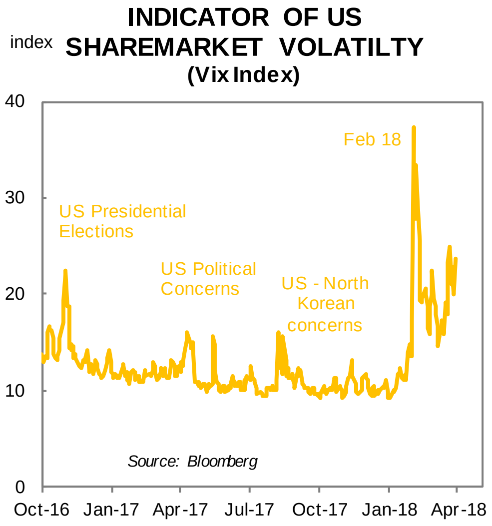
Sharemarket slide resumes in March

- Global sharemarkets declined over March, sinking to fresh 2018 lows. Global trade and growth concerns emerge.
- In the US, the FOMC lifted the Fed Funds rate. But long-term yields declined over the month.
- Widening credit spreads in the US (and Australia) warrant monitoring.
- The RBNZ got a new Governor and a new Policy Target Agreement in March. Neither changes our view the OCR is staying at 1.75% until the second half of 2019.

Sharemarkets weakened for a second consecutive month in March, eclipsing the gains recorded in January. As a result, the major share indices we monitor all ended Q1 2018 in negative territory. Investors grappled with a number of concerns including the risk of a tariff war between China and the US, signs of stress in US and Australian short-term funding markets, as well as another rate hike from the US Fed. The Russian diplomatic expulsions in response to a nerve agent attack in the UK added further uncertainty to the mix.

The big driver of market uncertainty was the trade skirmish between the US and China. US President Trump announced tariffs on steel and aluminium on 2 March, and introduced further measures against China specifically later in the month (and early April). In response to the initial tariffs, China imposed tariffs on US imports worth US$3bn. Trump signed a presidential memorandum outlining possible tariffs to be applied to circa US$50bn of Chinese imported goods.



Meanwhile, the tech-heavy NASDAQ share index declined 2.9% for the month, slightly more than the S&P 500 index of US shares (-2.7%). March was a particularly bad month for Facebook. Its shares fell 6.8% in a single day after it revealed that a political consultancy firm had obtained unauthorised access to 50 million accounts. Facebook shares are currently trading around 20% off the highs recorded in February.

Increased US protectionism and the associated risk of a trade war threaten the positive global growth outlook that has been supporting commodity prices. The tariff threats weighed on commodity prices over March. Oil was an exception

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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to the downtrend, with prices betwixt the opposing forces of OPEC supply cuts, expected US production gains, and emerging global growth concerns. Closer to home, dairy prices were largely flat (at healthy levels) during March, and Fonterra revised up its milk price forecast during the month.

The US Federal Reserve lifted the Federal Funds rate by 25 basis points, as expected in March. The US-China trade skirmish has not changed policy makers' outlooks at this juncture, and "the Fed" remains committed to its path of interest rate increases.

A concerning recent development has been some signs of stress in US short-term funding markets. Bank Bill or Libor-OIS spreads can be used as a measure of how expensive or cheap it will be for banks to borrow relative to a risk-free rate. These "spreads" provide a handy signpost for credit conditions and emerging pressures in money markets where banks can fund. The USD Libor-OIS spread has widened significantly over February and March. In saying that, the lift in spreads has been mild compared to the Global Financial Crisis, where concerns over the credit worthiness of financial institutions triggered a sharp increase in spreads (read more here).

The combination of the US rate hikes delivered, and the widening spreads discussed above is putting upward pressure on short-term rates in the US. In contrast, nervous investors moving out of shares and into bonds have put downward pressure on longer-term rates, which declined in the US and elsewhere.

