

New Zealand Equity Monthly January 2025

New Zealand market pauses and disruption risk comes to fore globally

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New Zealand market edges down in January after a strong second half of 2024

A look back at the past year shows that 2024 was very much a story of the second half of the year for New Zealand's equity market. Following the dovish turn taken by the Reserve Bank of New Zealand in the summer, the S&P/NZX 50 Index of New Zealand's largest companies by market capitalisation returned 12.2% for the year, the entirety of which was generated in the second half of 2024. After posting such a large return in a short amount of time, the market naturally paused for breath after the start of 2025 and the S&P/NZX 50 Index edged downward in January. Some of the decline reflected a dent in enthusiasm for consumer-facing and cyclical stocks after some weak trading updates. The global market jitters following recent news about Chinese AI technology also appeared to have an impact.

Reactions to disruption risk highlighted by jitters following Chinese AI news

Although it is a global story rather than a New Zealand one, the negative reaction to the recent announcement on Chinese AI capabilities highlights the impact disruption risk can have on equity markets in general. Disruption risk from an investor's point of view is believed to occur when a potential change to the status quo leads to the significant and rapid disruption of value or, in contrast, the creation of value. As the equity market is forward looking, market participants try to price in future disruption risk, and that is reflected in share prices. However, history shows us that the market struggles to do so effectively and consistently. In our view, the AI-related sell-off that followed the recent announcement from China provides an example of the market excessively pricing in disruption risk. This seems especially likely in view of China's history of focusing on the replication of technology rather than its invention. It should also be noted that any AI-related disruption is likely to be relatively small in New Zealand. This is due to the fact that the majority of significant advancements in the field take place in the US.

Markets may be under-reacting to risk from Trump tariffs

On the other side of the coin, we see the muted response to the widely reported tariffs proposed by US President Donald Trump as an example of the markets under-reacting to disruption risk. President Trump recently announced plans to impose 25% tariffs on Canada and Mexico. He has also proposed a 10% universal tariff, which would presumably apply to New Zealand. We believe that this could be of great significance to a wide range of companies, for example firms that generate a large amount of their sales revenue in the US. However, global share prices have not shown a marked reaction to the tariff news and have actually been testing all-time highs. In our view, the tariffs could create a difficult situation for affected companies, at least in the near term.

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