Markets Monthly

04 December 2019

Sharemarkets surge over November

- Sharemarkets were strong in November, with the main US share indices reaching fresh record highs late in the month. The NZ sharemarket posted an extremely strong 5% lift over the month.
- After the swift lift higher in October, long-term yields dipped modestly lower both here and offshore in November. Global bonds have been choppy: yields are up over the past three months, but remain significantly below year-ago levels.
- Conviction regarding multiple RBNZ interest rate cuts waned over the month, and the RBNZ remained on hold at its November review. The NZD was flat against the USD, but lifted on a trade weighted basis.

Date		30-Nov-19	Month %	Quarter %	Year %	5-Year %
Cash	NZ Official Cash Rate	1.00	0.00	0.00	-0.75	-2.50
	NZ 90-day bank bill	1.23	0.11	0.03	-0.75	-2.45
Fixed	NZ 5-year gov't stock	1.10	0.08	0.26	-1.46	-2.68
Interest	NZ 10-year gov't	1.30	-0.02	0.23	-0.72	-2.60
	AUS 10-year gov't	1.03	-0.13	0.14	-1.56	-2.03
	US 10-year gov't	1.77	-0.02	0.26	-1.25	-0.44
Australasian	NZ - NZX50 Capital (NZ$)	4860	4.7%	4.1%	23.9%	71.6%
	- NZX50 Gross (NZ$)	11331	5.0%	5.3%	28.4%	108.9%
Equities	AUS - All Ords (A$)	6948	2.6%	3.7%	20.8%	31.1%
International	JAP - Nikkei (¥)	23294	1.6%	12.5%	4.2%	33.4%
Equities	UK - FT100 (£)	7347	1.4%	1.9%	5.2%	9.3%
	US - S&P500 (US$)	3141	3.4%	7.3%	13.8%	51.9%
	WORLD - MSCI (US$)	2292	2.6%	7.2%	12.3%	31.8%
	MSCI in NZD (NZ$)	3569	2.7%	5.1%	20.1%	60.6%
Exchange	NZD/USD	0.6422	-0.1%	2.0%	-6.5%	-18.0%
Rates	NZD/AUD	0.9482	2.2%	1.1%	1.1%	2.9%
	NZD/JPY	70.31	0.7%	4.9%	-9.7%	-24.1%
	NZD/GBP	0.4973	0.1%	-3.8%	-7.4%	-0.2%
	NZD/EUR	0.5832	1.3%	2.3%	-3.2%	-7.3%
	NZ TWI	71.22	0.7%	1.1%	-4.8%	-8.9%
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.

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Market News

Where to next for interest rates remains a key question in financial markets, with bond yields trading well above the lows set in earlier months, but significantly down on year-ago levels. The swift move from the recent lows has caused some noticeable changes in bond portfolio valuations. Earlier in the year, many of the world's central banks were in easing mode, and that helped drive long-term yields lower (boosting bond portfolio valuations). Now we are seeing many (including the RBNZ) push pause. The pause has some market participants wondering if we are at the low point for policy settings, and past the low point for longer-term yields. We think we could see further cuts from the RBNZ and other central banks over 2020, but market sentiment regarding the future course for policy settings from the RBNZ (and others) has changed a lot over the past month.

Another key theme has been the US-China trade war and the related broader concerns over the global economic outlook. Sentiment that a US-China deal is imminent remained high for most of November, reflected by the optimism in sharemarkets. But realistically, the story remained the same – markets have been high on optimism, but light on specific details from officials. And now investors are taking a reality check in early December. Reuters reported that *"sentiment worldwide took a hit after US President Donald Trump said he would immediately restore tariffs on US steel and aluminium imports from Brazil and Argentina, accusing them of devaluing their currencies to the detriment of US farmers."* China has called for a rollback of US tariffs before it would agree to a trade deal. Then Trump said a Chinese trade deal might have to wait until after the US election (November 2020), dashing hopes a deal could be reached before the latest tariff increases go through on 15 December. Trump is also threatening 100% tariffs on a range of French products, drawing the inevitable response from French President Macron. Weaker US manufacturing and construction data also weighed on sentiment in early December, despite anecdotes of strong retail sales on Black Friday and Cyber Monday.

