fisher funds

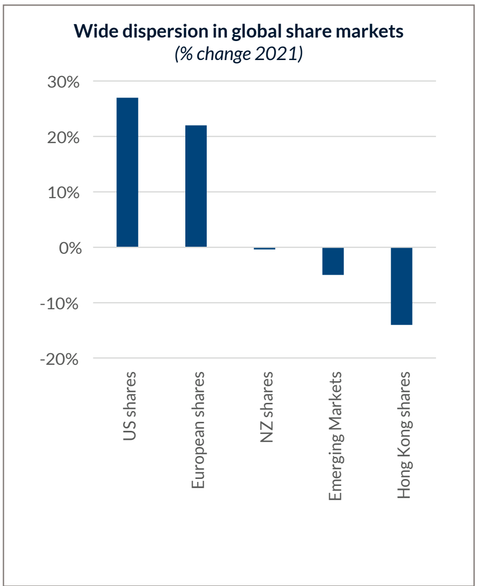
MARKET INSIGHTS

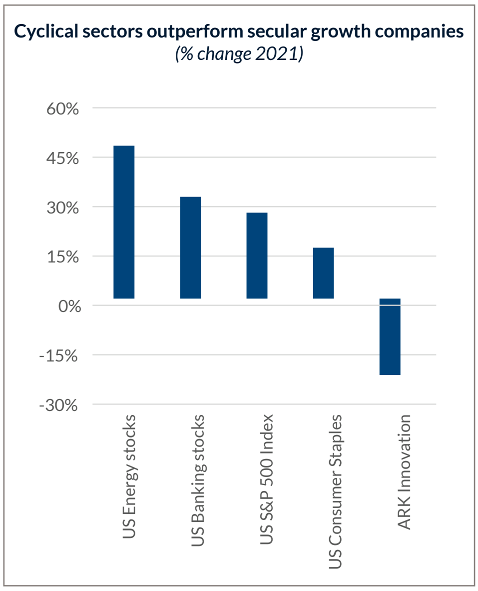
December 2021 Quarter

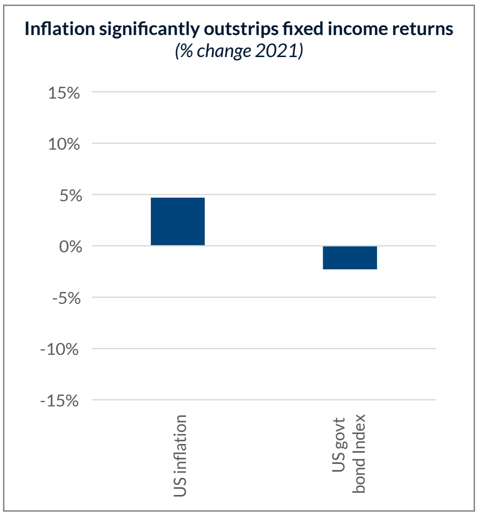
AN EVENTFUL YEAR IN MARKETS, SHOWING THE VALUE OF DIVERSIFICATION

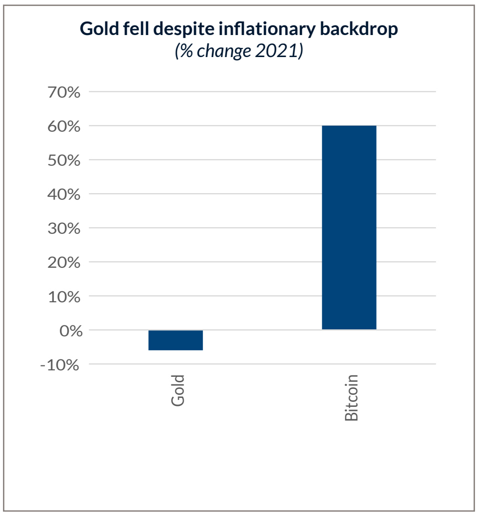
Ashley Gardyne, Chief Investment Officer

2021 was a year where the economic landscape was impacted by the aftershocks of COVID - supply chain disruptions, inflation, and the resulting rise in interest rates. This led to a wide dispersion in the outcomes for investors across different markets and asset classes. The US share market was up 27%, fuelled by economic reopening, while the New Zealand market was down slightly, partly due to rising domestic interest rates. Rising interest rates also led to the rare feat of negative returns in global bond markets, with the Bloomberg Global Aggregate Index falling 5% - the most since 1999. Sector performance was also very different compared to recent years, with many large cap tech companies like Netflix, Salesforce and Amazon underperforming the market, while the inflationary environment and higher interest rates led to outperformance by the energy and banking sectors. Many of last year's market darlings are also significantly off their highs - like Peloton (-79%), Zoom (-70%) and the ARK Innovation ETF (-46%). Gold, an often-touted inflation hedge, didn't live up to its promises last year - falling 4% despite surging inflation expectations. In contrast, Bitcoin, claimed by some to be the 'digital gold', surged.









