

Markets Monthly

18 June 2020

Volatility pays a visit to markets in Early June

By early June many sharemarket indices were getting close to a full recovery from the sharp falls that occurred in March. In the case of the tech-heavy NASDAQ index in the US, a fresh all-time high was set on 10 June.

Then on 11th June we got a reminder that's it's not a one-way street when it comes to sharemarket direction, and large dips were recorded in global markets, with major market indices down 4 to 6.5% in a single day. Markets have regained composure over subsequent sessions and recouped some of the dip.

Government bond yields here and abroad remain extremely low, as the RBNZ and the world's major central banks maintain ultra-loose policy settings.

The NZD firmed over May and was up 1% against the USD and on a trade-weighted basis during May.

Date		31-May-20	Month %	Quarter %	Year %	5-Year %	
Cash	NZ Official Cash Rate	0.25	0.00	-0.75	-1.25	-3.25	
	NZ 90-day bank bill	0.26	-0.01	-0.79	-1.41	-3.21	
Fixed	NZ 5-year gov't stock	0.35	0.03	-0.52	-1.04	-2.83	
Interest	NZ 10-year gov't	0.76	0.03	-0.30	-0.96	-2.87	
	NZ 10-year swap	0.73	-0.05	-0.46	-1.94	-3.16	
	AUS 10-year gov't	0.90	-0.02	0.04	-0.57	-1.84	
	US 10-year gov't	0.67	0.05	-0.59	-1.51	-1.46	
Australasian	NZ - NZX50 Capital (NZ\$)	4622	3.3%	-4.1%	4.4%	54.3%	
	- NZX50 Gross (NZ\$)	10882	3.3%	-3.4%	7.6%	86.8%	
Equities	AUS - All Ords (A\$)	5872	4.9%	-9.8%	-9.5%	1.7%	
International	JAP - Nikkei (¥)	21878	8.3%	3.5%	6.2%	6.4%	
	Equities	UK - FT100 (£)	6077	3.0%	-7.7%	-15.2%	-13.0%
		US - S&P500 (US\$)	3044	4.5%	3.0%	10.6%	44.5%
		WORLD - MSCI (US\$)	2148	4.6%	0.3%	5.0%	20.7%
		- MSCI return in NZD		3.6%	1.1%	10.1%	38.9%
Exchange	NZD/USD	0.6207	1.0%	-0.7%	-4.6%	-13.1%	
Rates	NZD/AUD	0.9334	-0.3%	-2.4%	-0.8%	0.2%	
	NZD/JPY	66.53	1.6%	-2.5%	-6.2%	-24.7%	
	NZD/GBP	0.5026	2.0%	3.5%	-2.6%	7.9%	
	NZD/EUR	0.5591	-1.1%	-1.7%	-4.4%	-14.3%	
		NZ TWI	69.80	1.0%	-0.3%	-2.8%	-6.8%

Equity indices are the respective end-of-month closes. Interest rates and exchanges rates are at 5pm NZ.

For the latest performance information on ASB's funds click [here for ASB KiwiSaver Scheme](#), click [here for ASB Investment Funds](#). More information on [ASB Securities is here](#).

Market News

By early June many sharemarket indices were getting close to a full recovery from the sharp falls that occurred in March. In the case of the tech-heavy NASDAQ index in the US, a fresh all-time high was set on 10 June. Several other indices (including New Zealand's) were only 4-7% off all-time highs. The MSCI world share index was 6% off its March peak on 10 June.

Then on 11th June we got a reminder that's it's not a one-way street when it comes to sharemarket direction, and large dips were recorded in the world's major markets, with market indices down 4 to 6.5%. Sharemarket indices recorded the biggest one-day falls since the COVID crisis took hold in mid-March.

The volatility wasn't just in sharemarkets; over the week ending 12th June Brent crude oil prices fell by 8.4%, recording the first weekly drop since April. FX market volatility also picked up, and the NZD declined around 2% from its recent peak vis-à-vis the USD.

