

Markets Monthly

04 June 2021

Mixed month of May for financial markets

Long-term global bond yields were mixed over May, even though there were plenty of headlines about rising inflation pressures. Nonetheless, government yields here and around the world are significantly higher than the levels they were a year ago. The lift in yield has weighed on bond valuations and fixed interest portfolios' performances.

At its May meeting, all the RBNZ's key policy levers remained steady. The RBNZ has published an OCR track for the first time in a while, which shows the Bank making its first 0.25% rate hike in Q3 2022. Following the meeting, ASB economists brought forward our forecast of the first RBNZ OCR increase to May 2022 (from August).

Meanwhile, the local sharemarket's underperformance over 2021 has continued into May. After posting modest gains over March and April, the local market dipped in May while the major global sharemarkets pressed higher.

The NZD was mixed during the month and dipped 0.3% on a trade-weighted basis.

Date		31-May-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	0.32	-0.04	0.02	0.06	-2.10
Fixed Interest	NZ 5-year gov't stock	1.07	0.19	0.36	0.70	-1.11
	NZ 10-year gov't	1.80	0.15	-0.10	0.98	-0.81
	AUS 10-year gov't	1.59	-0.11	-0.19	0.69	-0.71
	US 10-year gov't	1.58	-0.07	0.11	0.91	-0.28
Australasian Equities	NZ - NZX50 Capital (NZ\$)	5119	-3.4%	0.0%	10.8%	48.8%
	- NZX50 Gross (NZ\$)	12321	-3.2%	0.8%	13.2%	74.9%
Equities	AUS - All Ords (A\$)	7407	1.6%	6.7%	26.1%	36.0%
International Equities	JAP - Nikkei (¥)	28860	0.2%	-0.4%	31.9%	67.5%
Equities	UK - FT100 (£)	7023	0.8%	8.3%	15.6%	12.7%
	US - S&P500 (US\$)	4204	0.5%	10.3%	38.1%	100.5%
	WORLD - MSCI (US\$)	2976	1.3%	9.1%	38.5%	77.7%
	- MSCI return in NZD		1.1%	10.7%	18.5%	64.7%
Exchange Rates	NZD/USD	0.7259	0.2%	-1.4%	16.9%	7.9%
	NZD/AUD	0.9392	0.8%	0.2%	0.6%	1.2%
	NZD/JPY	79.60	1.0%	1.9%	19.7%	6.5%
	NZD/GBP	0.5113	-1.6%	-2.9%	1.7%	11.6%
	NZD/EUR	0.5951	-0.5%	-1.7%	6.4%	-1.5%
	NZ TWI	75.01	-0.3%	-1.5%	7.5%	3.4%

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](#).

Income Assets

Cash

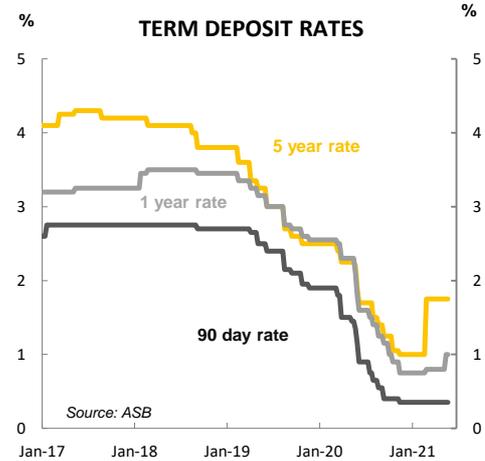
ASB's term deposit rates lifted in early March and again in May. The biggest movements have been in the longer terms. The shorter-term rates (up to six months) remain at or near their lows, as tabled below.

Term Deposit Rates	90-days	6 months	9 months	1 Year	2 years	3 years	4 years	5 years
10-year ave	2.70	3.34	3.39	3.45	3.67	3.84	4.01	4.15
Low	0.35	0.80	0.75	0.75	0.80	0.90	1.00	1.00
May-21	0.35	0.80	0.90	1.00	1.10	1.25	1.50	1.75

Despite the increases, 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, even though annual CPI inflation is expected to lift back above 2%.

A key influence is what the RBNZ does with the Official Cash Rate (OCR). Following the RBNZ's meeting in May, ASB economists brought forward our forecast of the first RBNZ OCR increase to May 2022 (from August). Our full report on the May meeting and the implications can be read [here](#).

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



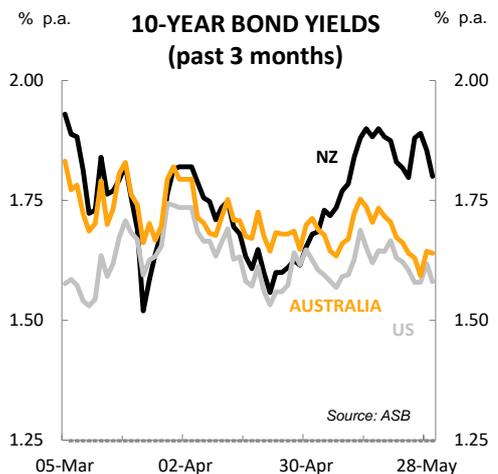
NZ Fixed Interest

NZ Government bond yields lifted in May, in contrast to the decline in offshore rates.