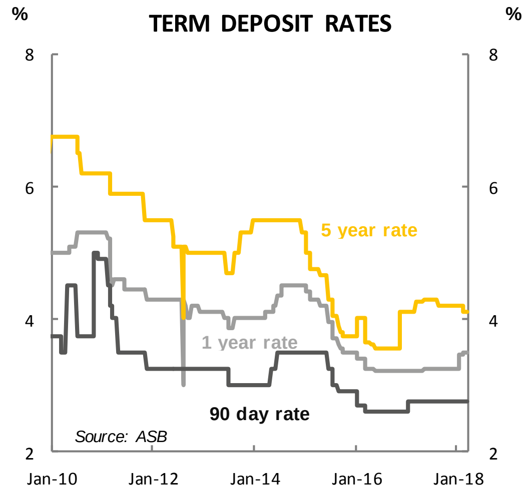
Also over the month the Government and the new RBNZ Governor signed a new Policy Targets Agreement . The Agreement retained the 1-3% CPI inflation target as the sole mandate, but added the requirement of the RBNZ to aim towards "supporting maximum sustainable employment within the economy" (read more here).

Lastly, the RBNZ held the OCR at 1.75% at its March review. We expect the OCR to remain at this level until the second half of 2019.

Date	Instrument	31-Mar-18	Month %	Quarter %	Year %	5-Year %
Cash	NZ Official Cash Rate	1.75	0.00	0.00	0.00	-0.75
	NZ 90-day bank bill	1.96	0.04	0.08	-0.04	-0.68
Fixed	NZ 5-year gov't stock	2.28	-0.15	0.03	-0.19	-0.57
Interest	NZ 10-year gov't	2.71	-0.24	-0.02	-0.48	-0.79
	AUS 10-year gov't	2.60	-0.18	-0.07	-0.11	-0.82
	US 10-year gov't	2.74	-0.16	0.30	0.32	0.90
Australasian	NZ - NZX50 Capital (NZ$)	3777	-1.7%	-2.0%	11.5%	52.7%
	- NZX50 Gross (NZ$)	8322	-0.6%	-0.9%	15.6%	88.2%
Equities	AUS - All Ords (A$)	5869	-4.1%	-4.8%	-0.6%	17.9%
International	JAP - Nikkei (¥)	21454	-2.8%	-5.8%	13.5%	73.0%
Equities	UK - FT100 (£)	7057	-2.4%	-8.2%	-3.6%	10.1%
	US - S&P500 (US$)	2641	-2.7%	-1.2%	11.8%	68.3%
	WORLD - MSCI (US$)	2067	-2.4%	-1.7%	11.5%	44.1%
	MSCI in NZD (NZ$)	2856	-2.5%	-3.7%	7.6%	66.4%
Exchange	NZD/USD	0.72	0.1%	2.0%	3.6%	-13.4%
Rates	NZD/AUD	0.94	1.6%	3.6%	3.2%	17.6%
	NZD/JPY	76.91	-0.7%	-3.9%	-1.8%	-2.2%
	NZD/GBP	0.52	-0.7%	-2.1%	-7.7%	-6.5%
	NZD/EUR	0.59	-0.6%	-1.1%	-10.2%	-10.1%
	NZ TWI	74.52	0.1%	0.5%	-1.8%	-2.7%
Equity indices are the respective end-of-month closes. Interest rates and exchanges rates are at 5pm NZ.						

Income Assets

Cash



A new Policy Target Agreement was signed by the Minister of Finance Grant Robertson and RBNZ Governor Adrian Orr in the final week of March. The RBNZ's annual consumer price inflation target range remains 1% to 3% over the medium term, with the ongoing focus on the 2% midpoint. However, an employment focus was added alongside the RBNZ's price stability objective. The announced changes are unlikely to significantly impact on the level of the OCR or its movements over the cycle.

The Reserve Bank of New Zealand (RBNZ) left the Official Cash Rate (OCR) on hold at 1.75% at its 22 March meeting, as expected. With inflation yet to pick up materially, the RBNZ should remain comfortable with earlier forecasts that suggest it will leave the OCR on hold until at least the second half of 2019.