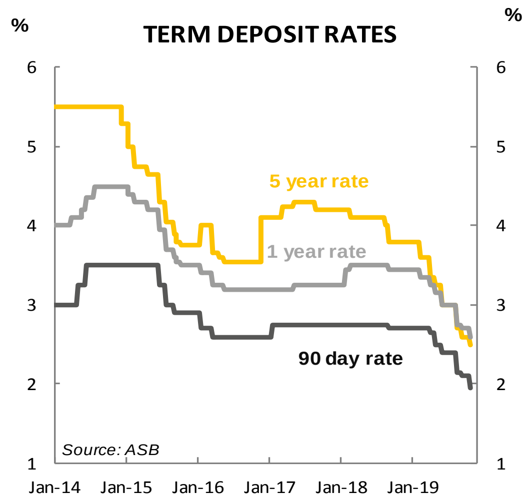
The UK heads back to the polls for a General Election on 12 December. The European Union (EU) has provided a Brexit extension till the end of January 2020, and fears of a "hard Brexit" have reduced. A lot rides on the election outcome, where PM Johnson looks to strengthen his power so he can push through the latest withdrawal agreement with the EU. A risk with this strategy is a repeat of the experience of former PM May in 2017, where the election result clearly made executing an exit from the EU harder, not easier. But at this stage the polls suggest the Conservatives should gain more seats from the election.

In Australia, the RBA left its cash rate unchanged in November and December (as expected), but it was clear from its statements and comments that Australia's central bank remains ready to cut, if needed, in the future. The RBNZ also left the Official Cash Rate (OCR) unchanged last month. In contrast to the RBA, the RBNZ was widely expected to cut the OCR at the review. Instead, the RBNZ appears comfortable with current interest rate settings now and into the future. The next RBNZ OCR review is in February, but before then there will be significant interest in the RBNZ's final decisions from its Capital Review (5 December). Despite the late 2019 pauses, we continue to expect the RBA and the RBNZ to reduce their respective policy settings in 2020.

Income Assets

Cash

The OCR was cut by 0.50% to a new record low 1.00% at the RBNZ's 7 August meeting, and then held it at this level at the subsequent OCR reviews in September and November. We were surprised by the RBNZ twice over recent months – we didn't expect the 0.5% cut in August (we expected a "standard" 0.25% cut), and we expected a 0.25% reduction in November. The RBNZ are clearly comfortable with the current interest rate settings.



The global scene looks to have stabilised and interest rate sensitive pockets of the economy are responding to the 75bps of OCR cuts delivered over 2019.

Nonetheless, we continue to expect another OCR cut from the RBNZ, and still have a 0.25% cut penciled into our forecasts for next May, with 0.75% now our expected low point for the OCR this cycle.

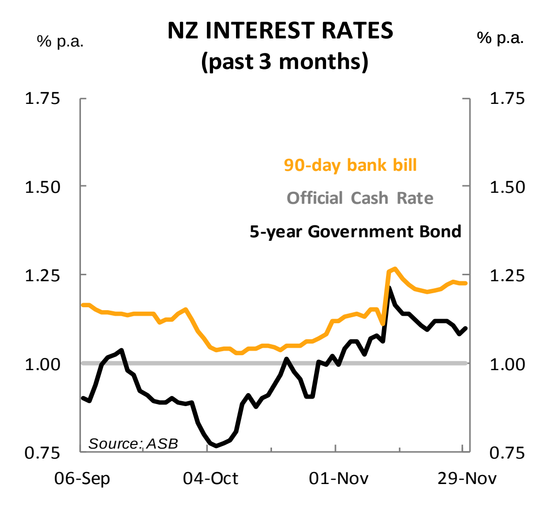
Term deposit interest rates have drifted lower since the August OCR cut, including modest falls over November. For amounts over $10k, term deposit rates for 2-5 years are around 2.5%. Rates for shorter 3-month terms are now slightly below 2%, and 4- to 12-month rates are between 2% and 2.6%.

We think the risk for savers is that term deposit rates move even lower, particularly if the OCR is cut further. The imposition of higher bank capital requirements for locally-incorporated banks from the RBNZ could also put downward pressure on term deposit rates (and/or upward pressure on borrowing rates). On 5 December, the RBNZ announce the details of the future capital requirements for locally-incorporated banks.

The latest ASB term deposit rates can be found here.

