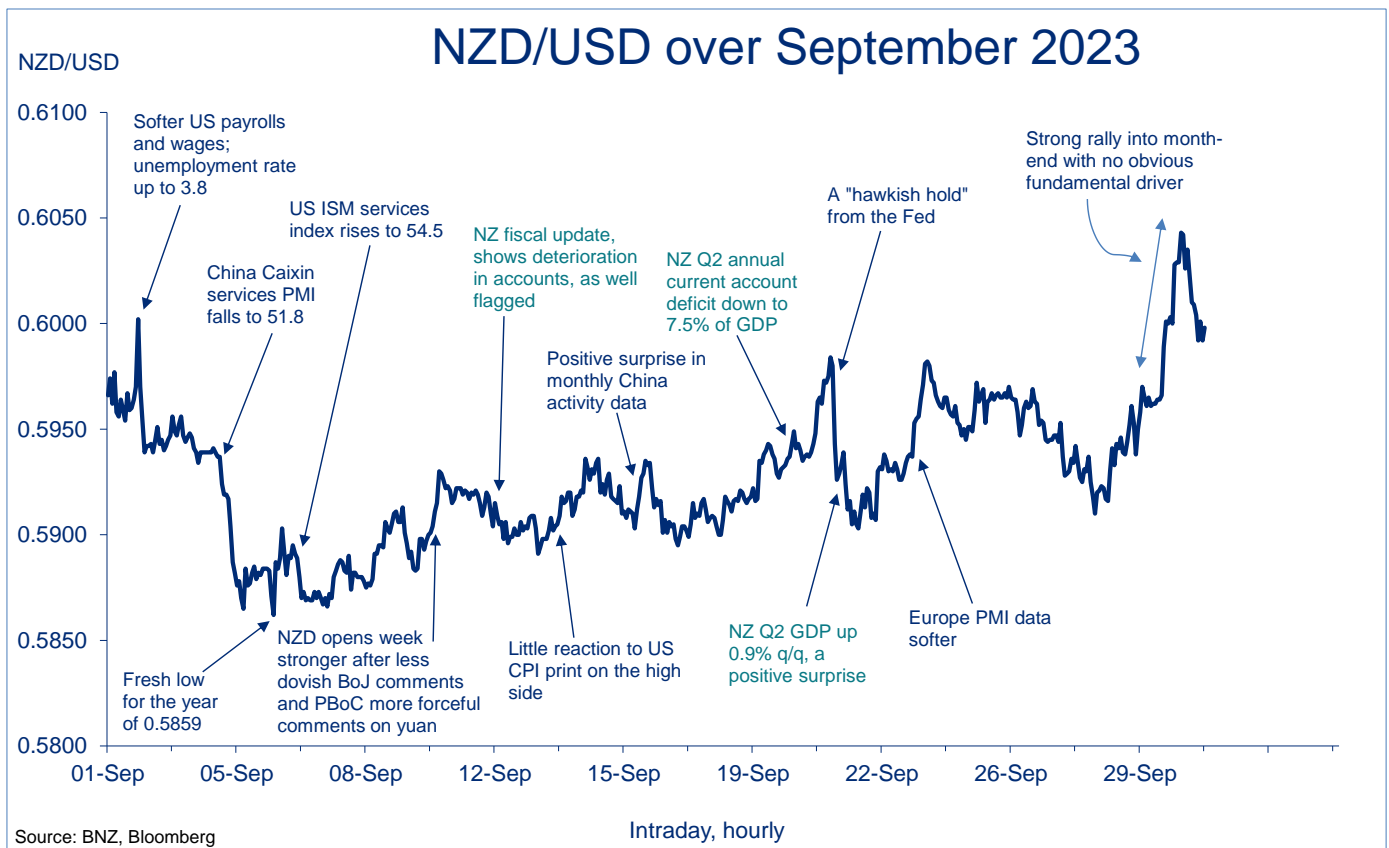


Financial Markets Wrap

2 October 2023

NZD ends September strongly, off a low base

- A late recovery saw the NZD as the best performing major currency in September against a backdrop of solid USD support
- A key theme was higher and steeper yield curves, seeing long rates at their highest level in over a decade
- The heavy influence of the PBoC prevented further yuan weakness, lending some support to the NZD



