Market and Portfolio Update
February 2022

What the Russian invasion means for investors

After months of rising tensions and repeated warnings, Russia's decision to invade Ukraine last week was shocking and saddening for humanity. These developments are understandably dominating international news headlines, and have caused some volatility in financial markets. This short-term volatility can be unnerving for investors, but what does the Russian invasion mean for investors looking forward?

It is important to remember that, barring further escalation, the economic impact of the invasion should be largely isolated to Russia and Ukraine. Both economies have been significantly disrupted, but the impact on the global economy has been relatively small. In addition, the sanctions levelled against Russia so far have been very targeted, and designed to limit the impact on the rest of the world.

We can also look at history for examples of how these kinds of events impact financial markets. Typically, geopolitical shocks tend to create volatility for markets in the short-term before reverting to follow the course of the global economy. For example, when Russia invaded Georgia in 2008, global stock markets experienced initial volatility but ended the month flat. Similarly, stock markets experienced some initial volatility during Russia's annexation of Crimea in March 2014, before bouncing back to end the month in the positive. So far, we have seen a similar dynamic play out with the Ukraine invasion. Initially, we've seen global share markets experience some volatility but we expect the state of the global economy to drive markets looking further out.

Managing risks in Booster funds

In an uncertain world, a combination of strategic planning and good risk management is essential for building a robust investment portfolio. Risk management often goes unnoticed in your portfolio when markets are steadily going up, but the benefits come to the fore during periods of heightened uncertainty like we have seen recently. Listed below are examples of how we help manage some of the risks in our portfolios:

- Booster's multi-sector funds are widely diversified around the world, providing some protection against country-specific shocks. As a result, our portfolios have only very minimal exposure to Russian investments (only about 0.2% of a balanced fund).
- As a small, open economy, the NZ Dollar tends to fall when markets are 'stressed'. This increases the value of overseas investments when they are converted back to NZ Dollars. To capture this risk management benefit, we have strategically left 50% of portfolios' global share investments 'unhedged' and free to move with foreign exchange rates.
- The fixed interest investments in our funds help buffer returns. Not only are their returns more stable, but higher investor demand for fixed interest investments like bonds typically means they rise in value when shares are weaker.
- We put some of our core funds' investments into direct holdings in NZ land and businesses, diversifying away from listed share markets. These investments are less affected by short-term market wobbles.

Investing is a long game

The conflict in Ukraine is a rapidly developing situation, and there could be increased volatility in financial markets for a while yet. It is a timely reminder of the importance of good risk management in your portfolio, but it is not an event that suggests you should change your long-term plan. The best thing you can do is to sit tight and ride it out. Investing is a long game, which is why sticking to a well-chosen plan that suits your financial goals is the best action to take.

Market Update

- Global share markets fell modestly in February (3%), with uncertainty regarding Ukraine tensions weighing on the market in the lead up to the invasion. While New Zealand and Australian share markets posted positive returns, being further from the conflict and experiencing the latest financial reporting season. Overall, the financial results have been positive, contributing to the 0.7% and 2% returns for the New Zealand and Australian sharemarkets.
- The conflict has put upward pressure on oil prices, with the international benchmark Brent Crude rising above USD 100 for the first time since 2014. Russia is a major oil exporter, supplying around 25% of Europe's oil. Oil and gas have not been included in sanctions to date, and it is still in the interests of Russia's economy to continue exporting to Europe. However, as we know, this situation is dynamic, and oil prices could rise further if caught up in the conflict.
- In New Zealand, the Reserve Bank hiked the Official Cash Rate 0.25% as expected – taking the rate to 1%. The Reserve Bank's updated forecasts now show the OCR reaching 2.6% by the middle of next year. However, this is subject to how the Ukraine invasion develops.