USD and US Treasury yields fall on dovish Powell comments

As was widely expected the US Federal Open Market Committee held the Federal funds rate at 0-0.25% and maintained its USD120bm in monthly asset purchases. The tone of the policy assessment was a touch hawkish, but comments from FOMC Chair Powell were at the dovish end of the spectrum. The policy assessment alluded to the recent 'progress' in meeting the Fed's objectives and dropped the decision to taper QE unless "substantial further progress" in meeting its inflation and employment objectives. This suggests the Fed is on the path towards at least considering the removal of extraordinary policy support, although it appears to be in no hurry to adjust settings given uncertainties and risks, with the course of COVID-19 still deemed to be the key swing variable in the US economy.

At the Press Conference FOMC Chair Powell struck a more cautionary note, with inflation expected to slow in the coming months, with the Fed a way away from seeing substantial progress in lifting employment. This suggests Powell still views rate rises in the US appear to be a long way off, and with some question marks over whether the FOMC will soon start to taper QE. The September FOMC meeting, the tone of data and other events will be crucial in the coming months.

This triggered a seesaw reaction in markets. Treasury yields initially ticked up but are currently 1-2bps below pre-announcement levels (10Y 1.23%). Equity markets were cheered by the signal that interest rate rises still were a long way off and firmed post-FOMC. The USD index initially lifted but is now below pre-announcement levels.

Leading up to the FOMC decision, equity markets were generally on the up. US equities had earlier been boosted by stronger-than-expected earnings reports for Apple and Microsoft. Strong corporate earnings results boosted European stocks, with tech shares amongst the biggest gainers, with airline stocks supported after the UK government allowed travel to the UK for fully vaccinated travellers from the US and European Union without needing to quarantine. Equities were lower in Asia-Pacific markets given concerns over regulatory crackdowns by Chinese authorities and COVID-19 worries.

US Treasury yields were largely becalmed leading to the Fed decision, with mixed moves in European government bond yields. NZ swap yields took their cues from earlier falls in global yields, with a curve flattening bias, with 10-year bond yields down 3bps to 1.63%. Australian yields were also lower and flatter along the curve, with 10-year government bond yields (1.15%) falling 6bps to late-January lows. **Lower US stockpiles provided a modest lift to oil prices.**

In contrast to the surprisingly strong Q2 NZ CPI release, markets took the in-line-with-consensus Australian Q2 CPI print (+0.8% qoq, 3.8% yoy) in their stride, with minimal market reaction. Sub 2% annual core CPI inflation measures were also in line with expectations. With the COVID-19 outbreak adversely impacting the NSW economy, our CBA colleagues now expect a later start to RBA hikes (to May 2023 from November 2022).

FX Update: The USD index dipped after the Fed decision, with the USD the weakest performer of the G10 overnight, with the Swiss Franc, NOK, and CAD amongst the strongest performers in the G10. The NZD traded in a 0.6900 to 0.6970 USD range overnight and is currently towards the top of that range. The NZD is currently 94.4 Australian cents. A solid commodity price backdrop, resilient domestic demand and widening interest rate differentials in NZ's favour support to the NZD.

Day ahead: The full July reading of the ANZ NZ business outlook at 1pm should confirm resilient business sentiment at a time of elevated cost, inflationary and capacity pressures. The $500m NZ government bond tender by NZDM just after 2pm today will no longer have the RBNZ as an active purchaser, with high NZ bond issuance ($30bn was earmarked for the June 2022 year) expected to nudge NZ yields higher. Today there is a scattering of mostly 2nd tier data released offshore, but market attention is likely to fucus on the 1st Q2 reading of US GDP and US jobless claims. Annualised Q2 US GDP growth is expected to lift to 8.5% in Q2 (from 6.4% in Q1), with the 419k spike in initial jobless claims in mid-July expected to ease back to 385k. **Author**: mark.smith4@asb.co.nz

Currencies			Currencies			Commodities			Equities		
NZD/USD	0.6953	-0.1%	NZD/SEK	5.977	-0.5%	NZX WMP	3775.0	0.5%	Dow	34984	-0.2%
NZD/AUD	0.9433	-0.2%	NZD/DKK	4.366	-0.3%	Gold $/o	1808.3	0.5%	S&P 500	4411	0.2%
NZD/EUR	0.5870	-0.3%	NZD/THB	22.8	-0.4%	WTI Oil $/b	72.4	1.0%	NASDAQ	14785	0.9%
NZD/JPY	76.42	-0.2%	AUD/USD	0.7371	0.1%	**Money Market (%)**			FTSE	7017	0.3%
NZD/GBP	0.5001	-0.2%	EUR/USD	1.185	0.2%	90 Day BB	0.47	0.00	CAC-40	6609	1.2%
NZD/CAD	0.8715	-0.6%	USD/JPY	109.9	0.1%	OCR	0.25	0.00	DAX	15570	0.3%
NZD/CHF	0.6329	-0.5%	**10 Yr Bond Yields (%)**			**ASB Swap Rates (%)**			H.Seng	25474	1.5%
NZD/HKD	5.409	-0.2%	NZ	1.63	-0.02	1yr	0.81	0.00	Nikkei	27582	-1.4%
NZD/SGD	0.9436	-0.4%	US	1.23	-0.01	2yr	1.04	-0.01	ASX200	7379	-0.7%
NZD/CNH	4.512	-0.3%	Aust	1.16	-0.05	5yr	1.43	-0.01	NZX50	12595	0.0%

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