Quick Outlook		September ranges
NZD/USD	Seasonally, Q4 is the strongest quarter of the year and Q3 is the weakest, providing some hope that the low for the year has been traded. We have a 0.60 end-Q4 target, consistent with a 0.58-0.62 trading range developing, with a more constructive view into 2024 assuming a weaker USD evolves	0.5860 – 0.6050
NZD/AUD	Currently near the top end of its trading range, supported by NZ-AU rate spreads, even though fundamentally macro headwinds look much more troubling for the NZD than AUD. We still target 0.90 sometime during this cycle	0.9155 - 0.9340
NZD/GBP	Recovery from a 7-year low seems fair with now more visibility on the peak policy rate for the UK. A period of consolidation below the 0.50 mark now looks appropriate	0.4670 - 0.4930
NZD/EUR	Recovery from recent 3-year low reflects some rising conviction that the ECB tightening cycle is now completed. Expect some consolidation now around the current level.	0.5460–0.5700
NZD/JPY	BoJ policy stance continues to hinder yen performance and it looks like negative short rates are here to stay until early next year. Cross remains vulnerable to significant downside pressure over the medium-term. Timing remains uncertain.	86.3 – 90.2

The key theme for September was higher and steeper yield curves around the world as the market embraced a likely “higher-for-longer” policy rate stance for developed-market central banks. This view hit risk appetite, driving global equity markets lower. The USD was broadly stronger. Commodity currencies outperformed – with the NZD leading the pack – supported by some stability in the yuan, while European currencies performed worst.

While the end of the tightening cycle for most developed market central banks drew closer, the market lost faith that an easing cycle would closely follow. A backdrop of sticky core inflation, higher oil prices that could keep inflation expectations elevated, some resilience of the US economy and central bank messaging were all factors in this view.

Many global rates rose to levels not seen for more than a decade, with steeper curves and the move driven much more by real rate increases than inflation expectations. The US 10-year rate ended the month up 46bps to 4.57%, after hitting a peak of 4.69%. The 2s10s curve steepened by 29bps to minus -47bps, the steepest in four months. NZ’s 10-year NZGB rose by 44bps to 5.31%. Swap rates were up 28-47bps, with the largest moves at the long end.

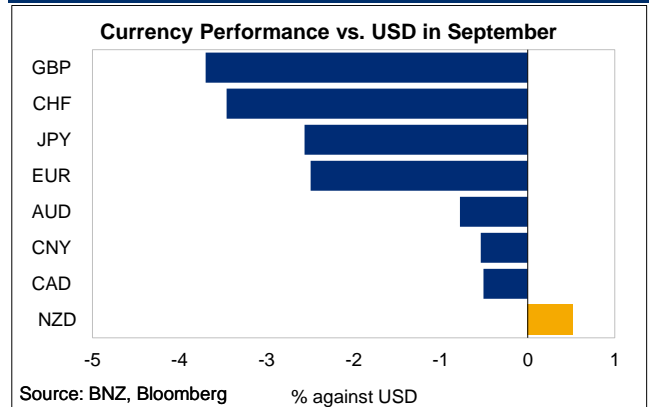
The US CPI report for August was slightly stronger than expected although annual core inflation fell to 4.3%, the lowest rate in nearly two years. Underscoring the resilience of the US economy, the ISM services index unexpectedly rose to 54.5 while the trend for initial jobless claims remained to the downside. The US Federal Reserve left the Fed Funds target range unchanged at 5.25-5.5% but signalled that rates were likely to stay higher for longer. Median projections of FOMC members continued to show one more rate hike this year but the number of rate cuts for next year reduced from four to two.

Higher bond yields, and the higher for longer message, saw a fall in risk appetite, with our index declining from 66% to 52% through the month. Lower risk appetite, and the US economy showing more resilience than others, supported a stronger USD. The DXY index broke up through 106 for the first time this year and closed the month up 2.5%.

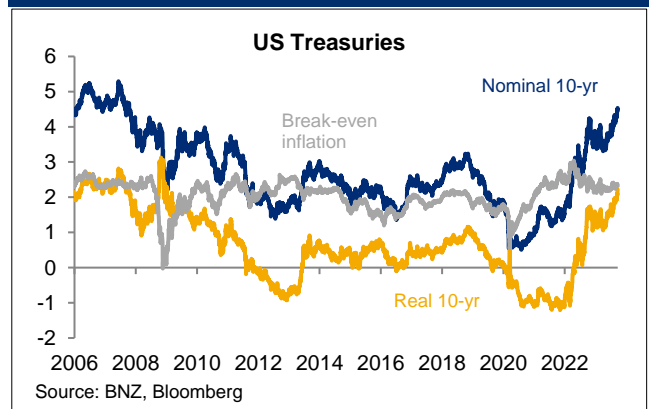
Against that backdrop the NZD was surprisingly resilient, trading in a relatively tight range and closing the month up 0.5% to just shy of 0.60. The high for the month of 0.6049 was the last day of the month, and possibly exaggerated by month-end flows. The low of 0.5859 was reached early in the month, with the currency showing a steady upward drift thereafter.

