

# Markets Monthly

15 December 2021

## Inflation and interest rates on the rise

The main themes in global financial markets over 2020 and 2021 have been related to the impact of Covid-19 on economic activity, and the policy responses of governments and central banks. Activity has held up and is lifting because the policy decisions of governments and central banks have largely worked.

In turn, over recent months the focus has been very much on some of the inflationary pressures that have built around the world. Related to this, central banks are starting to respond. In the Reserve Bank of New Zealand's case, it has been lifting its Official Cash Rate in October and November. Although the arrival of a new COVID variant, Omicron, weighed on sentiment during November, expectations that central banks will reduce monetary policy support over the year ahead remains high.

Meanwhile, governments continue to run large deficits, supporting economic activity that otherwise remains impacted by the various levels of restriction around the world.

Date		30-Nov-21	Month %	Quarter %	Year %	5-Year %
Cash	NZ Official Cash Rate	0.75	0.25	0.50	0.50	-1.00
	NZ 90-day bank bill	0.81	0.00	0.35	0.56	-1.24
Fixed Interest	NZ 5-year gov't stock	2.21	-0.14	0.85	1.92	-0.27
	NZ 10-year gov't	2.42	-0.16	0.70	1.57	-0.70
	AUS 10-year gov't	1.75	-0.27	0.59	0.85	-0.99
	US 10-year gov't	1.51	-0.07	0.23	0.67	-0.80
Australasian	NZ - NZX50 Capital (NZ\$)	5213	-3.0%	-4.5%	-2.8%	57.8%
	- S&P/NZX50 Gross (NZ\$)	12719	-2.9%	-3.8%	-0.4%	84.8%
Equities	AUS - All Ords (A\$)	7587	-0.7%	-3.0%	12.5%	37.9%
International	JAP - Nikkei (¥)	27822	-3.7%	-1.0%	5.3%	52.0%
	UK - FT100 (£)	7059	-2.5%	-0.8%	12.7%	4.1%
	US - S&P500 (US\$)	4567	-0.8%	1.0%	26.1%	107.7%
	WORLD - MSCI (US\$)	3102	-2.3%	-1.3%	20.1%	81.2%
	- MSCI return in NZD		2.9%	1.7%	23.6%	89.6%
Exchange Rates	NZD/USD	0.6826	-5.0%	-3.0%	-2.8%	-4.5%
	NZD/AUD	0.9551	0.3%	-0.7%	0.4%	-0.1%
	NZD/JPY	77.58	-5.0%	0.4%	6.3%	-3.6%
	NZD/GBP	0.5123	-1.6%	0.4%	-2.7%	-10.5%
	NZD/EUR	0.6041	-1.8%	1.5%	2.9%	-10.1%
	NZ TWI	73.15	-3.4%	-1.7%	-1.2%	-6.8%

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](#).

The management of the pandemic will remain a key challenge over the year ahead. However, the focus is increasingly on how economies will perform as they reopen. Central banks will remain focused on trying to support the economic recovery, while not letting inflation gather more momentum. Expectations of the outlook for inflation, and the paths that central banks will take are having a massive impact on fixed interest markets.

The lift in bond yields took a breather in as Omicron hit the newswires, but the upward pressure remains in place. Despite the movements over recent weeks, long term interest rates have risen significantly over the past year. That has led to declines in the value of bonds within investment portfolios. As the table above shows, the yield lift over the past year has been very strong here in New Zealand, so is having a noticeable impact on many kiwi investors with diversified funds that hold bonds.

Meanwhile, extremely supportive fiscal policy around the world remains a positive influence on the outlook for growth assets, and this is reflected in the strength in global sharemarkets, despite the challenges. Sharemarkets endured some omicron-induced wobbles in November. However, the S&P 500 index of US shares has gone on to set a fresh record high in early December. In contrast, the local sharemarket has struggled this year, and in early December the S&P/NZX 50 share index is down around 4% from the record high set at the start of the year.

