Markets Monthly

20 July 2021

Sharemarkets lift while bond yields ease

Long-term global bond yields were down over June, despite investors continuing to fret about rising inflation pressures. 10-year yields are also down over the full second quarter but remain significantly up on a year ago.

At its July meeting, the RBNZ held the OCR at 0.25% as expected, but signalled that the Large-Scale Asset Purchase (LSAP) programme will be halted by 23rd July 2021. This tool is "no longer necessary for monetary policy purposes". This is a frank admission that with market functioning now much, much better than in the depths of the COVID-19 gloom, a shift to more conventional policy tools is on the cards.

Halting the LSAP provides the RBNZ with more flexibility to bring OCR hikes forward, if needed. We have expected the RBNZ to cease weekly LSAP prior to hiking the OCR, so the door is open to act sooner than we have been forecasting in earlier reports. ASB expects the OCR to lift in August – i.e., next month! Our report on the July RBNZ meeting is here.

Meanwhile, the local sharemarket and most of the major global sharemarkets lifted over June. The NZD was weak during the month and dipped 2% on a trade-weighted basis.

Date		30-Jun-21	Month %	Quarter %	Year %	5-Year %
Cash	NZ Official Cash Rate	0.25	0.00	0.00	0.00	-2.00
	NZ 90-day bank bill	0.35	0.03	0.01	0.05	-2.06
Fixed	NZ 5-year gov't stock	1.13	0.06	0.16	0.70	-0.90
Interest	NZ 10-year gov't	1.77	-0.03	-0.04	0.84	-0.58
	AUS 10-year gov't	1.51	-0.13	-0.31	0.62	-0.51
	US 10-year gov't	1.48	-0.10	-0.26	0.85	-0.03
Australasian	NZ - NZX50 Capital (NZ$)	5242	2.4%	0.3%	8.0%	55.9%
	- NZX50 Gross (NZ$)	12655	2.7%	0.7%	10.5%	83.4%
Equities	AUS - All Ords (A$)	7585	2.4%	8.1%	26.4%	42.8%
International	JAP - Nikkei (¥)	28792	-0.2%	-1.3%	29.2%	84.8%
Equities	UK - FT100 (£)	7037	0.2%	4.8%	14.1%	8.2%
	US - S&P500 (US$)	4298	2.2%	8.2%	38.6%	104.8%
	WORLD - MSCI (US$)	3017	1.4%	7.3%	37.0%	82.5%
	- MSCI return in NZD		5.1%	7.0%	25.6%	84.5%
Exchange	NZD/USD	0.7004	-3.5%	0.3%	9.1%	-1.1%
Rates	NZD/AUD	0.9306	-0.9%	1.4%	-0.2%	-2.3%
	NZD/JPY	77.35	-2.8%	0.0%	11.9%	6.3%
	NZD/GBP	0.5054	-1.2%	-0.6%	-3.1%	-4.4%
	NZD/EUR	0.5882	-1.2%	-1.4%	3.0%	-7.8%
	NZ TWI	73.53	-2.0%	-0.1%	3.3%	-3.0%

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

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.

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Please refer to the important disclosures at the end of this document.

Income Assets

Cash

ASB's term deposit rates have lifted several times this year, including over the past month. The longest terms have lifted the most, with the 5-year rate now 1% above the all-time lows recorded over the past year. The shorter-term rates (less than six months) remain at or near their lows, as tabled below.

Term Deposit Rates	90-days	6 months	9 months	1 Year	2 years	3 years	4 years	5 years
10-year ave	2.68	3.32	3.37	3.43	3.64	3.81	3.98	4.12
Low	0.35	0.80	0.75	0.75	0.80	0.90	1.00	1.00
Jul-21	**0.35**	**1.00**	**0.90**	**1.20**	**1.40**	**1.70**	**1.85**	**2.00**

Over the past year term deposit rates have been at the lowest level on record going back to the 1960s. But we have turned a corner in 2021. There has been a lift off the lows for all but the shorter-term deposit interest rates over recent months, including the latest increases in July. Nonetheless, rates on offer are still very low and are expected to remain significantly below historical averages over the coming years. ASB's term deposit interest rates are tabled here.