The 5-year yield ended the month up 19 basis points over May and is trading around 10 points off their March peak, while 10-year yields were up 15 basis points in the month, such that they are also now just circa 10 points off their early March peak. The 10-year Government bond yield is now up around 100 basis points on year-ago levels, and 130 basis points off the lows of the past year. The annual lift in long-term yields has weighed on bond valuations and fixed interest portfolios' performances. Long term corporate bond yields also lifted over the month.

At its May meeting, all the RBNZ's key policy levers remain on hold, with the OCR on hold at 0.25%, the Large-Scale Asset Purchase (LSAP) parameters unadjusted at \$100bn by June 2022, and no adjustments to the Funding for Lending Programme. The RBNZ has published an OCR track for the first time in a while, which shows the Bank making its first 0.25% rate hike in Q3 2022, and with the OCR expected to reach 1.5% by the end of 2023 (versus our own view of a 1.25% OCR by that date).

On the LSAP front, the RBNZ, was explicit in noting that the \$100bn cap was unlikely to be met. The lower pace of government bond issuance relative to what was previously expected will tend to result in a slower pace of asset purchases by the RBNZ and will also reduce the leeway for the LSAP given the crown indemnity limit. We expect that the LSAP will peak at around \$75bn in early 2022, with the programme to be halted in 2022 prior to the OCR moving up (likely May in ASB's forecasts).



International Fixed Interest

The US 10-year treasury yields pressed lower over May, declining by around 7 basis points over the month, after a similar dip in April. Despite the decline over the past two months, long-term US yields are up significantly (circa 90 basis points) on year-ago levels. Similarly, the Australian 10-year government bond yield dipped in May but is up 74 basis points on a year ago.

The RBA left monetary policy unchanged at its May meeting and announced it will make a decision on its yield curve control and QE program at its meeting in July. The RBA significantly upgraded its economic projections in its May Statement of Monetary Policy.

US Treasury Secretary (and former FOMC Chair) Janet Yellen commented during the month that interest rates would need to rise somewhat to ensure the economy did not overheat. Ms. Yellen later watered down the comment, saying higher rates weren't something she was "predicting or recommending." Nonetheless, markets are keeping a wary eye on any comments from central bankers, as well as the inflation data. One such data focus was within the Institute of Supply Management (ISM) services index, where the prices paid index hit a 13-year high in April. The minutes from the April 27-28 Federal Reserve meeting also revealed a number of participants were open to discussing a plan for adjusting the pace of asset purchases should the economy continue to make rapid progress toward the (policy-setting) Committee's goals. Against this backdrop, the decline in long-term US yields over the month is surprising. Falling US 10 year nominal yields indicate confidence that the Fed will keep accommodative policy settings. Meanwhile, higher US 10 year inflation expectations reflect confidence in a strong recovery for the US economy.

Yields in the major bond markets in Europe remain lower than US and Australasian yields. UK 10-year gilt yields are near 0.82% at the time of writing, little changed on a month ago, and in the top half of the 0.683-0.896 range of the past three months. Yields remain negative out to 10 years in Germany, Switzerland, and the Netherlands. The French 10-year bond now is priced with a positive yield of 0.18%.

Weak prices in Japan stand in stark contrast to US inflation which has lifted on multiple measures. Data released in May showed Japan's core CPI fell into deflationary zone once again at -0.2%/yr for April. Japanese 10-year yields remain just above zero, yielding 0.07% at the time of writing.

Growth Assets

Asset	Index	31-May-21 Level	Month %	Quarter %	Year %	5-Year %p.a.
			Change			
Equities	NZ - NZX50 Capital (NZ\$)	5119	-3.4%	0.0%	10.8%	8.3%
	- NZX50 Gross (NZ\$)	12321	-3.2%	0.8%	13.2%	11.8%
	AUS - All Ords (A\$)	7407	1.6%	6.7%	26.1%	6.3%
	All Ords in NZD	7886	0.8%	6.5%	25.4%	6.1%
	JAP - Nikkei (¥)	28860	0.2%	-0.4%	31.9%	10.9%
	UK - FT100 (£)	7023	0.8%	8.3%	15.6%	2.4%
	US - S&P500 (US\$)	4204	0.5%	10.3%	38.1%	14.9%
	WORLD - MSCI (US\$)	2976	1.3%	9.1%	38.5%	12.2%

Australasian Equities

The New Zealand sharemarket weakened over May and is now down circa 10% on its January peak. In contrast, the Aussie sharemarket rose for the eighth consecutive month, and is trading at an all-time high.