Less pessimism on China and some stability in the yuan provided NZD support. After the recent run of poor data, China retail sales and industrial production grew faster than expected in August. China trade data were also not as bad as feared, with exports and imports contracting at a slower pace on an annual basis.

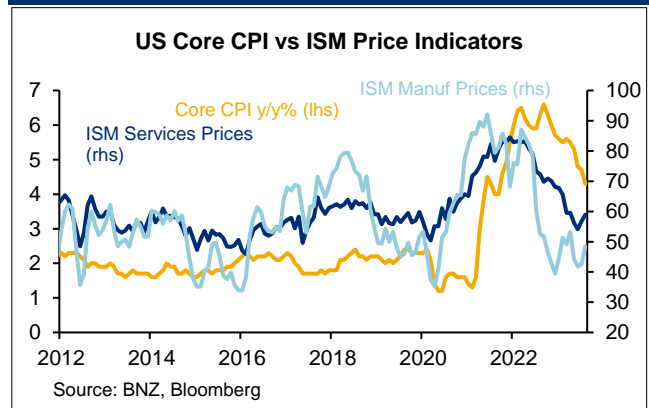
USD broadly stronger in September; NZD outperforms



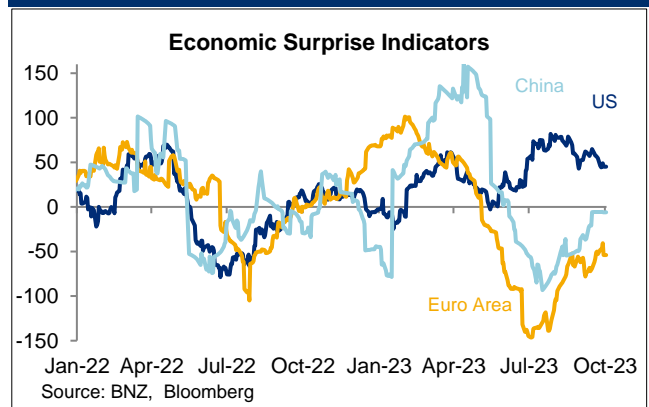
US 10-year rate up to 16-year high driven by real rates



US inflation heading in the right direction



China economic surprise indicator neutralising



The PBoC was active in supporting the yuan through a wide range of measures, including fixing the CNY reference rate at a “strong” level on a daily basis, making it more expensive to short the currency, directing state banks to sell USD/CNY aggressively and cutting foreign exchange reserve requirements. Measures to support the economy also continued on an incremental basis.

Domestically, the NZ dataflow was mixed. The PMI and PSI monthly indicators were consistent with the economy struggling in Q3. NZ Q2 GDP rose by 0.9% q/q and 1.8% y/y in Q2, a stronger bounce-back than expected from two consecutive weak quarters. While at face value, it appeared that the economy was on a stronger footing than many assumed in Q2, it didn’t change the picture of a sluggish underlying economy, particularly when viewed against population growth that exceeded 2%. NZ’s current account deficit narrowed to a smaller than expected 7.5% of GDP in the year to June, with the sluggish economy and revisions to prior data helping.

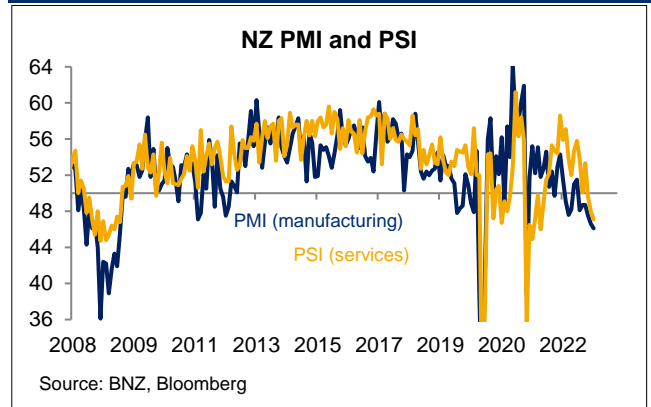
The government’s pre-election economic and fiscal update showed further deterioration in the fiscal accounts, with a shortfall in tax revenue (since the Budget estimates were compiled a few months ago) leading to the budget deficit running some \$3b larger than the government had expected for the June 2023 year, at \$10b for the OBEGAL measure. NZDM increased its borrowing programme by \$2b for the current fiscal year, with borrowing over the four-year projection period lifted by \$9b.

