Markets Monthly

06 April 2021

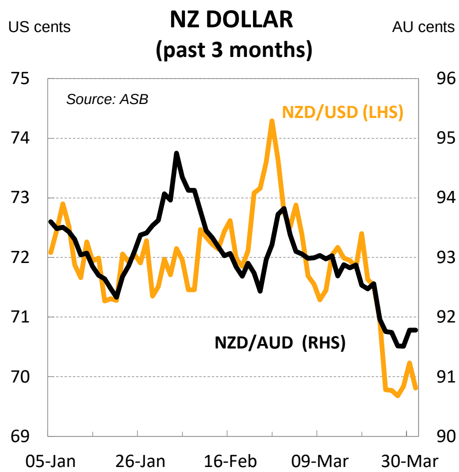
Financial markets remain mixed in March

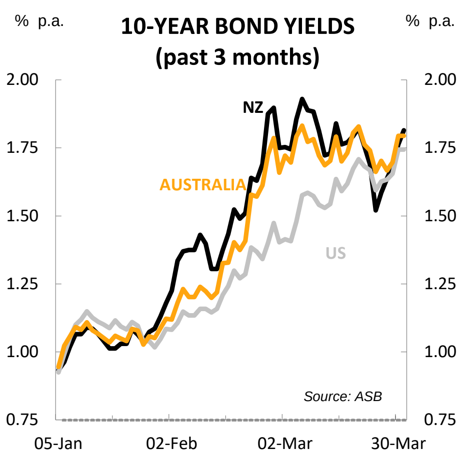
During March we saw a couple of recent financial market themes take a breather. Firstly, after strengthening for several months, the NZD dipped against the major currencies during March. Secondly, long-term bond yields have been on a swift upward rise since late last year, but local yields retreated from recent peaks during March.

Meanwhile, the local sharemarket's underperformance over 2021 has continued. The local market remains over 6% down on its early January peak. We're not alone – the tech-heavy NASDAQ share index is also down circa 6% on its record high as investors weigh up the implications rising interest rates, vaccines, and what it all means for some of the companies that performed so well during the pandemic. At the same time the DJIA and S&P500 indices of US shares are trading around all-time highs.

The big local news during the month was the Government's housing policy announcements. The Government rolled out a trifecta of policies to bolster housing affordability and provision. The policy that caught the most attention was the removal of interest rate deductibility from investor housing. Starting from October this year, deductibility will be reduced in 25% increments for existing properties and will be fully phased out by April 2025. For properties bought after March 26 there will be no ability to deduct. The nationwide impacts would be in the region of $0.5-$1bn per annum according to our estimates. The Government also announced policies to help on the supply side of the problem. Ultimately, we need to build more homes, but it will take time for the announced $3.8bn Housing Acceleration Fund to bear fruit. You can read more here.

During March the NZD lost the gains posted in February and weakened against the major currencies monitored in this report. The Government's housing announcements during the month caused a dip in local interest rates, which in turn weighed on the NZD. Another key theme during March was a firmer USD vis-à-vis most currencies.





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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Date		31-Mar-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	0.04	0.08	-0.14	-2.00
Fixed	NZ 5-year gov't stock	0.71	0.01	0.32	0.00	-1.56
Interest	NZ 10-year gov't	1.82	-0.08	0.82	0.73	-1.11
	AUS 10-year gov't	1.79	0.01	0.82	0.98	-0.70
	US 10-year gov't	1.74	0.27	0.82	1.04	-0.07
Australasian	NZ - NZX50 Capital (NZ$)	5226	2.1%	-4.8%	25.6%	57.9%
	- NZX50 Gross (NZ$)	12561	2.7%	-4.1%	28.2%	86.0%
Equities	AUS - All Ords (A$)	7017	1.1%	2.4%	37.3%	36.2%
International	JAP - Nikkei (¥)	29179	0.7%	6.3%	54.2%	74.1%
Equities	UK - FT100 (£)	6714	3.6%	3.9%	18.4%	8.7%
	US - S&P500 (US$)	3973	4.2%	5.8%	53.7%	92.9%
	WORLD - MSCI (US$)	2812	3.1%	4.5%	51.8%	70.6%
	- MSCI return in NZD		8.8%	8.1%	30.7%	68.6%
Exchange	NZD/USD	0.6981	-5.2%	-3.3%	16.1%	1.2%
Rates	NZD/AUD	0.9178	-2.1%	-2.1%	-5.7%	1.8%
	NZD/JPY	77.36	-1.0%	3.8%	18.6%	-0.2%
	NZD/GBP	0.5085	-3.4%	-4.1%	4.3%	5.7%
	NZD/EUR	0.5963	-1.5%	1.5%	9.3%	-2.2%
	NZ TWI	73.63	-3.3%	-1.6%	7.1%	0.9%