All of this shows the importance of diversification. A portfolio containing only the New Zealand share market index and bonds would have seen negative returns for the year, but introducing international shares or property & infrastructure would have led to solid portfolio returns. In this low interest rate world, we continue to believe that active management can be an important source of enhanced returns.

Where to from here? 2022 will be different with its own opportunities and challenges

The central economic themes this year could be very different to 2021, and the drivers of financial markets almost certainly will be. The consensus view seems to be that supply chain issues will take time to resolve, inflation will persist for a while longer before normalising, and central banks around the world will hike interest rates. For markets to move dramatically there will need to be a major shift in this narrative, or some other unexpected shock - either positive or negative.

Like any year, new challenges will present themselves. Will central banks hike interest rates too quickly and harm the real economy? Will China's slowing economy and troubled property market have a bigger than expected impact on the global economy? Or perhaps the hangover from last year's attempt to solve the supply chain issues (by ordering ahead and increasing inventories) will result in an oversupply issue and an economic slowdown in 2022?

The challenges we will face and the investment opportunities that present themselves are difficult to predict ahead of time. But there will be opportunities for active investors, and having the right investment strategy can help ensure investors are prepared to capitalise on these.

Grappling with how to build wealth and a retirement income in a low return world

Investors are still grappling with the same big question as last year – how to outrun inflation and create a reliable income in retirement.

In his book, The Intelligent Investor (which was revised a number of times), famed value investor Benjamin Graham used to give guidance on the mix of shares and bonds investors should hold based on the valuation level of the share market compared to the level of interest rates. In prior bull markets (like the 1990s) interest rates have typically increased as the market cycle progressed, giving investors an incentive to start reducing their share market holdings and increase their bond holdings as the cycle progressed. But we are in unprecedented times-despite a decade of strong equity returns, interest rates are still stuck near rock bottom – not the 7% government bond yield we saw in 1999. This time there is a higher opportunity cost for investors taking a more defensive position.

Unfortunately, there are no silver bullets or elegant solutions to this conundrum. It will be harder than in the past to generate high inflation adjusted portfolio returns. That said, there are some things to keep in mind to improve your long-term prospects.

Firstly, adopt the mindset of an investor, rather than a saver. Rather than just storing money in the bank, successful investors are willing to accept some short-term volatility in exchange for better long-term returns. Investing in growth assets like shares and property is likely to deliver materially better long-term outcomes than overly defensive strategies.

Second, watch out for fishhooks. Much like the late 1990s we are seeing excesses in parts of the market. Many thematic growth stocks in hot sectors, like genomics, electric vehicles, cybersecurity and fintech are trading at extremely stretched valuations and may result in significant losses for unwary investors. There is similar behaviour going on with the cryptocurrencies and NFTs. The record level of money flowing into Initial Public Offerings (IPOs), often of unproven businesses, is also a sign of the times. Keeping it simple, avoiding businesses you don't understand, and avoiding crowd favourites is likely to pay dividends.

Third, be ready to capitalise on opportunities when they arise. As we saw during the COVID sell-off, the best opportunities often present themselves at unexpected times.

Finally, like New Year's resolutions, short-term attempts to build wealth seldom work. What works is having a growth orientation and long-term strategy that you stick with through thick and thin. Consistency is the key. Our investment approach has stood the test of time and we intend to execute on it consistently again this year, taking advantage of any new opportunities that appear along the way.

Ashley Gardyne | **Chief Investment Officer**

NEW ZEALAND EQUITIES

Sam Dickie, Senior Portfolio Manager

Fourth quarter portfolio developments

Xero was the best performer in the portfolio for the fourth quarter, delivering an impressive improvement in its key business metrics, which demonstrate its attractive and improving business economics, and the strength of its customer proposition. Customer lifetime value increased +61% to $9.9 billion, far ahead of expectations, reflecting falling churn, pricing power, and increasing gross margin. The strong performance in Australia and New Zealand and the strong SaaS metrics mean the long-term power of the business model is potentially greater than we expected.

Fisher & Paykel Healthcare also delivered against the backdrop of a weak local market. The company reported a strong first half result, ahead of expectations, boosted by another wave of COVID hospitalisations in the US, Asia, and certain countries in Europe. The bulk of the strength was in sales of new hardware in the Hospital division, which continues to grow the installed base of F&P products in both established and new customers (70% of hardware sales were outside of the core markets of US/Europe).