Amidst a mixed performance for commodities, dairy prices stood out, with two consecutive strong GDT dairy auctions – a possible signal that after a large and protracted fall, the downturn was now over. The prior plunge in prices and concerns about dairy production, as we head into El Nino weather conditions, is seeing buyers return to the market. Wholemilk price futures on the SGX-NZX market rose 17% for the month. We earlier noted higher oil prices; Brent crude was 10% higher for the month and traded over USD97 per barrel at its peak. Demand for oil reached a record high and Saudi Arabia continued to enforce production curbs, extending the state of excess demand.

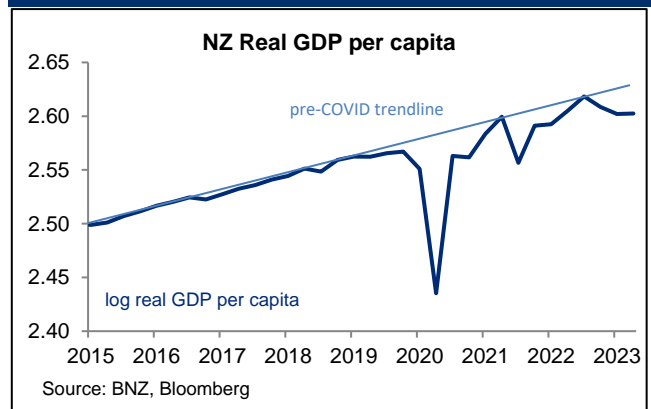
Higher oil prices supported CAD, as well as core CPI inflation that came in much stronger than expected, which kept alive the chance of further tightening by the Bank of Canada. Relevant to the AUD, the RBA kept its policy rate on hold and maintained a bias to tighten further, depending on the data. Added to the Statement was a line about the uncertainty around the outlook for the Chinese economy, which some saw as increasing the hurdle for another hike. The AUD fell by 0.8% for the month and NZD/AUD was 1.3% higher to be back over 0.93.

USD/JPY broke up through 149 for the first time this year. The BoJ remained as dovish as ever, maintaining its ultra-easy policy stance even in the face of higher-than-expected CPI inflation. Governor Ueda said the distance from being

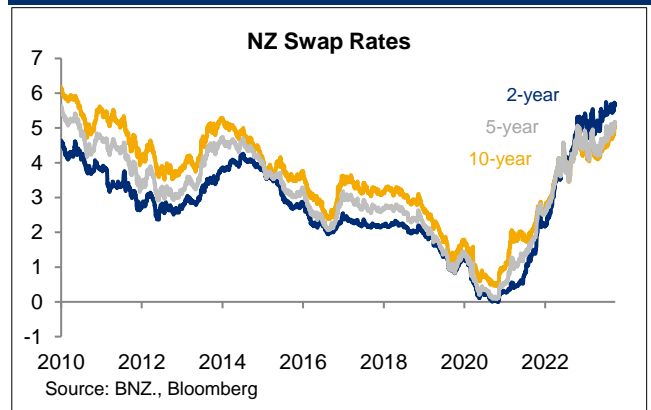
NZ PMI and PSI point to economy contracting in Q3



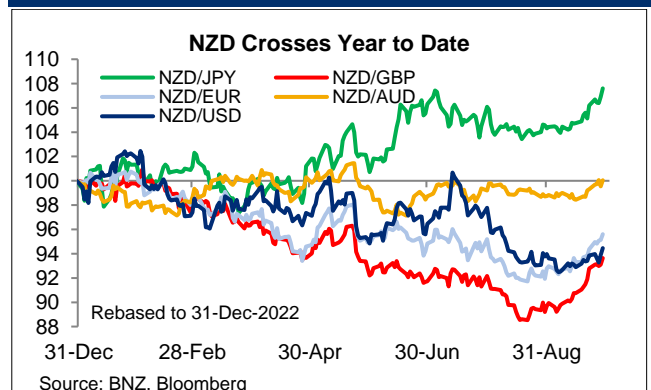
NZ economy running below trend on per capita basis



NZ rates push up to fresh multi year highs



NZD/JPY up YTD; NZD/AUD flat; other NZD crosses lower



able to adjust the negative rate hadn't changed much. There was plenty of verbal intervention through the month to contain the rate of depreciation, including Finance Minister Suzuki who frequently ran the line of watching FX moves "with a high sense of urgency". NZD/JPY was 3.2% higher to 89.6, with a fresh 8-year high just over 90 traded on the last day of the month.