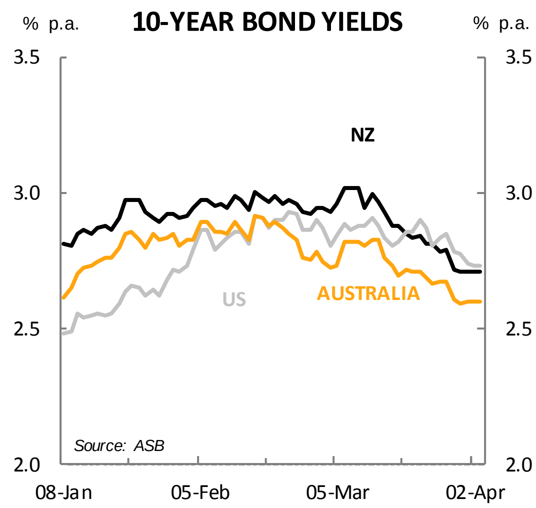
If OCR hikes are still a long way off, most short-term fixed interest returns on term deposits will likely stay near current levels over the year ahead. At the time of writing, **term deposit rates** are between 2.75% to 4.1% for terms between 90 days and 5 years for term deposits over $10K. Over the past 10 years deposit rates have averaged between 0.9% and 1.5% higher than the current rates available for the various terms.

The upward pressure on long-term global rates we have observed over Q4 2017 and early 2018, if resumed and sustained, could translate to slightly higher interest rates on some of the longer term deposit rates. The opposite actually happened in February, with the term rates for two years and longer dipping 0.1%, while the 9- and 12-month rates lifted 0.05%.

We are factoring in upward pressure on the longest term deposit rates over the year from lifting global rates. However, we expect term deposit rates for all terms to remain low this year relative to the long-term averages mentioned above.

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

NZ Fixed Interest



For the first time since 1994, New Zealand Government bonds are trading with lower yields than their US counterparts. New Zealand bonds typically trade with yields that are higher than their US equivalents, but that yield advantage has disappeared for now, with the NZ 10-year yield dipping below the US yield in March.

The dominant theme for bonds over recent months has been rising US (and global) yields. However, the recent concerns that have rattled sharemarkets have triggered a flight to the safety of bonds. That demand has seen yields decline both here and abroad during March, with New Zealand's yields declining by more than offshore yields during the month's rally.

We continue to expect long-term local bond yields to rise modestly over the year ahead, which will eventually boost the income for investors receiving income from fixed interest investments. Despite this, we expect the return on NZ fixed income investments over the year ahead will remain lower than long-term averages.

International Fixed Interest

The US Federal Reserve lifted the Federal Funds rate by 25 basis points, as expected in March. The Fed looks set to deliver several more interest rate increases over this year and next. Those Fed Funds rate increases have been putting upward pressure on US bond yields over the past year. But in March, sharemarket jitters as well as the fallout from the US-China trade issues saw long-term global government bond yields decline in the US and elsewhere.

Nervous investors moving out of shares and into bonds have put downward pressure on longer-term rates. This “flight to safety” saw the US 10-year Government bond yield fall 16 basis points or 0.16% over the month, to yield 2.74% at month end. Having swiftly lifted towards 3% over late 2017 and early 2018, the US 10-year yield has failed to break above the 3% mark for the third time since 2011. In Europe, 10-year German bund yields posted a similar decline over March, but yields are far lower than in the US. The German 10-year bund yield dipped from a high of 0.77% in February, back down to 0.5% by March end.