There is increasing evidence to suggest that nasal high flow product usage will structurally increase even as COVID wanes. This is because (1) the therapy has stood up in a crisis and doctors new to the products have now had first-hand experience in seeing its efficacy; (2) there is a still a sharply growing installed base of F&P hardware; (3) clinical evidence is supportive; (4) F&P is increasing its sales force to provide education to recent adopters and increase consumable usage. Market expectations do factor this as medium-term forecasts remain in line with the pre-COVID trajectory and imply meaningful under-utilisation of the much higher installed hardware base.

Economic re-opening plays Serko and Vista were a drag on Q4 performance.

Serko announced its first half result and simultaneously raised $85 million new equity from shareholders. The result and full year revenue guidance were below expectations, given COVID lockdowns in Australia and New Zealand and a slow resumption to travel in the US and Europe.

The Booking.com for Business (BfB) customer migration has completed successfully with over 300,000 customers transferred and over 30,000 new customers signing up. The platform is currently ramping up slowly with a run rate of 1000-1500 bookings per weekday, which represents less than 10% of the initial opportunity due to low travel numbers.

The opportunity remains intact and revenues will ramp up as COVID eases. Serko is accelerating the development of additional functionality for the BfB platform, which will increase the size of the revenue opportunity. It is also looking to expand to cater to Booking Holdings' other properties (RentalCars.com and Agoda). Serko has a very large and under-penetrated market ahead of it and the equity raise is to accelerate the pace of development to capture more than its fair share.

Vista's share price fell -12% during the quarter. The market is concerned that an increase in COVID lockdowns in Europe and the emergence of the Omicron variant will impact the near-term outlook for its exhibitor customers.

The company helped allay these fears late in the quarter when it re-affirmed revenue and earnings guidance. Industry health was improving and movie attendance was at 70% of pre-COVID levels before the release of the hugely successful Spiderman: No Way Home. The movie grossed more than US$260m in its first three days of release, the second highest grossing opening weekend of all time in the US domestic market. Cinema operators are cash flow positive at around 60% occupancy, and we don't expect severe cinema closures because of Omicron at this stage.

We re-introduced EBOS into the portfolio

EBOS has proven over a long period that it is the leading player in its core business of Australian pharmaceutical distribution. Its moat is based on being the lowest cost and highest efficiency operator in this defensive industry. It is the largest player and has the best processes and systems to deliver reliable service at low cost to its pharmacy customers.

We had previously removed the company from the portfolio in 2018 due to some concerns including its model being tested by new competitive threats and the modest industry growth rate in its core business. In the meantime, EBOS has extended its strong track record under CEO John Cullity, emerged with its moat firmly intact, and delivered growth through market share gains and entering higher growth adjacencies. A capital raising to fund a new acquisition gave us the opportunity to re-enter the stock at an attractive price.

Our re-entry was timely as during the month EBOS announced it was buying Australian medical devices distributor Lifehealthcare and raised new equity to partly fund the transaction. This is a logical acquisition in line with the company's previously stated strategy. Lifehealthcare is a leading player and EBOS having made several smaller medical device distributor acquisitions in recent years as this is an attractive and growing market. The transaction also provides a sensible entry point to South-East Asia through the Transmedic subsidiary, which still has its founders with skin in the game as minority shareholders. We participated in the equity raising.

Don't sneeze at the defensive characteristics of the New Zealand market

New Zealand equities had a disappointing quarter (-1.8% versus global equities +7.9%) and year (-0.4% versus global equities +22.3%). We have talked about the reasons throughout the year:

Firstly, New Zealand is a defensive and much more interest rate sensitive market than global equities. The NZX50 has five times more companies sensitive to interest rates than other global markets. So, low growth companies like utilities and property do relatively well when interest rates are falling, and poorly when interest rates are rising. With global interest rates (using the US 10-year bond rate as a proxy) almost doubling for the year, this provided a difficult headwind.

Secondly, the strongest market performers globally this year have been cyclical companies or re-opening plays. Investors have been buying companies that benefit as economies re-open - so oil companies, banks and industrial commodity companies have done very well. New Zealand has very few of these businesses.

Finally, as always in the relatively small New Zealand market, there are idiosyncratic or single stock reasons too. For example, the New Zealand gentailers were added to a US based global renewables index last year and their stock prices spiked irrationally (Meridian and Contact's share prices were up 60-80% in a few short months into the end of last year). This year the market has been digesting those gains and these stocks have been falling.