Asset	Instrument	30-Nov-19 Yield (%)	Month	Quarter	Year	5-Year
			Yield Change			
Cash	NZ Official Cash Rate	1.00	0.00	0.00	-0.75	-2.50
	NZ 90-day bank bill	1.23	0.11	0.03	-0.75	-2.45
	US 90-day bank bill	1.91	0.00	-0.22	-0.83	1.67
Fixed	NZ 5-year gov't stock	1.10	0.08	0.26	-1.46	-2.68
Interest	NZ 10-year gov't	1.30	-0.02	0.23	-0.72	-2.60
	NZ 10-year swap	1.49	0.07	0.23	-1.41	-2.84
	AUS 10-year gov't	1.03	-0.13	0.14	-1.56	-2.03
	US 10-year gov't	1.77	-0.02	0.26	-1.25	-0.44

NZ Fixed Interest

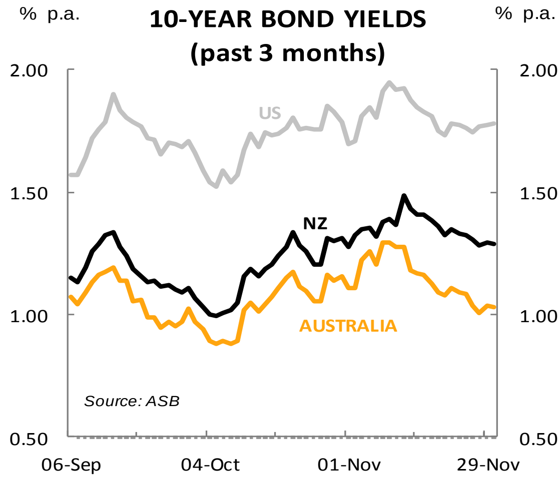


The NZ 10-year Government bond yield dipped to an all-time low of 0.979% in mid-August, and was back below 1% briefly for a second time in early October. But since 8 October, the yield has been drifting higher. At one point in November the yield was above 1.5%. However, by month end, the 10-year bond yield was back at 1.3%, 2 basis points, or 0.02% below where it was at the start of the month. At the time of writing the 10-year yield is 1.4%. The 5-year yield lifted 8 basis points or 0.08%. Bond prices move in the opposite direction to yield, so the sharp lift in yield from the lows has been negative for bond portfolios. However, even though bond yields are off the 2019 lows, NZ corporate and Government Bond yields remain incredibly low on a historical basis. Bond yields are also significantly lower than a year ago, which has supported annual returns for portfolios. Corporate bond yields also lifted over the month, particularly the shorter-dated bonds, as markets adjusted to factor in less RBNZ rate cuts.

We now only expect one further 25bp OCR cut, taking the OCR to a new record low 0.75% in 2020. We still expect global central banks to continue to ease policy settings. Accordingly, our view remains that we could see lower NZ bond yields over the year ahead, but improved economic sentiment is seeing yields move in the opposite direction in late 2019.

International Fixed Interest

After the US Federal Open Market Committee's (FOMC, or Fed) last cut to the Federal Funds rate target range on 30 October, committee members including Chair Powell have indicated that the bar to further rate cuts is high, and "monetary policy is in a good place". The FOMC's stance, combined with positive sentiment regarding the US economy, has helped long-term US yields move significantly off the lows recorded in the third quarter.



US 10-year yields dipped 2 basis points over the month, and are trading around 0.3% above recent lows. European 10-year yields remain negative in France, Germany, Sweden, the Netherlands and Switzerland. Japanese 10-year yields also remain negative. But in each case, yields have become "less negative" over recent months.

We continue to think policy settings at the world's major central banks risk moving lower. And related to this, long-term interest rates could retrace the recent lift if some of the recent threats resurface, muting global growth and inflationary pressure. Another turn for the worse in the US-China situation is the obvious risk, and indeed bond yields have dipped in early December as the negotiations appeared to sour.