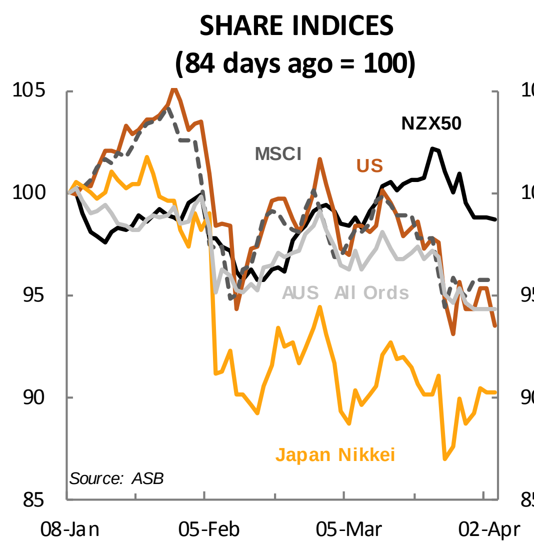
For now, global bond yields are moving in the opposite direction (down) to our long-term forecasts of modestly increasing global interest rates. While global growth concerns and sharemarket jitters persist, long-term yields are expected to remain contained.

Growth Assets

Australasian Equities

The local NZX50 Gross Index has been caught in the downdraft of the US sharemarket decline over February and March, but the declines have been modest relative to global sharemarket weakness. The local sharemarket was down by 0.6% during March and 0.9% over Q1 2018 (NZX 50 Gross).

The Australian All Ords share index eased 4.1% over the month. The consumer durables & apparel industry sector was hardest hit, and fell by 9.1%. The Resources sector fell by 5.7% in March, dragged down by weaker iron ore prices.



International Equities

Three developments were important to global sharemarket sentiment during March. Most important was the US announcements on tariffs, and the associated responses. But the US Federal Funds rate hike and the data breaches at Facebook were also significant events.

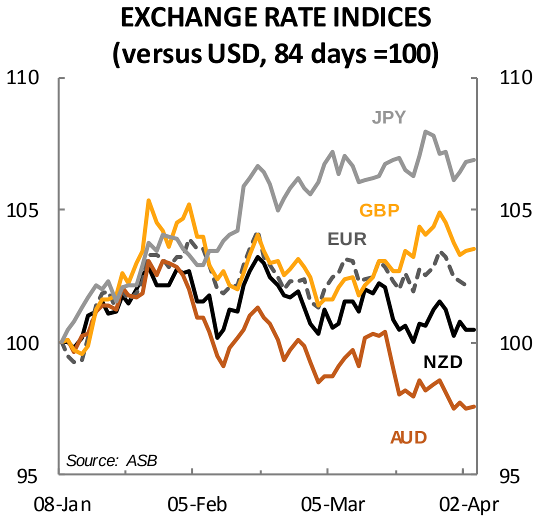
Over the early stages of March the US sharemarket posted solid gains, with the S&P 500 index lifting 4% between 1 and 9 March. But from the month’s high the S&P 500 index declined over 6%, and closed the month down 2.7%. Across Europe the German DAX fell by 2.7%, while the London FTSE fell by 2.4%. In Japan, the Nikkei was 4.1% lower.

On March 19 shares in Facebook fell 6.8% after it revealed that political consultancy Cambridge Analytica obtained unauthorised access to 50 million social media accounts. The breach weighed on share prices of Facebook, but the potential for greater regulation also hurt the share prices of other technology companies.

On March 22 US President Trump signed a presidential memorandum outlining possible tariffs to be applied on Chinese goods. Global shares were particularly weak on March 22 and 23 on fears of a trade war between the US and China.

ASB Securities has more information on sharemarkets and trading here.

Exchange Rates:



NZD lifted in the first half of March, but gave back all its gains over the rest of the month, to end little changed vis-a-vis the USD, as well as on a trade-weighted basis.

Data at the start of the month showed that New Zealand's Terms of Trade reached a record high in Q4 2017. The high Terms of Trade is a key factor behind ASB Economics' strong NZD exchange rate forecasts over the next few years.

Rising global trade tensions knocked the NZD (and AUD) lower later in the month.

GBP strengthened against the other major currencies during March, and NZD/GBP eased 0.7%. GBP sentiment was boosted by the EU and the UK government agreeing to a Brexit transition deal which will last until December 2020.

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