## 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. The 3- to 5-year rates are now over 2% above the all-time lows recorded over the past year. The short term rates of less than six months remain closer to 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	2.53	3.17	3.22	3.28	3.50	3.66	3.82	3.96
Low	0.35	0.80	0.75	0.75	0.80	0.90	1.00	1.00
<b>Dec-21</b>	<b>0.70</b>	<b>1.30</b>	<b>1.55</b>	<b>2.00</b>	<b>2.50</b>	<b>3.00</b>	<b>3.05</b>	<b>3.10</b>
2021 increase	0.35	0.50	0.80	1.25	1.70	2.10	2.05	2.10

ASB's term deposit interest rates are [tabled here](#). Inflation has been low until recently, but is now 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, above all but the longer term deposit rates. Related to the inflation outlook, and the strong economic recovery in the wake of the COVID-19 pandemic, the RBNZ lifted the Official Cash Rate in early October, and again in November. More increases are signalled for next year. ASB Economics thinks every meeting over the year ahead is "live" for a rate increase from the RBNZ. Our report on the RBNZ's latest decision and the outlook [is here](#). We also expect to see some more increases in term deposit rates over the years ahead, and our term deposit reports can be [read here](#).

Asset	Instrument	30-Nov-21 Yield (%)	Month	Quarter	Year	5-Year
		Yield Change				
Cash	NZ Official Cash Rate	0.75	0.25	0.50	0.50	-1.00
	NZ 90-day bank bill	0.81	0.00	0.35	0.56	-1.24
	US 90-day bank bill	0.17	0.04	0.05	-0.05	-0.76
Fixed	NZ 5-year gov't stock	2.21	-0.14	0.85	1.92	-0.27
Interest	NZ 10-year gov't	2.42	-0.16	0.70	1.57	-0.70
	NZ 10-year swap	2.70	-0.04	0.74	1.83	-0.56
	AUS 10-year gov't	1.75	-0.27	0.59	0.85	-0.99
	US 10-year gov't	1.51	-0.07	0.23	0.67	-0.80

### Fixed Interest

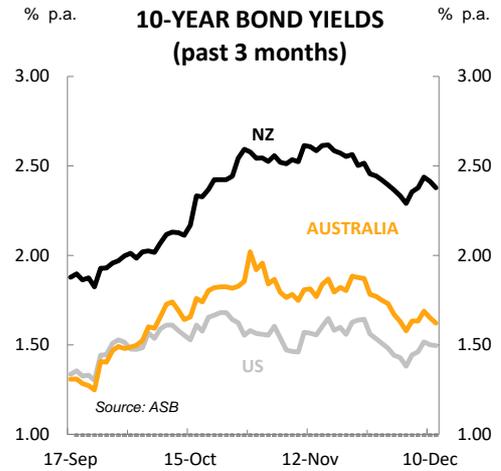
NZ Government bond yields have risen sharply over the past year, but the upward lift has paused over the past month. The pattern is similar in the US and Australia, with long-term yields retreating from recent peaks, but still up significantly on year-ago levels.

The NZ 10-year government bond yield eased 16 basis points over the past month but remains close to 2% higher than the lows reached last year. The five-year yield dipped 14 basis points over the month. Last year the 5-year bond briefly traded with a negative yield to maturity. The circa 2% annual lift in long term yields have caused significant drops in the mark-to-market valuations of bonds within portfolios.

The Australian 10-year government bond yield was up 54 basis points over October (0.54%), but dipped 27 basis points in November, to trade around 85 basis points higher than a year ago. The big development in Australia was the Reserve Bank abandoning its yield target of 0.1% in October. Stepping away from this target paves the way for RBA rate hikes coming much sooner than the RBA has been suggesting during the pandemic.

The US 10-year yield dipped a modest 7 basis points in November, unwinding the lift of the same amount over October. US 10-year yields are up 67 basis points (0.67%) over the year.

One of the consequences of the larger lift in local rates is that New Zealand bonds resume the more normal pattern of trading with a yield advantage vis-à-vis the Australian and US equivalents.