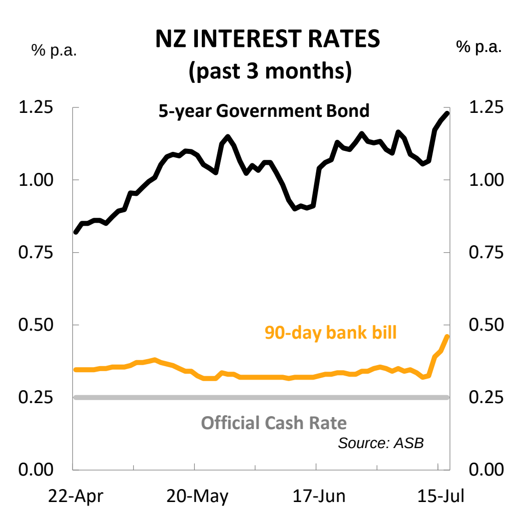
Inflation has been low but is on the rise and could well erode all the return from term deposits. Consumer price (CPI) inflation has generally been within the lower half of the Reserve Bank of New Zealand's 1-3% target range over the past five years. However, CPI inflation has lifted over 2021, and is expected to run at between 2-3% p.a. over the coming years. That's above all the current term deposit rates. Related to the inflation outlook, and the strong economic recovery in the wake of the COVID-19 pandemic, we expect the RBNZ to begin lifting the OCR very soon – next month in fact! Our report on the July RBNZ meeting is here. We also expect to see more increases in term deposit rates over the years ahead. You can read more in our Term Deposit report, and the ASB term deposit rates can be found here.

Asset	Instrument	30-Jun-21 Yield (%)	Month	Quarter	Year	5-Year
			Yield Change			
Cash	NZ Official Cash Rate	0.25	0.00	0.00	0.00	-2.00
	NZ 90-day bank bill	0.35	0.03	0.01	0.05	-2.06
	US 90-day bank bill	0.14	0.01	-0.06	-0.15	-0.50
Fixed Interest	NZ 5-year gov't stock	1.13	0.06	0.16	0.70	-0.90
	NZ 10-year gov't	1.77	-0.03	-0.04	0.84	-0.58
	NZ 10-year swap	1.88	-0.12	-0.09	1.15	-0.78
	AUS 10-year gov't	1.51	-0.13	-0.31	0.62	-0.51
	US 10-year gov't	1.48	-0.10	-0.26	0.85	-0.03

NZ Fixed Interest

NZ 10-year Government bond yields dipped modestly in June but remain significantly higher than US and Australian yields. The 5-year yield ended up 6 basis points over June, while 10-year yields were up down 3 basis points over the month. At the time of writing the NZ 5-year government bond yield is trading around 1.23%, the highest it has yielded since January 2020. Last September the 5-year yield was negative.

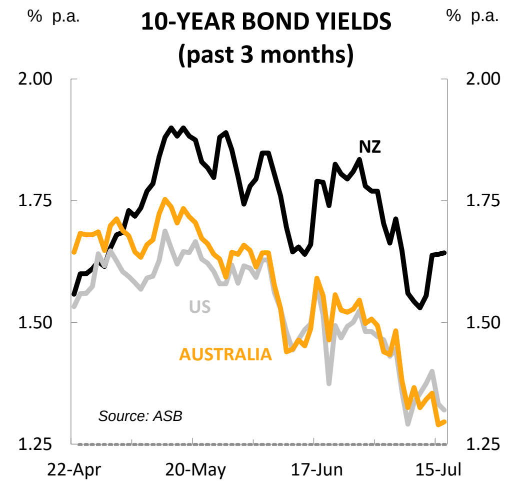
At its July meeting the RBNZ said that the Large-Scale Asset Purchase (LSAP) programme will be halted by 23rd July 2021, with this tool "no longer necessary for monetary policy purposes". This is a frank admission that with market functioning now much, much better than in the depths of the COVID-19 gloom, a shift to more conventional policy tools is on the cards.