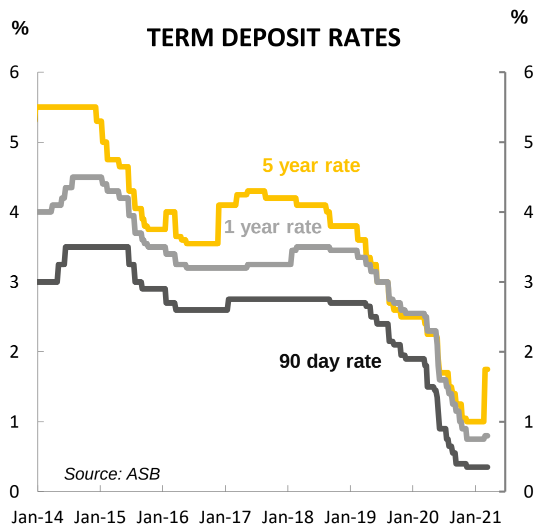
Equity indices are the respective end-of-month closes. Interest rates and exchanges rates are at 5pm NZ. Source ASB, Macrobond.

Income Assets

Cash

ASB's term deposits lifted in early March and have been steady since then. The better-than-expected performance of the economy has significantly reduced the likelihood that New Zealand interest rates will get lower, as we speculated about in 2020, and now we have seen longer-term interest rates start to lift, while the shorter-term rates remain near record lows.

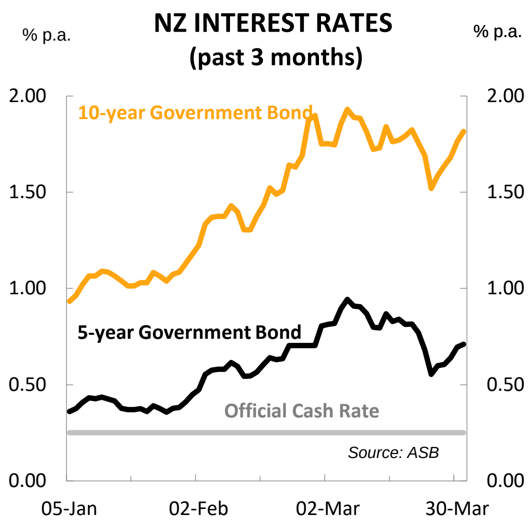
At the time of writing, ASB's term deposit interest rates for amounts over $5,000 are largely between 0.35% and 0.80% for terms between 90 days and 1 year, and between 1% and 1.75% for terms between 18 months and 5 years. Although the lift in early March could be a turning point, rates are still incredibly low. Term deposit interest rates have averaged around 2% to 3% higher than the current rates available for the various terms over the past 10 years. **Furthermore, term deposit returns are still expected to remain low relative to historical averages over the year ahead.**



For the popular term deposit rates – short terms up to 1 year – a key influence is what the RBNZ does with the Official Cash Rate (OCR). In our view, the most likely course for the OCR is that the RBNZ holds it steady over 2021 and early 2022. Then we expect the RBNZ to gradually lift the OCR over several years. We are currently forecasting the OCR to be only 1% higher than it is today in 2024. Over this time term deposit rates should lift, but by a similar modest amount. **Still, we continue to emphasise the uncertainty around the outlook: if the economy struggles again, the OCR could get cut lower than the current 0.25% setting**. We are hopeful that won't transpire, but the surprise weakness in NZ's recent Q4 GDP is a reminder of the risks to our nascent recovery. The RBNZ next monetary policy announcement is on 14 April. Our review of the RBNZ's February meeting is here.

You can read more in our Term Deposit report, and the ASB term deposit rates can be found here.

NZ Fixed Interest



NZ Government bond yields had a mixed month, with both the 5- and 10-year bond yields trading at their highest levels of the year in the first week of the month, then retreating from those highs until 24 March, then selling off (yields higher) into month end. The net result was 5-year yields ended the month little changed, while 10-year yields were down circa 14bps. The 5-year yield is also little changed on year-ago levels, but the 10-year yield is up nearly 70bps on where it traded back in March 2020.

Back in September, the 5-year yield went negative, and the 10-year yield dipped below 0.5%. In early March the 5- and 10-year bonds traded with yields well over 1% higher than last year's lows, at around 1.2% and 1.9%, respectively.