New Zealand's defensive characteristics come in handy when we are not in a global equity bull market. In the rare times global equities have corrected or pulled back in the last 2-3 years, New Zealand equities have outperformed every time – as can be seen in the table below.

NZ equities outperform global equities in a correction

Start	End	Global	NZ	NZ vs global
30 Apr 19	31 May 19	-5.9%	+1.0%	+6.9%
26 Jul 19	15 Aug 19	-6.1%	-1.0%	+5.1%
19 Feb 20	23 Mar 20	-33.6%	-29.1%	+4.5%
2 Sep 20	24 Sep 20	-7.4%	-1.8%	+5.6%
12 Oct 20	30 Oct 20	-6.9%	-2.2%	+4.7%
7 Sep 21	6 Oct 21	-4.7%	-1.2%	+3.5%
19 Nov 21	3 Dec 21	-4.0%	-0.5%	+3.5%
4 Jan 22	7 Jan 22	-1.9%	-0.6%	+1.3%

AUSTRALIAN EQUITIES

Robbie Urquhart, Senior Portfolio Manager

Uncertainty affiliated with the Omicron COVID variant and inflationary concerns have tempered share price gains as we end the year.

Sonic Healthcare (+14.7%) was our best performing company in Q4. It continues to benefit from heightened COVID testing volumes. Credit Corp (+10.3%) was another top performer for us in Q4. It was assisted by the acquisition in December of a consumer leasing business in Australia. The acquired business diversifies Credit Corp's revenue base and boosts its future earnings growth.

Domino's fell -26.4% in Q4 as its growth rates in the key Japanese market subsided. Despite this, Dominos has had a good year returning +38.2% over 2021. Two of our bank shareholdings, Westpac (-15.7%) and CBA (-3.2%) also dragged down Q4 returns as pricing pressures and elevated costs weighed on bank margins.

A bumper year for new listings on the Australian share market

Assisted by low interest rates and significant fiscal and monetary policy stimulus, 2021 has been a good year for share markets globally. Investor appetite for equities has been strong, leading to a boom in new companies listing on the Australian stock exchange (known as Initial Public Offerings or IPOs).

In total, close to 200 companies listed on the ASX during the year. Eight of these listed with valuations of over A$1 billion. It was the biggest year of new listings in Australia since the mining boom in 2007. Like then, resources and mining companies made up a large number of new listings in 2021.

This environment has also proved conducive for mergers and acquisitions (M&A). A private consortium led A$24 billion acquisition of Sydney Airport proved that companies of any size could end up as takeover targets.

Applying our investment approach to IPOs

We welcome new companies listing on the stock exchange as it broadens the range of investments available to us. However, we approach IPOs in a cautious manner.

When selling a house, a vendor and real estate agent can be counted on to present the house in the best possible light. Photos may be taken with wide angled lenses or home décor might be staged for sale.

Similarly, when a company lists, the owners (vendors) of the company and their agents (investment banks) are incentivised to highlight the positives of the business. IPO processes are typically completed on compressed timetables, creating a sense of urgency and helping the marketing process.

We seek to avoid getting caught up in this hype. We apply the same disciplined investment process in evaluating IPO candidates as we do for any existing listed investment opportunity.

We look to understand the breadth and durability of the core competitive advantage of the company. We evaluate management and assess their track record. We consider whether a company is meeting an unmet customer need. We gauge whether it can grow revenues in good and bad economic environments. We assess a company's valuation. And we compare IPO candidates against the quality of our existing portfolio companies. If these thresholds are met, we will actively participate in the IPO process.

During 2021, many candidates didn't fit our quality and growth investment criteria (e.g. resources companies) and were screened out quite early in the IPO process.

We pursued detailed work on a handful of companies that looked interesting to us. We worked closely with the investment banks from an early stage in the IPO process to ensure we could complete our due diligence within the prescribed IPO timetable. In the end, we did not buy shares in any IPO in the year. However, we will be keeping our eye on some of these companies over the next few years.

A number of our companies have also grown through M&A this year

The surge in global M&A activity has kept us busy. A number of our portfolio companies expanded by acquiring businesses during the year including Credit Corp (mentioned above). We have also previously written about Carsales' expansion into the United States through an acquisition earlier in the year which we supported.

In December, CSL launched a large A$16.4 billion takeover offer for Vifor, a Swiss based pharmaceutical company. Vifor specialises in nephrology (kidney complications), dialysis and iron deficiency therapies. CSL has been researching Vifor over several years. With Vifor's revenue growth temporarily impacted by COVID and with its share price languishing, CSL launched its takeover offer.

