

NZ yields jump as inflation soars

Yesterday saw a 2.2% Q3 jump in CPI prices and decade-high 4.9% annual inflation print, well above market, ASB and RBNZ expectations. Sources of price increases were widespread and reflective of a combination of transitory and more persistent influences. Our [view](#) is that annual CPI inflation is well on track to crack 5% at the end of this year, with the clear risk that high inflation outcomes persist well into 2022 (and likely beyond that). **Yesterday afternoon's jump in the RBNZ sectoral core inflation measure to 2.7%, its highest level since 2009, has reinforced the risk that the RBNZ is well behind the curve and may have to play catch-up with speedier rate hikes further down the track.**

While the currency market reaction to the NZ CPI print was fleeting, yesterday has seen a large pick-up in NZ yields and upward revisions for OCR rate hike pricing. NZ swap yields were up 15-35bps across the curve, with similarly-sized jumps for NZ bond yields. Swap yield increases were the largest in the fixed mortgage belt, with circa 27-35bp rises in the 1- to 5-year swap rates and a close to 60bp increase in the 2-year swap rate (at 2.00% a 3-year high) since the start of this month. If these increases stick, and we expect they mostly will despite a worryingly high number of COVID-19 cases reported yesterday, further rises in mortgage interest [rates](#) we earlier warned about will be sooner and more sizeable.

There are other central banks with similar concerns to the RBNZ, with UK yields and market pricing firming after Bank of England Governor Bailey warned they will "have to act" (i.e. rate hikes) if the tick-up in consumer prices becomes more enduring. Market pricing has 40bps of BoE rate hikes by the end of the year, a 20bp gain over the last week, with 100bps of hikes by August 2022.

The grind higher in global yields continued overnight, albeit at a less frenetic pace, given the lack of catalysts. Weaker than expected September US industrial production data (-1.3% mom) and the strengthening NAHB housing index (80) data featured in a quiet session. There was a 1bp gain in US10-year Treasury yield (1.58%), with a curve flattening bias. Movements in global yields were modest, with the outsized gain in NZ the major outlier.

Global equities were a mixed bag. Bolstered by encouraging corporate earnings, US stocks saw modest gains overnight, with European luxury goods shares under downward pressure after Chinese authorities reportedly signalled plans for property tax legislation. Despite the jump in NZ yields, the NZSX50 was little changed.

Energy prices have hovered at elevated levels with near-term contract prices for Brent and WTI above USD82 per barrel after OPEC+ failed to meet (higher) production targets and Russia reportedly opted against sending more natural gas to Europe. That's not good for assuaging inflation concerns.

A confluence of factors – including the delta outbreak and associated restrictions, regulatory changes, and power rationing/outages – **were behind the slowdown in Q3 Chinese GDP growth, which slowed to its lowest pace for 2021** (+0.2% qoq, 4.9% yoy). Cooling industrial production growth (3.1% yoy) contrasted with rising retail sales (to 4.4% yoy). Our CBA colleagues note uncertainties remain, but they expect Chinese growth to rebound in Q4 as policymakers address growth challenges.

FX comment: Higher NZ yields have propelled the NZD to the top of the G10 currency leader board, albeit with some volatility, with spikes in the NZD following the CPI release and higher RBNZ core inflation figures partly unwound, before the NZD roared back into life over the last few hours. The NZD has traded in a 0.7050 to 0.7110 USD range over the past 24 hours and has firmed to 95.5 Australian cents at present. The large positive NZ yield differential and the solid export commodity price backdrop (we are looking for increases from the GDT auction tonight) remain key NZD supports.

Day ahead: Noting locally today apart from the 1pm COVID-19 numbers ahead of tonight's Global Dairy Trade event (1-2% gains to WMP on the cards). In Australia the RBA Board meeting minutes are due at 1.30pm (nothing new expected). Eurozone construction output, US housing starts and building permits highlight a quiet night for global data. The odd central bank comment speech is likely to pepper the wires. **Author:** mark.smith4@asb.co.nz

Currencies			Currencies			Commodities			Equities		
NZD/USD	0.7088	0.3%	NZD/SEK	6.142	0.9%	NZX WMP	3885.0	0.5%	Dow	35227	-0.2%
NZD/AUD	0.9553	0.3%	NZD/DKK	4.542	0.2%	Gold \$/o	1765.8	-0.1%	S&P 500	4480	0.2%
NZD/EUR	0.6104	0.2%	NZD/THB	23.7	0.3%	WTI Oil \$/b	82.1	-0.2%	NASDAQ	15009	0.8%
NZD/JPY	80.95	0.5%	AUD/USD	0.7419	0.0%	Money Market (%)			FTSE	7204	-0.4%
NZD/GBP	0.5161	0.5%	EUR/USD	1.161	0.2%	90 Day BB	0.77	0.07	CAC-40	6673	-0.8%
NZD/CAD	0.8774	-0.3%	USD/JPY	114.2	0.0%	OCR	0.50	0.00	DAX	15474	-0.7%
NZD/CHF	0.6542	0.2%	10 Yr Bond Yields (%)			ASB Swap Rates (%)			H.Seng	25410	0.3%
NZD/HKD	5.513	0.4%	NZ	2.41	0.16	1yr	1.52	0.29	Nikkei	29025	-0.1%
NZD/SGD	0.9562	0.4%	US	1.58	0.01	2yr	2.00	0.35	ASX200	7381	0.3%
NZD/CNH	4.556	0.2%	Aust	1.75	0.09	5yr	2.32	0.27	NZX50	12999	0.0%

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