The Monetary Policy Committee reiterated that the Official Cash Rate is the preferred tool when responding to economic conditions in the future. However, the RBNZ did not close to door to restarting asset purchases completely, noting that it remained an important tool for supporting New Zealand debt market efficiency "if required", and an important monetary policy tool "if needed". Moreover, the RBNZ did not signal when, if at all, it planned to sell its current LSAP holdings.

The signal to cease weekly asset purchases towards the end of this month will be coming at a time when the NZ Debt Management Office has stepped up NZ government bond issuance (currently $500-$550m weekly to hit their $30bn 2021/22 issuance target) and will pressure yields higher at the margin.

Halting the LSAP will also provide the RBNZ with more flexibility to bring OCR hikes forward, if needed. We had earlier expected the RBNZ to have ceased weekly bond purchases via the LSAP prior to hiking the OCR in November – the door is now open to lift the OCR earlier, as we think is likely.



International Fixed Interest

The US 10-year treasury yields pressed lower over June, declining by around 10 basis points over the month, after a similar dip in the preceding two months. The US 10-year yield is down 26 basis points over the quarter but remains 85 basis points on year-ago levels. Similarly, the Australian 10-year government bond yield dipped in June but is up 62 basis points on a year ago.

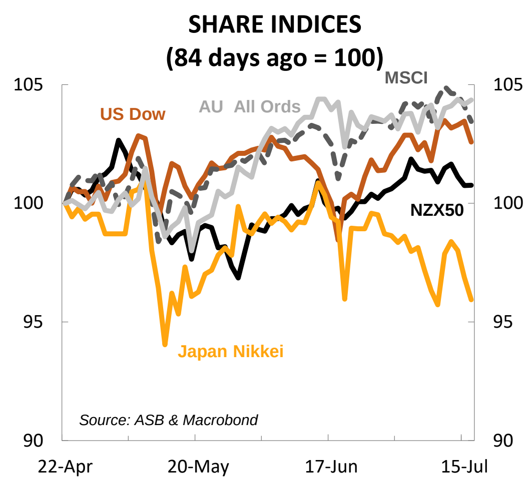
The Reserve Bank of Australia (RBA) left monetary policy unchanged at its June meeting and announced it will make a decision on its yield curve control and QE program at its meeting in July. In turn, at the highly anticipated July meeting, the cash rate was held steady at a record low 0.1%, but previous forward guidance (or pre-conditions) on the potential timing of the first rate hike was adjusted, *"The Bank's central scenario for the economy is that this condition will not be met before 2024. Meeting it will require the labour market to be tight enough to generate wages growth that is materially higher than it is currently."* Another policy decision handed down in July related to whether the Board would retain its 3-year government bond yield target – which links the April 2024 borrowing rate to the 0.1 per cent cash rate – or to roll over the target to the November 2024 maturity. By retaining the status quo, the Board has potentially laid the foundations for eventually retiring its yield curve control program. There has been a lot of interest in whether the RBA would renew its $100 billion bond buying or quantitative easing ('QE') program for a third time. In the end, the Board opted for a flexible approach, incrementally scaling down its bond purchases, enabling it to be data-dependent and responsive to central bank policy changes globally. The RBA will slow its bond-buying program from early September, reducing its weekly bond purchases from $5 billion to $4 billion until at least mid-November. The near term economic outlook in Australia has deteriorated sharply because roughly half of Australia's population and economy is locked down. The covid 19 outbreak, and associated disruption to the economy, suggests the RBA may delay tapering its asset purchases.

Growth Assets

Asset	Index	30-Jun-21 Level	Month %	Quarter %	Year %	5-Year %p.a.
				Change		
Equities	NZ - NZX50 Capital (NZ$)	5242	2.4%	0.3%	8.0%	9.3%
	- NZX50 Gross (NZ$)	12655	2.7%	0.7%	10.5%	12.9%
	AUS - All Ords (A$)	7585	2.4%	8.1%	26.4%	7.4%
	All Ords in NZD	8150	3.3%	6.6%	26.7%	7.9%
	JAP - Nikkei (¥)	28792	-0.2%	-1.3%	29.2%	13.1%
	UK - FT100 (£)	7037	0.2%	4.8%	14.1%	1.6%
	US - S&P500 (US$)	4298	2.2%	8.2%	38.6%	15.4%
	WORLD - MSCI (US$)	3017	1.4%	7.3%	37.0%	12.8%

Australasian Equities

The New Zealand sharemarket has been out of step with global markets over 2021 but played some catch up in June. The Aussie sharemarket rose for the nineth consecutive month and has set more record highs the past month. During June the NZX 50 capital index and the All Ords (in AUD terms) both rose 2.4%.



