

US inflation hits 5.4%, markets hold their nerve

A stonker of a US inflation print dominated market sentiment overnight. June CPI figures eclipsed expectations for the third month running, and by a large margin. Headline inflation rose to 5.4% (4.9% expected) with the core (ex-food & energy) measure at 4.5% (4.0% expected). A large part of the surprise was due to a whopping 10.5% mom jump in used car prices, which is expected to be transitory. But there were still signs of US inflation pressures broadening out, putting pressure on the Federal Reserve to get cracking on policy normalisation.

In response, US fixed interest markets brought forward the expected timing of the first lift in the Fed Funds rates to late 2022 and US bond yields lifted. The 10-year treasury yield is up around 5bps to 1.41%, helped by a weak auction of 30-year bonds. Stock market sentiment has soured on signs earlier rate hikes might be necessary. Having started the session in the black, the S&P500 has reversed course and is off around 0.3%. European stock indices closed mostly flat.

Australian business confidence and conditions pulled back in June reflecting the early part of lockdowns in New South Wales (NSW) and in other states. NSW accounts for over 30% of the Australian economy. NSW COVID cases were down yesterday and, encouragingly, the NSW and the Federal Government also announced an economic support package worth A\$500m a week (0.02% of GDP). It features increases in the emergency payments for businesses that can demonstrate a loss of revenue of 30% and maintain current staffing levels.

Also out yesterday, China's June trade data topped expectations, easing concerns over a sharp Chinese slowdown. The trade surplus widened in June to the highest since January 2021 with exports and imports up by 32.2% yoy and 36.7% yoy, respectively. Moreover, the PBoC's 50bps cut to the reserve requirement ratio suggests the deceleration in China credit growth will ultimately stabilise in favour of domestic demand activity.

Yesterday's REINZ housing figures showed that, if anything, the property market tightened up in June (full report [here](#)). This of course runs counter to widespread expectations (including our own) of a decent slowdown in the rate of house price growth over the coming months. House sales lifted 5.7% on the prior month (s.a), tightening the sales/listing ratio, and houses also sold at a marginally faster pace relative to May. Annual house price inflation held at 30% y/y. The next big hurdle for the market is the turning of the mortgage rate cycle.

FX Comment: USD strength was the order of the day thanks to the chart-topping US inflation figures. All of the major FX pairs felt it, with the NZD/USD back down to around 0.6940 after it poked above 0.7000 yesterday. The 0.6920-0.7030 range remains in-tact with today's RBNZ meeting the next big hurdle.

Day ahead: Big day, with the RBNZ meeting at 2pm. Our full preview is [here](#). Market pricing and the economist consensus are firmly centred on a November 2021 start to the OCR hiking cycle. So we'll need to see some firm hints that the RBNZ's thinking has shifted the same way for current levels of the NZD and wholesale interest rates to be sustained. That will likely include a dropping of the "considerable time and patience" line from the prior statement and, possibly, guidance on when the LSAP (quantitative easing) programme will be wound up.

An upside scenario for the NZD & rates would be the RBNZ providing a strong signal that a higher OCR is imminent, with markets likely to then firm up an August MPS hike. The most obvious downside scenario is for the Bank to hold the line ah-la RBA and retain the "considerable time and patience" line. Rate hike pricing would then likely shift back to 2022.

Tonight, Fed chair Powell delivers his semi-annual testimony to Congress and the Bank of Canada is expected to announce a further tapering of its bond purchases.

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Currencies			Currencies			Commodities			Equities		
NZD/USD	0.6944	-0.6%	NZD/SEK	6.0101	0.3%	CRB Index	214.1	0.7%	Dow	34889	-0.3%
NZD/AUD	0.9327	-0.1%	NZD/NOK	6.0951	0.4%	NZX WMP	3730	-0.4%	S&P 500	4369	-0.4%
NZD/EUR	0.5896	0.1%	NZD/THB	22.68	-0.6%	Gold \$/o	1808	0.1%	NASDAQ	14678	-0.4%
NZD/JPY	76.82	-0.3%	AUD/USD	0.7445	-0.5%	WTI Oil \$/b	75.3	1.6%	FTSE	7125	0.0%
NZD/GBP	0.5027	-0.1%	EUR/USD	1.1778	-0.7%	NZD Swap Rates (%)			DAX	15790	0.0%
NZD/CAD	0.8692	-0.1%	USD/JPY	110.62	0.3%	OCR	0.25	0.00	CAC-40	6558	0.0%
NZD/CHF	0.6379	-0.2%	10 Yr Bond Yields (%)			3mth	0.33	0.01	H.Seng	27963	1.6%
NZD/HKD	5.3930	-0.6%	NZ	1.68	0.02	1yr	0.59	0.02	Nikkei	28718	0.5%
NZD/SGD	0.9414	-0.3%	US	1.41	0.04	2yr	NA	NA	ASX200	7332	0.0%
NZD/DKK	4.3852	0.1%	Aust	1.33	0.01	5yr	Na	NA	NZX50	12785	0.2%

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