It's difficult to pin-point an exact trigger for financial market moves like this. The news wires were generally attributing it to both the Federal Reserve's cautious assessment of the US economy following its June meeting, as well as fears about a possible second wave of COVID-19 infections globally. It could just as likely be an overdue pull-back given how far and how fast stock markets had risen over earlier weeks. Markets have regained composure over subsequent sessions and recouped some of the dip.

Meanwhile, government bond yields here and abroad remain extremely low, as the RBNZ and the world's major central banks maintain ultra-loose policy settings. With the conventionally targeted cash rate settings already slashed, the focus for central bank meetings over May and June has been on any tweaks to the unconventional policies. i.e. adjustments and expansion of asset purchase programmes. In this vein, the RBNZ expanded its bond purchase programme to \$60bn, from \$33bn in May, as expected.

Apart from the jolt of volatility around 11th June, the general theme in the FX world over recent months has been a softening of the USD as confidence in the global recovery lifts. That softer USD has helped NZD/USD to trade just shy of 0.6580 against the USD in June, although the cross is 1.4c below this level at the time of writing, trading near 0.6450.

Income Assets

Asset	Instrument	31-May-20 Yield (%)	Month	Quarter	Year	5-Year
			Yield Change			
Cash	NZ Official Cash Rate	0.25	0.00	-0.75	-1.25	-3.25
	NZ 90-day bank bill	0.26	-0.01	-0.79	-1.41	-3.21
	US 90-day bank bill	0.35	-0.34	-1.23	-2.17	0.07
Fixed	NZ 5-year gov't stock	0.35	0.03	-0.52	-1.04	-2.83
Interest	NZ 10-year gov't	0.76	0.03	-0.30	-0.96	-2.87
	NZ 10-year swap	0.73	-0.05	-0.46	-1.19	-3.16
	AUS 10-year gov't	0.90	-0.02	0.04	-0.57	-1.84
	US 10-year gov't	0.67	0.05	-0.59	-1.51	-1.46

Cash

In response to the escalation of COVID-19 in March, the RBNZ cut the Official Cash Rate (OCR) to 0.25% and announced an asset purchase programme of NZ \$30bn in NZ Government bonds. The RBNZ also committed to keep the OCR at 0.25% over the year ahead and have not ruled out moving it lower still. NZ yields are well below where they were in late March and we expect returns from NZ cash investments to remain extremely low. In April the RBNZ added \$3 billion of Local Government Funding Agency (LGFA) debt to its asset purchase programme, and in May the overall size of the programme was expanded to \$60bn.

Term deposit interest rates and mortgage rates have fallen over the past month. For amounts over \$10k, term deposit rates for 1-5 years are now between 1.80% and 1.9% (a decline of between 0.6% and 0.75% on where they were prior to the RBNZ's March cut). Rates for shorter 3-month terms are now around 1.15%, and 4- to 12-month rates are between 1.3% and 1.8% (down by 0.25%-0.90% on the levels of early March). **We continue to think the risk for savers is that term deposit rates remain low for an extended period (years) and could press even lower than today's levels over the year ahead.**

One issue we get asked about regularly is negative interest rates.

When we talk about negative interest rates, in New Zealand's case we are generally talking about the Reserve Bank of New Zealand setting a negative Official Cash Rate (OCR). If the OCR was

negative, financial institutions would be required to pay interest for depositing excess reserves with the RBNZ.

Importantly, ASB aren't forecasting a negative Official Cash Rate, and the Record of Meeting from the RBNZ Monetary Policy Committee in May reaffirmed earlier guidance that the OCR will remain at the current 0.25% setting until early-2021. However, the Committee noted that **a negative OCR could become an option in the future**, although at present, financial institutions are not yet operationally ready. In other words, a negative OCR is a possibility next year, but we think other actions the RBNZ can take are likely to be more effective and timelier in terms of supporting the economy. It's important to note that even if the RBNZ cuts the OCR further and sets a negative OCR, **we don't expect negative term deposit rates**. But we would expect term deposit rates to be even lower than they are today.

The latest ASB term deposit rates [can be found here](#).