Vifor adds a new division to CSL's armoury. This reduces its reliance on plasma therapies. CSL also likes the rising demand for Vifor's market leading renal products. This is driven by ageing demographics in many countries, dietary trends and an associated increase in diabetes. With its global reach and scale, CSL believes it can help Vifor accelerate its distribution of these products. CSL believes that Vifor's longer term revenue growth rate and profitability is a match for its core plasma business. It also sees this as a compelling acquisition given it is being undertaken at a discount to CSL's overall valuation.

CSL have a long track record as an astute acquiror of peers. Its equity raising to help fund the deal was well supported by investors.

Macquarie is well positioned to grow

We were pleased to add Macquarie Group to our portfolio in December. Macquarie has grown into a high-quality diversified financials business with over 65% of its income generated outside of Australia. Two thirds of its income is stable and predictable. The balance is derived from more volatile financial markets activity, like investment banking.

Macquarie is well run. It has a track record that includes over 50 years of unbroken profitability and strong share price performance. Culture is critical to its success. It invests in its people and has a history of developing and promoting internal talent.

Macquarie is ramping up its investment in fast growing areas of the global economy such as the growth in renewable energy generation. To facilitate this, Macquarie has bolstered its balance sheet by raising A$2.8 billion in equity in Q4. It also recently cut its dividend to retain more cash that it can use to invest in these growth projects. It is well positioned for growth.

We sold our Rio Tinto shareholding to help fund the addition of Macquarie to the portfolio.

We remain confident in the longer-term outlook for our portfolio companies

As always, entering 2022 brings with it a range of uncertainties for equity markets including (again!) how much COVID will disrupt our lives for another year.

We remain confident that our portfolio mix of high quality and growing companies will stand us in good stead over the next few years.

SELECT INTERNATIONAL EQUITIES

Ashley Gardyne, Senior Portfolio Manager

A final surge in the fourth quarter saw global markets end a strong year at all-time highs. The gains came despite temporary volatility caused by the Omicron variant and global central banks starting to unwind their accommodative monetary policy settings.

A strong year for global equities

It has been another strong year in global share markets, with the US S&P 500 Index up +27% and the MSCI World Index up +20%, resulting in solid gains for many investors. While global markets have rallied, a lot has gone on behind the scenes economically. COVID aftershocks, including supply chain disruptions and elevated consumer spending featured strongly, and the resulting inflation and interest rate increases have created uncertainty for investors. Despite the uncertainty, global markets have continued to climb given a strong economic impulse caused by reopening, policy stimulus and a resilient consumer. This has fuelled strong corporate earnings growth, particularly in the US, where over 80% of companies reported earnings growth ahead of market expectations in the most recent quarter. US corporate earnings are now more than 30% ahead of 2019 levels, despite the business disruption caused by COVID.

It isn't only the US market that has had a strong run. Markets in Europe, the UK, Japan and Australia were also up double digits. The only black mark was China and emerging markets more generally, with the MSCI China Index and the MSCI Emerging Markets Index falling -22% and -5% respectively.

Fourth quarter portfolio developments

Dollar Tree (+47%), a US discount retailer, was the top performer in the portfolio in the quarter. Shares rallied on news that the company was moving away from its fixed $1 price point. The announcement that they are 'breaking the buck' and rolling out a new US$1.25 price point in all 8,000 Dollar Tree stores is a positive step given the inflationary pressure the company has been facing. Freight costs have been a significant headwind for the company recently and the 25c price increase should help offset cost inflation and lift profit margins back to prior levels. Even with this price increase, we still believe Dollar Tree retains a very strong customer value proposition compared to peers. The rollout of $3 and $5 price points will also allow the company to add new categories for customers and offer the prospect of higher sales growth and margins in the years ahead.

US homebuilder NVR (+23%) had a strong quarter on the back of housing data in the US that continued to show a robust demand environment. Low interest rates and demographic-based tailwinds (millennial household formation) continue to support the backlog of new orders, while tight housing inventories and the difficulty ramping up production quickly have helped push US house prices up almost 20% in the last year. As a result, we expect a number of years of growth in homebuilding activity (at elevated margins), as the industry plays catch-up after a decade of under-building.

Signature Bank (+19%) continues to perform well. An update during November was further evidence that the bank is outpacing peers in loan and deposit growth. While 2021 has been a standout year with assets up 70% year-over-year, we continue to think the company can produce robust growth going forward. The bank has a unique operating model of hiring high-performing banking teams from competitors, incentivising them well, and providing a high-touch service for clients. This has allowed Signature Bank to continually grow organically and enter new regions and markets. With best-in-class profitability and excess cash on the balance sheet to deploy, we believe earnings can grow ahead of deposit and revenue growth in the coming years.