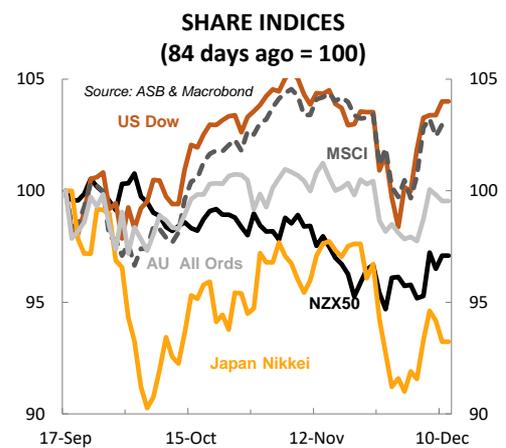
## Growth Assets

Asset	Index	30-Nov-21 Level	Month %	Quarter %	Year %	5-Year %p.a.
Equities	NZ - NZX50 Capital (NZ\$)	5213	-3.0%	-4.5%	-2.8%	9.6%
	- NZX50 Gross (NZ\$)	12719	-2.9%	-3.8%	-0.4%	13.1%
	AUS - All Ords (A\$)	7587	-0.7%	-3.0%	12.5%	6.6%
	All Ords in NZD	7944	-1.0%	-2.3%	12.1%	6.7%
	JAP - Nikkei (¥)	27822	-3.7%	-1.0%	5.3%	8.7%
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### Local and International Equities

**The New Zealand sharemarket** has been out of step with global markets over 2021. While the US sharemarket has pressed upwards to set fresh record highs through the year, the local sharemarket has traded below its peak set back in January, not helped by a 3% dip in November. **The Aussie sharemarket** had been outperforming the NZ market throughout 2021. In contrast with the local sharemarket's decline of 0.4% over the year to 30 November, the Australian All Ords benchmark is up 12.5% over the period, despite some weakness over the past three months.

**US shares** dipped in November, with the S&P500 index of shares slipping 0.8%. But earlier gains meant the index was up 26.1% over the year to 30 November. **Japanese shares** have had a volatile year, but strength earlier on has kept the Nikkei index in positive territory over the year to 30 November, despite the bouts of weakness shown in the chart above. The Nikkei index of shares dipped 3.7% during November but is up 5.3% over the 12-month period.



In sum, **the MSCI index of global shares** was down 2.3% in USD terms for November, and down 1.3% the past three months, but up 20% on a year ago.

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

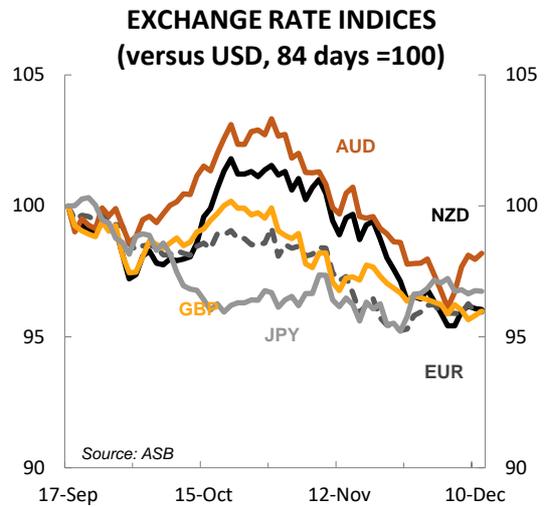
## Exchange Rates

**It's been a mixed time for the NZD recently, with the NZD weakening on most cross rates during November to be down 3.4% on a trade weighted basis for the month.**

The NZD maintains two key supports – key export commodity prices are strong, and the NZD has an interest rate advantage against the major currencies.

However, the global anxieties noted at the start of this report are making the traditional safe-haven currencies (USD, JPY, EUR, and GBP) look more attractive than their procyclical peers (of which NZD is one). The AUD has suffered from the same theme, and the NZD/AUD cross rate is little changed.

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



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