NZ Fixed Interest

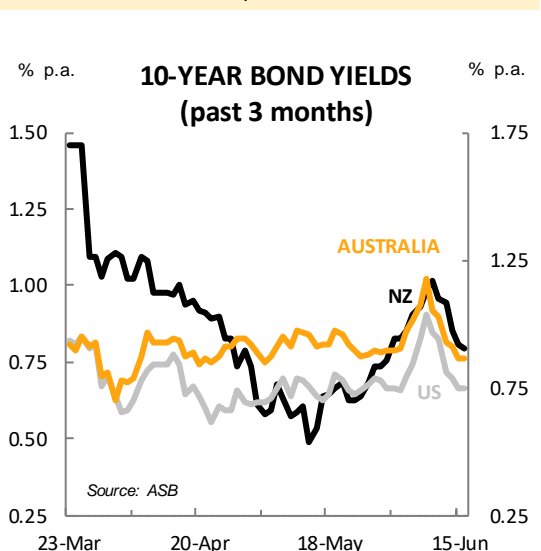
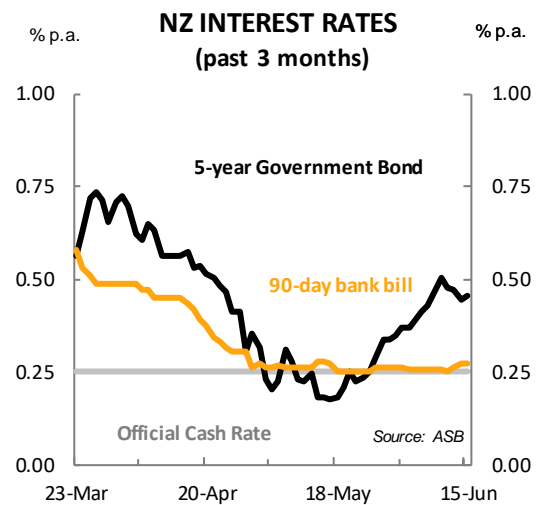
Government bond yields were extremely volatile in late March, with yields spiking higher on the stresses and strains plaguing financial markets globally. Central bank action restored some calm over the subsequent months, as discussed in last month's report. In New Zealand's case, the RBNZ's 0.75% OCR cut and the subsequent "Large Scale Asset Purchase Programme" has helped drive key fixed interest rates to record low levels.

Through all the volatility, 10-year government bond yields in New Zealand, Australia and the US have touched record lows during recent months. The New Zealand 10-year Government Bond yield closed at an all-time low of 0.49% on 13 May.

International Fixed Interest

Fears of a widespread economic slowdown due to the coronavirus had already driven global bond yields lower in January and February, then central bank action during March added to the downward pressure on yields.

Government bond yields are negative out to the 10-year tenor in some European economies and in Japan. US and UK 10-year Government Bond yields remain positive, albeit sub 1%, and not far off their respective record lows. We expect long-term yields to remain low, given very low inflation, the weak global economic outlook and the likelihood that the world's major central banks will maintain ultra-loose monetary policy settings for the foreseeable future.



Growth Assets

Asset	Index	31-May-20 Level	Change			
			Month %	Quarter %	Year %	5-Year %
Equities	NZ - NZX50 Capital (NZ\$)	4622	3.3%	-4.1%	4.4%	9.1%
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	AUS - All Ords (A\$)	5872	4.9%	-9.8%	-9.5%	0.3%
	All Ords in NZD	6291	5.2%	-7.6%	-8.8%	0.3%
	JAP - Nikkei (¥)	21878	8.3%	3.5%	6.2%	1.2%
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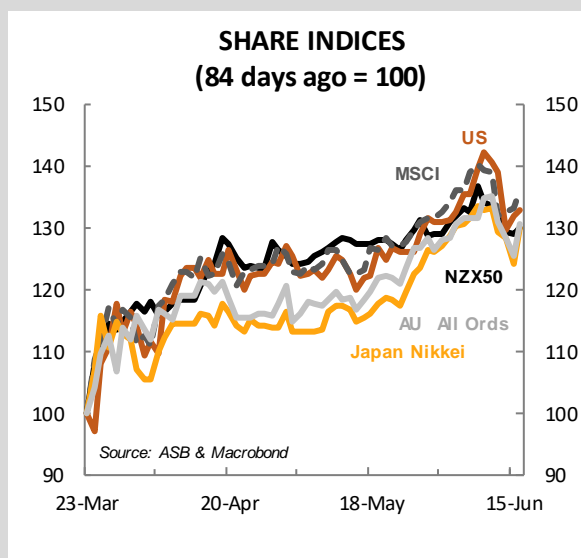
Australasian Equities