On the negative side of the ledger, PayPal (-28%) sold off during the quarter after the company lowered its 2021 revenue guidance and provided 2022 growth expectations that were slightly below market expectations. The weaker guidance was due to eBay transitioning away from PayPal (a temporary headwind which should abate later in 2022), but also due to more consumers shopping in-store this holiday season (to reduce the risk of supply chain disruptions stopping ecommerce parcels arriving in time for Christmas). On a positive note, PayPal announced a partnership that will allow Amazon customers to pay with PayPal's Venmo app, which should drive incremental payment growth over time. PayPal are also gaining traction in the buy now pay later space. Overall, we believe PayPal is executing effectively on its long term strategy, while growing its payment volumes at over 30% per annum and its revenue and earnings at close to 20% per annum.

Alibaba (-20%) continued to slide this quarter after reporting earnings that showed slowing e-commerce growth due to Chinese economic headwinds and intense competition. Over time there are three variables that will drive Alibaba's share price: its e-commerce market share, profit margins and the level of investment required to keep driving growth. We think the market is being too negative on the eventual outcome of these drivers and we remain confident that growth in Alibaba's core e-commerce business will eventually accelerate. We also remain positive on the company's international retail and cloud computing segments which both continue to grow strongly.

StoneCo (-51%), a Brazilian payment service provider, was the worst performer in the portfolio during the quarter. While StoneCo's third quarter earnings showed that it continues to grow its customer base and payment volumes rapidly, profitability missed expectations and weighed heavily on the company's share price. The main concern from the earnings release was the company's rising financial expenses (and compressed margins) due to increasing interest rates, which it has not yet been able to pass on to customers. The positive news in the quarter was that the company continues to sign on new customers at a rapid rate, more than doubling the client base in the past year to 1.3 million active clients. We were disappointed by StoneCo's results and are doing more research to understand the company's ability to pass higher interest rates through to customers. We believe that the long-term tailwinds behind the company are still intact, and the company's strategy and products are still being well received by customers.

While the recent performance of Alibaba, PayPal and StoneCo has created a disappointing drag on performance, we believe these are quality businesses that are well positioned to deliver continued growth and strong shareholder returns in the years ahead.

NEW ZEALAND CASH AND FIXED INTEREST

David McLeish, Senior Portfolio Manager

The dawn of a new year has long been marked by a celebration of what was and what lies ahead. But after such a torrid year, fixed income investors like us will probably just happy to see the back of 2021. Looking ahead though, we see reason to be more optimistic about the prospects for this beleaguered asset class in 2022.

Rising interest rates across a wide cross-section of fixed interest assets have hurt returns

As the going rate of interest in an economy rises, the price of all existing fixed interest assets falls. This is because the fixed rate of interest which previously issued assets pay become less attractive to investors who can now receive a higher rate of interest from newly issued bonds.

This has been a strong and persistent headwind to performance throughout the year.

Higher interest rates have improved the outlook for fixed interest returns

The very same interest rate rises that caused fixed interest asset prices to fall in 2021 are now a source of optimism.

As the name suggests, fixed interest assets pay a fixed amount of interest throughout their life. This means, the lower the price you pay for an asset like this, the higher the income each dollar invested will generate.

This income, also known as the assets yield, is one of the most important drivers of return. So, to have our flagship domestic fixed interest portfolio start 2022 with a yield of 2.6%, a whole 1.4% more than this time last year, this has markedly improved the return outlook for the portfolio this year.

Inflation remains unpredictable. But price pressure should begin to alleviate

The other major factor which impacts a fixed interest assets return is any change that occurs in its price. As we saw in 2021, this can be meaningful because interest rate movements impact the price of a fixed interest asset.

We believe the efforts of central banks to tackle inflation by curtailing consumer demand through higher interest rates strengthens the already strong case that inflation will retreat from its current lofty levels during 2022.

This is not to say inflation will fall back quickly. Instead, we think a combination of persistent global supply chain issues and pent-up consumer demand will keep inflation elevated during the early part of 2022. But even without much higher interest rates, we expect today's level of inflation to reduce consumer appetite, causing price pressures to self-correct lower.

Fixed interest assets already imbed an expectation for interest rate rises

If our expectations turn out to be off the mark, we think the already higher yields offered on fixed interest assets today provide a valuable safety net. This is because yields imbed an expectation for what interest rates will be in the future. And this 'market' expectation is for interest rates to move higher throughout 2022.

In New Zealand, short-term fixed interest asset yields include an expectation that the Official Cash Rate will rise six times this year, each time by 0.25%. Therefore, because this is already factored into asset yields today, even if those hikes were to come to pass, investors should not expect the price of these assets to be meaningfully impacted.