Offshore yields have followed a similar pattern, although the dip and subsequent rise in local yields towards the end of the month has been larger than elsewhere**.** A decent chunk of the fall in NZ yields at this time was due to market reaction around the Government's announcement on housing (see our take).

In the wake of the housing announcement, markets have pushed back the timing of OCR hikes, with the first 25bp move not fully priced until early 2023, about 6 months later than it was implied by market pricing earlier in March. Indicative of the change in market views on the direction of NZ yields, the RBNZ was only able to fully secure $362m of the (scaled down) $430m in NZ Government bonds it was to purchase in the week following the announcement.

International Fixed Interest

Long-term yields in key markets continued to lift over the month, and the US 10-year yield was up 27 points. Meanwhile, central bankers are keeping shorter-term yields low by maintaining their respective record-low target rate settings. The Australian 10-year yield was only up 1 basis point over the month, but that comes after some significant increases in the preceding month. In both Australia and the US, the equivalent US 10-year bond yields are up over 80 basis points or 0.8% over Q1, and around 1% up on year-ago levels.

Japanese and key European yields remain much lower than in Australasia and the US but have also lifted off last year's lows. The lift in long-term yields over the last quarter and 12-month period will have dented global bond portfolio valuations (bond valuations move down as market yields rise).

Central bank messaging remains dovish, but with varying levels of concern about the outlook, and rising long-term yields. The improvement in the US economy discouraged Federal Open Market Committee (FOMC) chair Powell from suggesting the FOMC is considering increasing its pace of asset purchases in the face of higher US yields during the month. The FOMC's stance stands in contrast to the ECB's concern about higher yields and a higher EUR. At its 11 March policy meeting, the European Central Bank (ECB) indicated it will significantly boost the pace of asset purchases under the Pandemic Emergency Purchase Programme (PEPP) over the second quarter. The ECB wants to ensure that the increase in European government bond yields does not move ahead of the domestic economic recovery. At its March meeting, the Bank of England (BoE) made no policy changes and suggested again that additional stimulus is unlikely. The BoE still projects UK GDP to recover rapidly towards pre Covid levels over 2021 and CPI inflation to rise quite sharply towards the 2% target in the spring. The BoE appears unconcerned with higher longer-term government bond yields at this stage.

Meanwhile RBA Governor Philip Lowe struck a dovish tone when he spoke at the AFR Business Summit in mid-March. Governor Lowe also reinforced that a rise in the cash rate in Australia is still a long way off. He said wages growth of around 3% is needed to lift inflation sustainably within target.

UK 10-year GILT yields are near 0.84% at the time of writing, while Japanese 10-year yields remain just above zero. Yields remain negative out to 10 years in France, Germany, Switzerland, and the Netherlands.

Growth Assets

Asset	Index	31-Mar-21 Level	Month %	Quarter %	Year %	5-Year %p.a.
			Change			
Equities	NZ - NZX50 Capital (NZ$)	5226	2.1%	-4.8%	25.6%	9.6%
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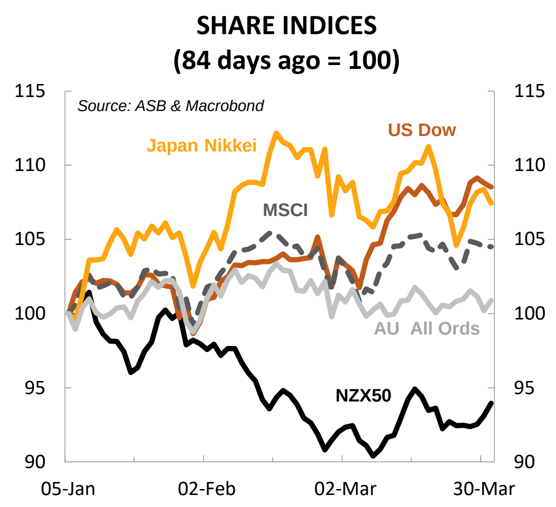
	All Ords in NZD	7645	3.2%	4.6%	45.6%	6.0%
	JAP - Nikkei (¥)	29179	0.7%	6.3%	54.2%	11.7%
	UK - FT100 (£)	6714	3.6%	3.9%	18.4%	1.7%
	US - S&P500 (US$)	3973	4.2%	5.8%	53.7%	14.0%
	WORLD - MSCI (US$)	2812	3.1%	4.5%	51.8%	11.3%

Australasian Equities

After two months of declines, the New Zealand sharemarket recovered some of the lost ground in March and the NZX 50 Gross index lifted 2.7%. The Australian All Ords index rose a more modest 1.1% over the month but has had a much better start to the year and is up 2.4%. Despite the March lift, weakness in January and February has the NZ benchmark down 4.1% over the year to date.