Australasian markets have lifted significantly off the late March lows, with the NZX50 Gross index up 3.3%, and the All Ords index up 4.9% over May, building on the gains recorded in April. Both market indices had set record highs during February before COVID-19 fears sent sharemarkets lower. The gains have carried on into June, although sharemarkets on both sides of the Tasman dipped in the wake of the big drops in the US and Europe on June 11th. However, the declines were modest (around 2%) compared with the larger declines elsewhere.

At the time of writing, the NZ sharemarket is trading around 6% below its February peak, while the Australian market is around 16% off its highs.

International Equities

Global sharemarkets have continued to recover from the lows reached on March 23. Over May the US Dow rose 4.3%; S&P 500 rose 4.5%; and the Nasdaq rose 6.8%. In Asia, Japan's Nikkei index rose 8.3%. In Europe, the UK's FTSE rose 3.0% and the German Dax index was up 6.7%. However, on 11th June we got a reminder that it's not a one-way street when it comes to sharemarket direction. Large dips were recorded in the world's major markets, with market indices down 4% to 6.5%. The drops were the biggest one-day falls since the COVID-19 crisis took hold in mid-March. Markets have regained composure over subsequent sessions and recouped some of the dip. At the time of writing the NASDAQ index of US Shares is only 1% off an all-time high it set on 10th June. The S&P 500 index of US shares is 8% off its all-time high set back in February. The MSCI World share index is down closer to 9% from its peak. There is still a way to go, but the recovery is impressive nonetheless, given many markets were down 30-35% in late March.



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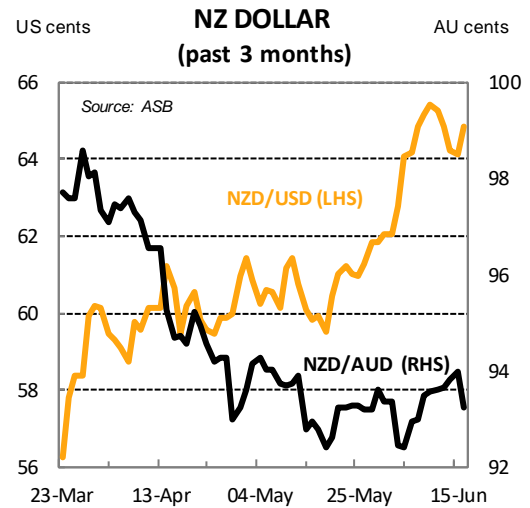
We expect that volatility will continue while the markets grapple with the uncertainties of the coronavirus impact. Investors have reacted positively to the policy support from central banks and governments over April and May, and the prospect of economies re-opening. Now investors face the prospect of several months of tough data that will reveal the economic impact of the lockdowns, as well as the developments of the pandemic itself. And if that's not enough, the US-China tensions could easily re-emerge as an issue, as we saw in early May.

ASB Securities has more information on sharemarkets and trading [here](#).

Exchange Rates:

From a low point near 0.5600 USD in March, the NZD has climbed nearly 10c to a peak just shy of 0.6600 USD in June. Growing discussion regarding negative interest rates in New Zealand pushed NZD to its recent low of 0.5921 on 15 May. But from that point until 9 June it was pretty much onwards and upwards for the NZD/USD.

Part of these gains were a function of increased confidence in the global recovery and associated with this was an easing USD. Confidence in the economic outlook pulled down the USD because it is a counter-cyclical currency. The AUD also benefited from improved confidence in the economic outlook. As well as lifting against the USD, the AUD has strengthened against the NZD in recent months. The NZD/AUD cross rate has eased from 0.9800 to as low as 0.9200 in early June. NZD/AUD is back around 0.9375 at the time of writing.



More information about currencies is available in ASB's weekly economic report which can be [downloaded here](#).

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