By taking the Official Cash Rate to 2.5% by November, the Reserve Bank of New Zealand will have to deliver the quickest series of interest rate hikes in its history. This will be a tall order in our opinion. It is because of this that we do not expect the price of New Zealand fixed interest assets to be as impacted by interest rate changes this year.

A tactical shift towards local fixed interest assets is underway

The New Zealand market is pricing the most aggressive interest rate hiking cycle of any of the major global fixed interest markets we follow. This makes New Zealand fixed interest assets attractively priced relative to offshore assets.

It is for this reason we have recently begun increasing our allocation to local fixed interest assets at the expense of foreign assets.

PROPERTY AND INFRASTRUCTURE

Sam Dickie, Senior Portfolio Manager

Fourth quarter portfolio developments

US railroads were the standout performers in the fourth quarter. Union Pacific and Norfolk Southern rebounded strongly after a period of underperformance, and both posted better than expected profits for the third quarter. This solid performance was driven by strong pricing in a tight freight market, with higher truck spot rates increasingly reflected in rail pricing. The companies also both delivered impressive productivity improvements from their Precision Scheduled Railroading (PSR) initiatives despite challenges from congestion and delays due to supply chain disruption plus bad weather.

Our global airport holdings were a drag on performance in the quarter. The stop/start nature of global border re-opening and the emergence of Omicron negatively impacted global airports during the quarter. More than 30 countries have closed their borders to some nations and others have imposed stricter measures to curb the spread of Omicron. We continue to take a long-term view. We will travel again, pent up demand will be significant, and our global airports are strongly positioned to capture this inevitable rebound.

Targeted mergers and acquisitions (M&A) drive value

Equinix and American Tower both use targeted M&A to expand globally and bolster capability.

Equinix announced its expansion into Africa through the acquisition of MainOne, a leading West African data centre and connectivity solutions provider. MainOne is in Nigeria, Ghana and Côte d'Ivoire. The deal, at 14x EBITDA and with an Enterprise Value of US$320M, is expected to be immediately accretive to earnings.

This is Equinix's first entry into Africa, and they have a long-term strategy to be the market leader on the continent. MainOne has extensive telecoms assets to support its position as a leader in low-latency connectivity, with a submarine network extending 7,000 kilometers from Portugal to Lagos, Accra and along the West African coast, with landing stations in Nigeria, Ghana and Côte d'Ivoire. Additionally, it owns a terrestrial network of more than 1,200 kilometers of terrestrial fibre in Lagos, Edo and Ogun States.

The deal is a long-term bet. The African market is small currently, but the sub-Saharan population is estimated to double over the next 30 years to 2.5 billion, led by Nigeria, which will overtake the U.S. as the world's third-most populous country. Importantly, the UN also predicts that more than half of Africa's population will live in cities by 2040, eight of which will be mega-cities of over 10 million inhabitants. This will drive demand for data and connectivity, and it makes sense for Equinix to get a foothold in the market now with a modest initial investment.

We like the acquisition, as it is done on sensible economic terms and continues Equinix's strategy of using selective M&A to broaden geographic leadership and be the provider of choice for global enterprises.

American Tower pulled back intra-quarter due to its unexpected deal to acquire US data centre business CoreSite. American Tower is acquiring CoreSite to help it pioneer the development of a leading “edge computing” offering, which will move elements of cloud data processing closer to the user (computers/mini-data centres at tower mast sites) as future applications require increasingly lower latency.

We can see why American Tower wants to own and control the edge opportunity entirely in house, but much of the future of edge computing is yet to take shape, so it will take some time to uncover how much value the deal will create.

The company admits that this opportunity is not likely to be meaningful in the near term and it has moved early and paid a full price to put its foot on a high-quality asset, with no near-term value creation. CoreSite has 25 retail data centres in high quality US metro locations near internet “on-ramps” and with a high number of interconnects. We believe CoreSite is an attractive business in its own right. We see little downside from the acquisition, and the potential for significant upside if they execute on the edge computing opportunity.

Infratil has been busy

After exiting its highly successful Tilt investment, Infratil has been busily re-investing the proceeds.

In December Infratil announced the further expansion of its diagnostic imaging business, with Bay Radiology to join Pacific Radiology and Auckland Radiology Group as part of the broader platform. Infratil’s New Zealand diagnostic imaging business now employs 141 radiologists across 70 clinics through the combination of the three businesses. Infratil has now invested $700 million across Australia and New Zealand developing the diagnostic imaging platform.