Having set an all-time high in early January, the New Zealand sharemarket was down by over 10% at one stage. Over the month of February, the NZ market declined 6.9%, while the Australian market continued to lift. A more buoyant month of March for NZ shares has the NZ sharemarket trading around 6% off the January highs at the time of writing. Meanwhile the Australian market is trading just over 2% off its peak, and global share indices are similarly buoyant, with the MSCI index of world shares trading within 1% of its all-time high at the time of writing.

There are several factors behind the local sharemarket's underperformance this year covered in earlier Markets Monthly reports. A key part of the local market's weak performance during 2021 has been a function of the strong performance of NZ shares in late December and early January.

Annual performance now includes the recovery from the major sharemarket plunge in March 2020 but drops out the months of decline that occurred as the pandemic unfolded in Q1 2020. The NZX 50 Goss index is up over 28%, and the Australian All Ords is up 37.3% over the year ending 31 March 2021.

International Equities

The MSCI index of world shares rose 3.1% in USD terms in March and starts the second quarter trading within 1% of its all-time high that it reached in mid-February. As discussed above, annual performance numbers now include the recovery from the major sharemarket plunge in early 2020, but not the plunge itself. Accordingly, the annual lift in the MSCI world shares benchmark is a whopping 51.8% over the year to 31 March 2021. The low point for the major sharemarket indices occurred around 23 March 2020.

Although the global sharemarket benchmark posted solid gains, there was a wide range of returns when we look at regional benchmarks. Over the month the US Dow Jones index rose 6.6%, and the S&P 500 index rose 4.2%, with both indexes setting fresh highs. Meanwhile the NASDAQ index was only up 0.4% over March and is 6% off the highs set in mid-February. At one stage the NASDAQ index was down over 10%, and like the New Zealand sharemarket, has only partially recovered. The rapid rise in bond yields that has been occurring over 2021 continues to impact investor sentiment, with mega-cap growth technology shares particularly impacted in late February. Investors also continue to weigh up the implications of current waves of COVID lockdowns. In the US President Biden's US$1.9 trillion stimulus plan and US$2.3 trillion infrastructure package have influenced investor sentiment, and news that a ship had run aground in the Suez Canal added to the global shipping challenges late in the month.

In Europe, the German DAX index surged 8.9% and the UK FTSE rose 3.6% over March.

Japanese shares have performed well over the first quarter of 2021. In February the Nikkei index rose by 4.7%. In March the gains were more modest, but the 0.7% lift means the Nikkei is up 6.3% over the first quarter, and 54.2% over the year to 31 March.

ASB Securities has more information on sharemarkets and trading here.

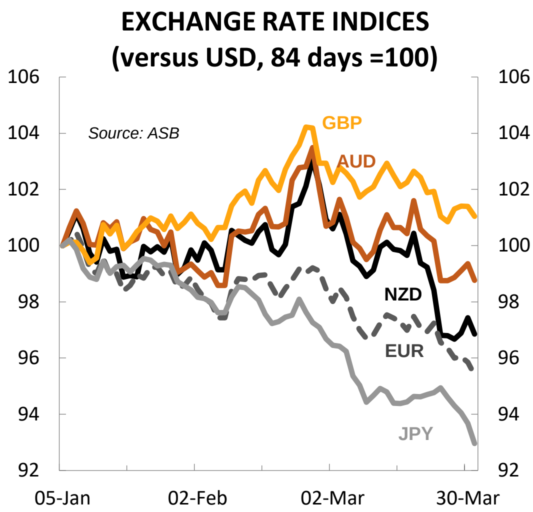
Exchange Rates

During March the NZD lost the gains posted in February and weakened against the major currencies monitored in this report. The Government's housing announcements during the month caused a dip in local interest rates, which in turn weighed on the NZD. Another key theme during March was a firmer USD vis-à-vis most currencies, as shown to the right.

NZD/USD dipped over 5% during the month, in doing so the pair dipped below 0.7000 for the first time since late last year. NZD/AUD also broke out of its recent range centred on 0.9300, dipping below 0.9200 over the last week of March.

On a trade-weighted basis the NZD declined 3.3% over the month, but is up 7% on year-ago levels, when the COVID-19 pandemic was causing significant stress in financial markets.

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



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