The a2 Milk Co's share price dipped below \$6 during the month, from \$12 at the start of the year. During the month the company's latest announcement confirmed that the trading dynamics in the China infant nutrition market continue to be challenging.

Fisher & Paykel Healthcare dipped below \$30 in late May, having started the month near \$36. Late in the month the company announced that net profit after tax was \$524 million, which is up 82% over the previous financial year. However, the outlook for the year ahead is difficult to forecast, and the company noted that "with the ongoing uncertainties of vaccinations, lockdowns, COVID-19 variants, localised waves and return to stable hospitalisation rates

around the world, the company is not providing guidance for the 2022 financial year”.

Fonterra Shareholders’ Fund’s price was also a laggard during May, dipping below \$4. At the start of May Fonterra announced a consultation process about options to change its capital structure. The unit price is down circa 15% since the announcement.

It wasn’t all bad news in the local market however, and Freightways, Mainfreight, Fletcher Building, Spark, Contact Energy, Infratil and EBOS all posted solid gains.

The Australian All Ords index rose 1.6% over the month in AUD terms and 0.8% in NZD terms. That’s eight consecutive months of gains for the Australian benchmark, which starts June at a record high.

Reserve Bank of Australia commentary reaffirmed that interest rates would remain at record low levels for several years, but July appears to be a pivotal month for the RBA, as discussed in the *International Fixed Interest* section above. During May, seven of the 11 industry sectors posted gains led by Financials (up 4.4%) and Health Care (up 3.5%). Information Technology lost 9.9% and Utilities were down 7.0%.

International Equities

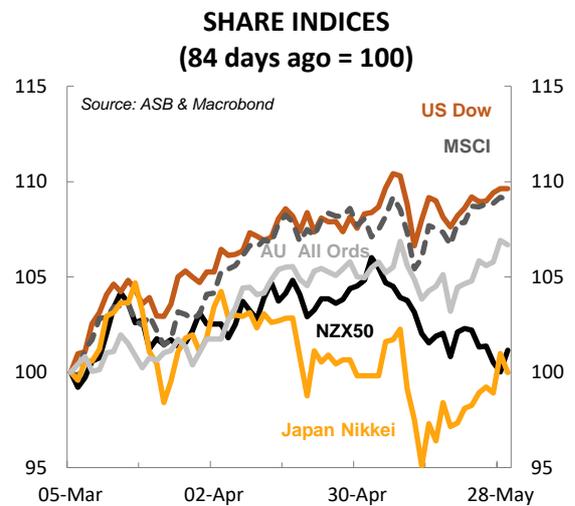
The MSCI index of world shares rose 1.3% in USD terms in May and set fresh record highs during month.

Over May, global bourses were generally higher. In the US, value stocks appeared in favour over growth stocks. Reflecting this theme, the Dow rose 1.9%; the S&P 500 rose 0.6%; but the Nasdaq fell by 1.5%.

In Asia the Japanese Nikkei rose 0.2%.

European shares received a boost at the start of the month after the European Commission outlined plans to loosen Covid-19 restrictions on tourism, following new figures that showed a lift in vaccinations against the virus. The German Dax rose 1.9% in May, while the UK FTSE rose by 0.8% over the month.

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



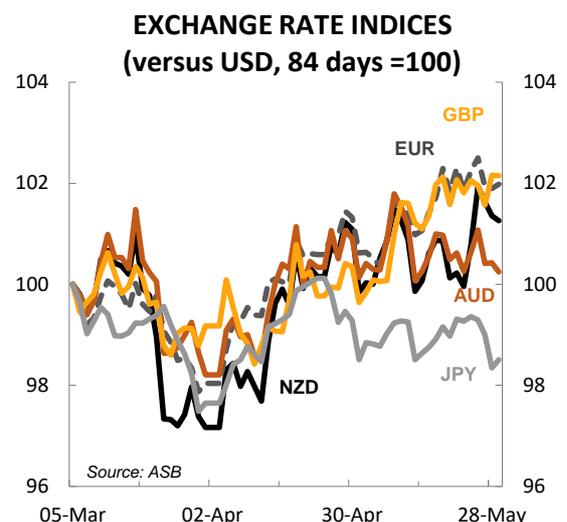
Exchange Rates

NZD was little changed on a trade-weighted basis in May. NZD outperformed against the USD, AUD and JPY, but eased against GBP and EUR.

NZD/USD was largely driven by the USD’s direction in the first half of May. However, the largest catalyst for a jump in NZD during the month was the hawkish turn by the RBNZ on 26 May. The RBNZ surprised market participants and analysts by publishing an Official Cash Rate profile with 150bps of hikes, starting next year. NZD jumped around 1.3% to trade above 0.7300 after the release.

NZD outperformed the AUD during the month, with the cross rate lifting 0.8% over May, to trade back around 0.9400 at month end.

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



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