasing amount of time on social media and mobile devices, and less time watching TV.

Facebook has already demonstrated that it is a very powerful advertising platform. Instagram is hugely popular and has just passed 1 billion user mark. This is still only half the number of users of Facebook, but it is rapidly catching up and is starting to show its promise as great place for businesses to advertise. Facebook and Instagram are well positioned to capitalise on its unprecedented global advertising reach.

## Contact us

Frank Jasper  
**Chief Investment Officer**  
Phone 09 484 0344 | Email [frank@fisherfunds.co.nz](mailto:frank@fisherfunds.co.nz)

Kate Meyers  
**Institutional Client Relationship Manager**  
Phone 09 487 2637 | Email [kate@fisherfunds.co.nz](mailto:kate@fisherfunds.co.nz)

# Market Movements

As at 31 July 2018

Stock Markets*	Closing Values	Changes over:			
		1 Mth %	3 Mths %	6 Mths %	12 Mths %
S&P Developed LargeMidCap - (Local Curr)	775	3.1	4.6	0.8	13.0
S&P Developed LargeMidCap (\$NZ)	N/A	3.1	8.8	10.1	25.1
S&P Global LargeMidCap (\$NZ)	N/A	2.5	6.2	5.8	22.8
USA - S & P 500	5550	3.7	6.9	0.7	16.2
USA - Nasdaq	8869	2.2	8.9	4.1	22.1
Japan - Topix	2582	1.3	-1.1	-3.4	10.6
UK - FTSE100	6730	1.5	4.1	5.3	9.4
Germany - DAX	12806	4.1	1.5	-2.9	5.7
France - CAC40	14430	3.5	2.0	3.3	11.7
HK - Hang Seng	79067	-0.5	-5.4	-10.9	8.6
Australia - S & P 300	63088	1.3	5.8	6.0	14.7
NZ-S&P/NZX 50 Gross Index (inc imp credits)	10696	-0.2	5.8	6.2	17.3
NZ-S&P/NZX 50 Gross Index (excl imp credits)	8922	-0.2	5.7	5.7	16.0
Market Volatility - VIX	12.8	-20.3	-19.5	-5.2	25.0

New Zealand Property		%	%	%	%
S&P/NZX All Real Estate (inc imp credits)	1342.5	1.6	6.6	5.7	12.3
S&P/NZX All Real Estate (exc imp credits)	1302.1	1.6	6.3	5.2	11.3

Ten Year Bonds	%	Yield Changes			
USA	2.96	0.11	0.01	0.24	0.64
Japan	0.06	0.03	0.01	-0.02	-0.01
United Kingdom	1.34	0.07	-0.09	-0.17	0.11
Australia	2.66	0.02	-0.12	-0.13	-0.02
New Zealand	2.76	-0.09	-0.25	-0.14	-0.23

90 Day Interest Rates	%	Yield Changes			
USA	2.03	0.10	0.16	0.57	0.94
Japan	0.07	0.00	0.00	0.00	0.01
United Kingdom	0.80	0.12	0.09	0.28	0.51
Australia	1.97	-0.15	-0.05	0.22	0.28
New Zealand	1.91	-0.09	-0.11	0.02	-0.04

	Closing Values	Changes over:			
		1 Mth %	3 Mths %	6 Mths %	12 Mths %
<b>Bond Indices</b>					
S&P/NZX Bank Bills 90-Day	711.57	0.18	0.51	0.98	1.97
S&P/NZX NZ Government Bond Index	1704	0.44	1.70	2.49	4.26
Barclays Capital Global Aggregate Index (Hedged NZD)	N/A	0.03	0.60	0.88	1.84

		%	%	%	%
<b>Hedge Funds &amp; Commodities</b>					
HFRX Global Hedge Fund Index (USD)	1263	-0.1	-0.1	-3.4	1.4
DJ-UBS Commodity Index Total Return	176	-2.1	-4.2	-4.0	2.7
Gold (US\$/ounce)	1223.70	-2.2	-7.0	-8.6	-3.4
Oil (US\$/barrel)	74.19	-4.2	-2.3	9.5	42.7

		%	%	%	%
<b>Currencies</b>					
NZD / USD	0.6808	0.6	-3.4	-8.0	-9.2
NZD / EUR	0.5819	0.3	-0.2	-2.1	-8.5
NZD / GBP	0.5190	1.2	1.5	-0.3	-8.7
NZD / AUD	0.9158	-0.1	-1.9	0.2	-2.5
NZD / YEN	76.21	1.6	-1.2	-5.7	-8.0
Trade Weighted Index	72.96	-0.7	-2.6	-2.6	-7.0

\*Total Return Indices. Indices are net of offshore tax.

Source: Thomson Reuters Datastream

Disclaimer: The content of this publication is intended for Fisher Institutional wholesale clients. It may not be circulated or copied without the express permission of Fisher Institutional. No responsibility or liability is accepted by Fisher Institutional or any of its related companies including Fisher Funds Management Limited (Fisher Funds) for the accuracy of any statement, opinion or advice contained in this publication, except to the extent that statutory liability cannot be excluded by law. While all reasonable care has been taken in presenting this publication, the contents are intended to provide general information in summary form only and do not constitute legal, financial or business advice and should not be relied on as such. Fisher Funds and its related companies do not provide any representation or warranty that the information is free from errors, omissions or inaccuracies. You should rely upon your own enquiries or research before making any decisions or taking any action based upon information contained in this publication. This information is current as of August 2018 and is subject to change without notice.

© 2018 Fisher Institutional. All rights reserved.