

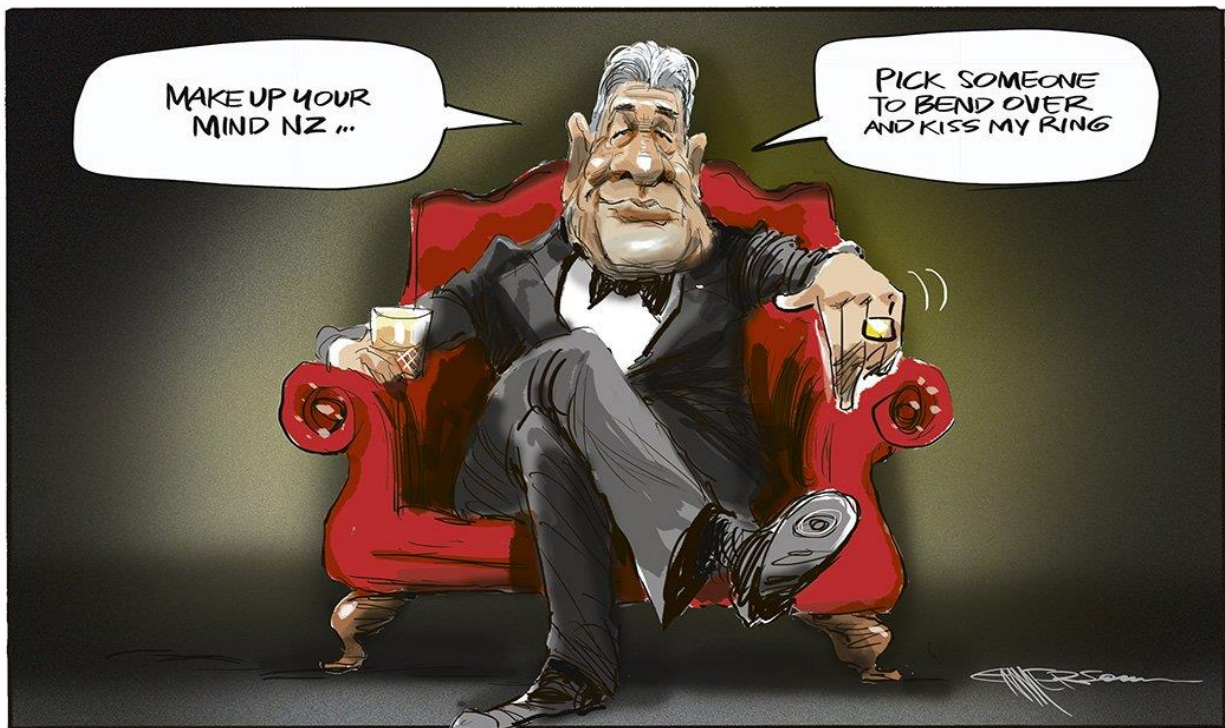
## Steve's Soap Box



The following is yet another contentious piece of opinion Steve has written for the newsletter. As we have warned previously, these pieces are on current issues affecting New Zealand and will be hard hitting and sometimes controversial. Steve is not known for his diplomacy and political correctness, and we have given him an opportunity to say it as he sees it. The opinions stated in these pieces will be his own and not necessarily those of the company or other staff members. We hope you enjoy them as much as Steve enjoys writing them.

## What does the Election mean for Local Markets?

As the provisional election results came rolling across our screens on Saturday night it quickly became apparent that a clear and decisive outcome was unlikely. This wasn't unexpected but the reality of the process under Mixed Member Proportional (MMP) voting is that we now enter a period of uncertainty and this is a backdrop that financial markets rarely appreciate. As we stand today National has 58 parliamentary seats, Labour has 45 while New Zealand First, the Greens and Act have 9, 7 and 1 seats respectively. The problem is that to govern, a party or coalition of parties, requires a total of at least 61 seats and consequently Winston Peters now appears to hold the balance of power. He has indicated he will make a decision by October 12. Negotiations however may well be slow as Winston's objectives are not particularly clear.



Winston has a large number of publicly stated "bottom lines" for a coalition arrangement but it is hard to know what is really important to him. He may even choose not to become part of a coalition and remain on the cross-benches, only supporting the Government on matters of confidence and supply. This would be the worst of all outcomes as it would be highly unstable. You will hear the term "horse-trading" used a lot over the next few weeks describing the intense negotiations that the major parties will be engaged in to swing Winston's vote either way.

There will be concessions made on both sides and the final result and what it means for local equity and currency markets is uncertain. Peters has had a turbulent career and this is the third time that he has held the balance of

power. He was sacked as a Cabinet Minister by National Party Prime Minister Jim Bolger in 1991, but held the balance of power as NZ First Leader in 1996. He entered in coalition with National but it didn't last in spite of Peters being given a newly created position of Treasurer and also Deputy Leader. In 2005 he entered into coalition with Labour as Minister of Foreign Affairs but stood down in 2008 as a Minister during a police investigation into the funding of NZ First. In 2008 he and NZ First were tossed out of Parliament after failing to win a seat or reach the 5% threshold but he returned to Parliament in 2011 with 6.8% of the vote, and again in 2014 with 8.6%, although he was in opposition both times.



We have attempted to analyse Peter's publicly stated bottom lines (there's about 15 of them!) but it is very hard to know which ones he's truly committed to as part of a potential coalition deal. There's also a chance that at 72 this may be Peter's last term in Parliament and this may affect his choice of coalition partner. This all adds to the uncertainty of the process.



We all have regularly heard favourable comment on the relatively stable political platform that New Zealand has enjoyed. Compared to Australia for example who have endured 5 different prime ministers over 5-years, New Zealand has been heralded as something of a benchmark. Although the likely outcome is a market-friendly National led government for the next 3-years, the possibility exists that we could end up with a Labour, Greens, NZ First coalition which would bring with it a perception, from many offshore investors, of increased political instability and a potential shift to the left in policy.

Although it is hard to accurately quantify, over the past month, financial markets have reacted to polls, with any evidence of Labour progress being reflected in concern from offshore investors. With just over 50% of the New Zealand share market being owned by these offshore investors, how they feel is more important today than it ever has been.

Given the strong performance of the New Zealand equity market over the past 5-years, which is up over 105% in that time, and the expensive valuations that characterise many of the local stocks, we at Rede believe a conservative approach is needed in the short term. The current political uncertainty in New Zealand is the type of event that could catalyse such a lift in volatility but we are confident going into the next 3-weeks of deliberations with Winston, that your portfolio is sufficiently diversified to manage short term risks.