European currencies had a weak month. UK labour market data showed the unemployment rate rising to a near two year high of 4.3% while core CPI inflation for August was much lower than expected at 6.2%. In a 5-4 vote split the BoE left its policy rate at 5.25%, breaking a run of tightening at every meeting since the end of 2021. GBP

was the weakest of the majors and NZD/GBP rose a chunky 4.4% to 0.4915.

The ECB lifted its deposit rate by 25bps to 4%, against expectations that were finely balanced on whether the ECB might hike or pause. But it was a dovish hike and the statement suggested that the tightening cycle was now over. NZD/EUR rose over 3% to 0.5670. Data showed the ECB getting good traction with its tightening, with borrowing by corporates and households running at their weakest growth rates in about eight years.

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Monthly Performance Table							
	end-Sep	end-Aug	Change		end-Sep	end-Aug	Change
Currencies				NZ Rates			
NZD/USD	0.5998	0.5967	0.5%	OCR	5.50	5.50	0.00
NZD/AUD	0.9322	0.9201	1.3%	NZ 90day BB	5.74	5.65	0.09
NZD/EUR	0.5672	0.5502	3.1%	NZ 2yr sw ap	5.72	5.44	0.28
NZD/GBP	0.4915	0.4708	4.4%	NZ 5yr sw ap	5.23	4.83	0.40
NZD/JPY	89.58	86.83	3.2%	NZ 10yr sw ap	5.18	4.71	0.47
NZD/CNY	4.377	4.331	1.1%				
TWI	71.1	69.9	1.7%	NZ Govt (4/25)	5.74	5.45	0.30
AUD/USD	0.6434	0.6485	-0.8%	NZ Govt (5/28)	5.28	4.89	0.39
EUR/USD	1.0573	1.0844	-2.5%	NZ Govt (4/33)	5.31	4.87	0.44
GBP/USD	1.2204	1.2673	-3.7%	NZ Govt (5/41)	5.53	5.06	0.47
USD/JPY	149.37	145.54	2.6%				
USD/CNY	7.30	7.26	0.5%	Global 10 year bond rates			
USD/CAD	1.3578	1.3509	0.5%	US	4.57	4.11	0.46
USD DXY	106.17	103.62	2.5%	Canada	4.02	3.56	0.46
Asia dollar index	90.43	91.30	-0.9%	UK	4.44	4.36	0.08
				France	3.40	2.98	0.42
Equity Markets				Germany	2.84	2.46	0.38
MSCI AC Wrlld, loc.	1,806	1,871	-3.5%	Italy	4.78	4.12	0.66
MSCI World, loc.	10,290	10,681	-3.7%	Spain	3.93	3.48	0.45
MSCI EM, USD	2,447	2,511	-2.6%	Portugal	3.58	3.17	0.41
US S&P 500	4,288	4,508	-4.9%	Ireland	3.24	2.84	0.40
Euro STOXX 600	450.2	458.2	-1.7%	Japan	0.76	0.65	0.11
Germany DAX	15,387	15,947	-3.5%	Australia	4.49	4.03	0.46
France CAC 40	7,135	7,317	-2.5%				
UK FTSE 100	7,608	7,439	2.3%	Commodities (USD)			
Aust S&P/ASX 200	7,049	7,305	-3.5%	WTI Crude	90.79	83.63	8.6%
Japan Topix	2,323	2,332	-0.4%	Brent Crude	95.31	86.86	9.7%
China CSI 300	3,690	3,765	-2.0%	R/B CRB Index	284.5	281.9	0.9%
NZX50	11,296	11,554	-2.2%	Gold spot	1,849	1,940	-4.7%
Volatility: VIX	17.52	13.57	29.1%	Silver spot	22.18	24.44	-9.3%
				Copper	373.8	377.3	-0.9%
3-mth Bill Futures				Iron Ore	119.74	113.51	5.5%
NZD Mar-24	94.02	94.27	-0.25	Thermal coal	160.10	156.00	2.6%
AUD Mar-24	95.55	95.73	-0.18	Corn	476.8	478.3	-0.3%
USD Mar-24	94.63	94.80	-0.17	Wheat	541.5	602.0	-10.0%
EUR Mar-24	96.05	96.23	-0.18	SGX-NZX Dairy WMP	2,965	2,525	17.4%
GBP Mar-24	94.62	94.29	0.34	SGX-NZX Milk Price '24	7.54	6.91	9.1%
CAD Mar-24	94.33	94.46	-0.13				

Source: BNZ, Bloomberg

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