Covid-19 remains a significant theme for the local sharemarket. For example, Vista (up 13% in June) continues to benefit from the reopening of its customers' cinemas around the world. During June the company confirmed its cashflow continues to improve with most of its customers cinemas now open. ASX-listed ResMed appreciated significantly during the month, due to developments for respiratory device manufacturers including the recall of a competitor's product. Fisher & Paykel Healthcare shares were trading below $29 in early June but are back trading just shy of $31 at the time of writing. In contrast, the construction outlook in New Zealand looks strong, but Fletcher Building's share price has pulled back from its early June peak just shy of $8, to trade under $7.30 in mid-July. Nonetheless, that's a strong lift from a year ago when the share price was around $3.40. The a2 Milk Co's share price has lifted $2 off the May lows and is trading back near $7.40 per share. Although the lift has been significant, the share price is still languishing when compared to a year ago, when it was over $20.

Across the Tasman it's the end of the financial year, and the All Ordinaries index was up 26.4% over the year to June 30. That's the biggest rise for a financial year in 34 years. Consumer Discretionary shares rose by 42.6% over the year, ahead of Information Technology (+38.9%) and the Financials sector (+35.7%). At the other end of the scale, the Utilities sector fell by 22.9%.

At the time of writing the Australian market is trading circa 1% shy of the record high touched in mid-June, while the NZ market is still around 7% off its early January peak.

International Equities

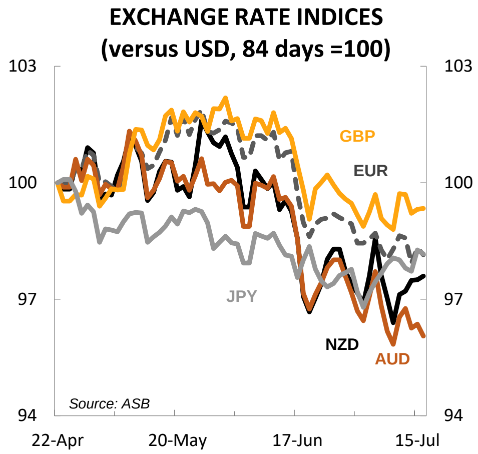
For yet another month, global equity markets pressed higher, bursting through all-time highs in much of the world. That theme saw the MSCI index of world shares lifting 1.4% in USD terms over June.

Sharemarket gains were particularly pronounced on Wall Street, as the American recovery picks up the pace and sentiment continued to lift. All-up, the benchmark S&P500 lifted 2.1% over the month. Among major developed markets, Japan was the exception to the trend of higher equities, with the Nikkei down 0.2%.

European shares also notched up gains over the month, with the UK FTSE, German Dax and pan-European Stoxx index all making gains. Each has since given up some of those gains in the aftermath of rising COVID cases and severe flooding.

ASB Securities has more information on sharemarkets and trading here.

Exchange Rates



USD strength was the big theme in markets over the course of June, with most other currencies – including the NZD – falling against the greenback over the course of the month. The upshot saw NZD/USD fall 3.5%, and it's continued to hover around or below the 0.70 mark for most of July. This USD strength has come even as global risk sentiment continued to improve over the month.

Typically, the USD is a 'countercyclical' currency, meaning it tends to fall in value when the economy is growing as investors shift away from 'safe' assets. But with the US economy diverging from much of the world (given the scale of its recovery), the USD has behaved like a 'normal' currency – lifting rather than falling on positive news and data.

NZD was mixed against other currencies over the month, falling 0.9% against the AUD to around 0.9306, and falling 1.2% to 0.5882 against the EUR. All up, NZD was down about 3.1% on a trade-weighted basis.

More information about currencies is available in ASB's weekly economic report which can be downloaded here.

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