

## Saying Haere Rā to Alert Levels

**Market sentiment swung back to positive overnight**, as markets continue to get whipped around by news on the Omicron variant. This promises to continue as we await data on its severity and transmissibility. Overnight, investors were buoyed by soothing comments from the WHO's chief scientist who said "...we think vaccines will still protect against severe disease as they have against the other variants".

**European share markets bounced strongly (Eurostoxx +2.86%), but the recovery looks a little unconvincing** in places and, in the US, it generally lost steam as the night wore on. The S&P500 is currently up around 0.8%, having been up 1.9% at one stage. Commodity prices have posted light gains, while bond yields are flattish and largely unmoved on another testimony from Fed chair Powell. Powell now appears to be on board with a speeding up the tapering process, and this is now baked into market pricing.

**US economic data released overnight didn't throw up any major surprises.** The closely-watched ISM manufacturing survey broadly matched analyst expectations for a small increase in November from levels already up around 17-year highs (61.1, from 60.8). The prices paid sub-component remained at stratospheric levels, like just about every US inflation indicator at the moment (82.4 vs. expectations of 85.5). Meanwhile, the 534k lift in November ADP employment was close to expectations and thus will solidify market expectations for a similar sized gain in Friday's Non-farm Payrolls.

**An update on our views: We updated our call on NZ house price inflation yesterday** (see [full note](#)). The prospect of three macro negatives showing up around the same time compelled us to attach a health warning to the 2022 house price inflation outlook, and we now expect small falls in house prices over the second half of 2022. The cumulative forecast fall, of around 4%, should be interpreted more as a hat-tip to the risk profile than a precise point forecast. But we suspect momentum will start to sputter quite quickly from here.

**Meanwhile our friends at CBA changed their call on the US interest rate cycle.** FOMC chair Powell's admission that inflation is not, in fact, all transitory means CBA now expect a faster tapering of asset purchases. In turn, this allows an earlier (June 2022) start to hikes in the Fed Funds rate, which is now expected to be lifted to a higher peak of 2.5%. All else being equal, this would reduce the NZ dollar's interest rate differential to the US and hence should be read as a (further) erosion of fundamental support for the kiwi.

**The decline in Q3 Aussie GDP reported yesterday didn't turn out to be as bad as local analysts feared** (-1.9% qoq vs. -2.7% expected, 3.9% yoy), in what's become a familiar post-COVID refrain. CBA scribe Gareth Aird nevertheless points out that the lockdown-driven decline was still the third worst on record. Financial markets barely blinked as they remain focused on more timely information. On this score, CBA's expectation is that a very strong economic expansion next year will be accompanied by an acceleration in inflation and wages growth, and a higher RBA cash rate from November 2022.

**FX Update:** It's been a mixed night in FX markets, with the recovery in risk sentiment not delivering the usual FX reaction of higher commodity currencies and lower safe-havens. Indeed, the JPY has outperformed overnight, with the NZD in second place. The NZD/USD lifted to a high of around 0.6860 overnight but has since declined back to 0.6830 in line with the paring of equity market gains.

**Day Ahead:** We're expecting a 2.5% qoq lift in the Q3 terms of trade in figures released this morning. This would amount to a new all-time high and provide another rousing confirmation of the strong position of our export sector. It's unlikely to be market moving though, and the same can be said of some second-tier data out of Australia (trade balance and housing lending). All eyes remain on news on US monetary policy and the Omicron variant for direction. Of course, tonight at midnight, we bid farewell to NZ's Alert Level system, with the country moving to the 'traffic light' COVID management system.

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Currencies			Commodities			Equities					
NZD/USD	0.6825	0.1%	NZD/SEK	6.1861	0.5%	CRB Index	219.187	-2.9%	Dow	34572	0.3%
NZD/AUD	0.9584	0.1%	NZD/NOK	6.2083	0.6%	NZX WMP	4225	0.0%	S&P 500	4592	0.6%
NZD/EUR	0.6026	0.1%	NZD/THB	23.00	0.0%	Gold \$/o	1781.6	0.4%	NASDAQ	15552	0.1%
NZD/JPY	76.98	-0.2%	AUD/USD	0.7121	0.1%	WTI Oil \$/b	66.3	0.2%	FTSE	7169	1.5%
NZD/GBP	0.5136	0.0%	EUR/USD	1.1325	0.1%	NZD Swap Rates (%)			DAX	15473	2.5%
NZD/CAD	0.8742	0.3%	USD/JPY	112.79	-0.3%	OCR	0.75	0.00	CAC-40	6882	2.4%
NZD/CHF	0.6273	0.1%	10 Yr Bond Yields (%)			3mth	0.80	-0.01	H.Seng	23659	0.8%
NZD/HKD	5.3177	0.0%	NZ	2.46	-0.03	1yr	1.59	0.04	Nikkei	27936	0.4%
NZD/SGD	0.9312	0.0%	US	1.44	-0.01	2yr	2.20	0.06	ASX200	7236	-0.3%
NZD/DKK	4.4816	0.0%	Aust	1.74	0.04	5yr	2.62	0.03	NZX50	12724	0.0%



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