This capped off a busy quarter for Infratil. Earlier in the quarter the company announced a £130 million investment in Kao Data, a UK datacentre business focused on high performance computing. Clients include Nvidia, which has the UK’s most powerful supercomputer on Kao Data’s campus. The business is in the early stages of development, but Infratil hopes to grow it to a £500 million platform in time.

Key portfolio investment Canberra Data Centres (CDC) purchased a new site in Melbourne during the quarter and expects to begin construction in the first half of 2022, contingent on signing an anchor tenant. The new site will eventually provide 150 megawatts of capacity and takes CDC’s total planned capacity to 700 megawatts. This follows CDC’s expansion into Sydney in 2018 and Auckland in 2021, with Microsoft acting as a strong anchor tenant in those locations.

In early January 2022, Infratil announced a 15% increase in the independent valuation of its CDC stake as at December 31 2021. The previous valuation update was only six months prior.

MARKET MOVEMENTS

As at 31 December 2021

Stock Markets*	Closing Values	Changes over: 1 Mth %	3 Mths %	6 Mths %	12 Mths %
S&P Developed LargeMidCap - (Local Curr)	1247	4.0	7.9	8.5	24.2
S&P Developed LargeMidCap ($NZ)	N/A	4.0	9.7	11.8	31.7
S&P Global LargeMidCap ($NZ)	N/A	3.1	7.3	7.8	24.8
USA - S & P 500	9987	4.5	11.0	11.7	28.7
USA - Nasdaq	18660	0.7	8.4	8.2	22.2
Japan - Topix	3179	3.4	-1.7	3.5	12.7
UK - FTSE100	7314	4.8	4.7	6.8	18.4
Germany - DAX	15885	5.2	4.1	2.3	15.8
France - CAC40	20358	6.5	9.9	10.3	31.9
HK - Hang Seng	71788	-0.3	-4.7	-17.9	-11.8
Australia - S & P 200	86118	2.7	2.1	3.8	17.2
NZ-S&P/NZX 50 Gross Index (inc imp credits)	16054	2.6	-1.7	3.4	0.2
NZ-S&P/NZX 50 Gross Index (excl imp credits)	13034	2.5	-1.8	3.0	-0.4
Market Volatility - VIX	17.2	-36.7	-25.6	8.8	-24.3

New Zealand Property		%	%	%	%
S&P/NZX All Real Estate (inc imp credits)	2058.4	6.7	2.0	5.4	3.5
S&P/NZX All Real Estate (exc imp credits)	1947.6	6.5	1.8	5.1	2.9

Ten Year Bonds	%	Yield Changes			
USA	1.52	0.09	0.00	0.07	0.59
Japan	0.07	0.00	0.00	0.01	0.05
United Kingdom	0.97	0.18	0.02	0.25	0.77
Australia	1.67	-0.03	0.18	0.14	0.70
New Zealand	2.39	-0.09	0.39	0.63	1.40

90-Day Interest Rates	%	Yield Changes			
USA	0.06	0.01	0.02	0.01	-0.03
Japan	0.07	0.01	0.01	0.01	-0.01
United Kingdom	0.26	0.17	0.18	0.18	0.24
Australia	0.08	0.04	0.06	0.05	0.07
New Zealand	0.97	0.16	0.32	0.62	0.70

Bond Indices	Closing Values	Changes over: 1 Mth %	3 Mths %	6 Mths %	12 Mths %
S&P/NZX Bank Bills 90-Day	737.06	0.06	0.15	0.24	0.39
S&P/NZX NZ Government Bond Index	1814	0.55	-1.84	-3.05	-6.17
Barclays Capital Global Aggregate Index (Hedged NZD)	N/A	-0.37	0.19	0.28	-1.23

Hedge Funds & Commodities		%	%	%	%
HFRX Global Hedge Fund Index (USD)	1431	0.5	0.1	-0.1	3.7
DJ-UBS Commodity Index Total Return	212	3.5	-1.6	4.9	27.1
Gold (US$/ounce)	1827.50	3.0	4.1	3.2	-3.5
Oil (US$/barrel)	77.24	9.0	-0.7	0.4	50.8

Currencies		%	%	%	%
NZD / USD	0.6847	0.9	-0.8	-2.0	-4.9
NZD / EUR	0.6020	-0.2	1.1	2.2	2.3
NZD / GBP	0.5055	-1.5	-1.2	-0.1	-4.0
NZD / AUD	0.9417	-1.6	-1.4	1.2	0.9
NZD / YEN	78.84	2.3	2.4	1.7	6.1
Trade Weighted Index	73.19	-0.2	-0.7	-0.7	-1.4

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

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