Growth Assets

Asset	Index	30-Nov-19 Level	Month %	Quarter %	Year %	5-Year %
				Change		
Equities	NZ - NZX50 Capital (NZ$)	4860	4.7%	4.1%	23.9%	11.4%
	- NZX50 Gross (NZ$)	11331	5.0%	5.3%	28.4%	15.9%
	AUS - All Ords (A$)	6948	2.6%	3.7%	20.8%	5.6%
	All Ords in NZD	7328	0.4%	2.6%	19.5%	5.0%
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	US - S&P500 (US$)	3141	3.4%	7.3%	13.8%	8.7%
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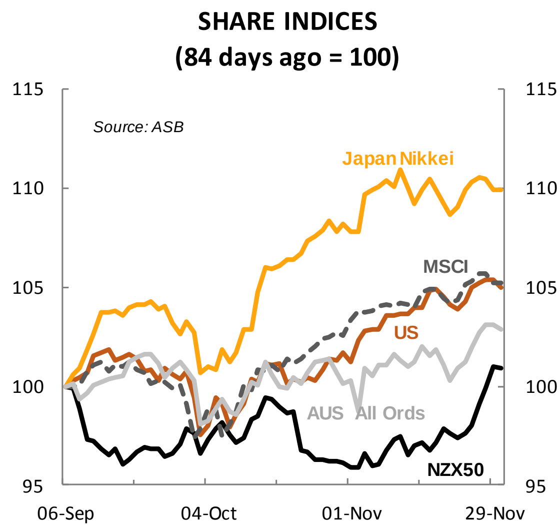
Australasian Equities

Australasian markets recorded strong gains in November. The Australian All Ords index lifted 2.6% and the NZX50 Gross index was up a whopping 5.3% for the month. The NZ index is still just shy of its peak set in September, but the All Ords set a fresh record high on the second-to-last trading day of the month.

In NZ, Metlifecare, Ryman Healthcare and Summerset all posted solid gains of close to 20% during November. Pushplay Holdings and The a2 Milk Company also posted similar large gains over the month. And Fletcher Building recovered nearly 15% in November. Across the Tasman, 18 of Australia's 22 sub-industry sectors posted gains during November. Consumer durables rose the most (up 11.9%), while banks fell the most (down by 5.5%). Shares in Westpac fell after Austrac accused the bank of breaching money laundering laws.



International Equities

Global sharemarkets recorded solid gains over November. Key influences over the month included the US-Chinese trade talks; corporate earnings results; central bank interest rate decisions; and economic data. In addition, there were a number of merger/acquisition announcements in Europe and the US that drove individual stock movements.

The S&P 500 index of US shares gained 3.4% over the month, and is 13.8% higher than a year ago. The Dow Jones Industrial Average gained 3.7% and the NASDAQ gained 4.5%. All three US indices set record highs the day before Thanksgiving, before easing on the last trading day of the month and early December.

Japan's Nikkei share index gained 1.2% over November, and is up 12.5% over the past three months. It has been quite an impressive recovery for Japanese shares in recent months after some heavy losses in late 2018 and May 2019.

The FTSE100 index of UK shares lifted 1.4% in November. The focus remains on the 12 December General Election, where PM Johnson looks to strengthen his power and push through the latest withdrawal agreement with the EU.

ASB Securities has more information on sharemarkets and trading here.

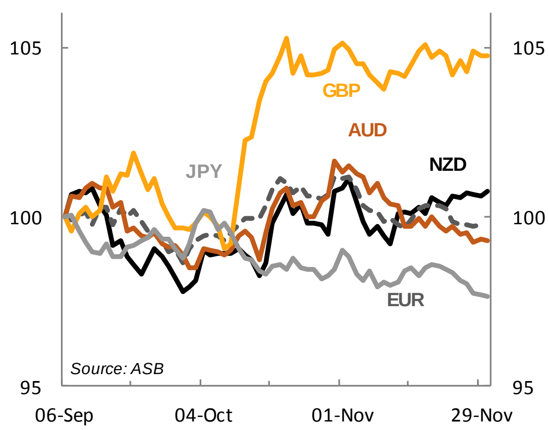
Exchange Rates:

The NZD was little changed against the USD, but up on the other cross rates we monitor over November, lifting 0.7% on a trade-weighted basis.

The RBNZ's decision to hold the OCR at its November meeting was one source of NZD support during the month. FX volatility has also been low, with NZD/USD volatility falling to the lowest level in over 20 years in early December.

Weaker-than-expected Australian data weighed on AUD during the month. That weakness saw NZD/AUD lift back towards 0.9500. EUR weakness saw NZD/EUR gain 1.3% over the month, with the cross rate back above 0.5800.

EXCHANGE RATE INDICES (versus USD, 84 days =100)



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

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