RESEARCH

Markets Today

14 November 2022

Events Round-Up

NZ: BNZ Manufacturing PMI, Oct: 49.3 vs. 51.7 prev.

NZ: Food prices (m/m%), Oct: 0.8 vs. 0.4 prev.

UK: GDP (m/m%), Q3: -0.2 vs. -0.5 exp.

UK: Uni. Mich. consumer sentiment, Nov: 54.7 vs. 59.5 exp.

US: Uni Mich. 5-10y infl. expectations, Nov: 3 vs. 2.9 exp.

Good Morning

The downside surprise to US CPI on Thursday night continues to reverberate around markets. US equities continued to power higher, the S&P500 up 0.9% on Friday, the USD slumped further, and commodities rallied strongly. The NZD broke through 0.61, up more than 3% on the week and now at its highest level in two months. The risk-on vibes were reinforced by China incrementally loosening its covid policy. US rates consolidated after their huge falls following the CPI data. The significant repricing of Fed rate expectations has spilled over to the NZ market, with the market now pricing the November RBNZ meeting as a 50-50 bet between a 75bps hike and a 50bps move.

Investors have been waiting for the turn in US inflation for several months now, only to have been disappointed by a relentless string of upside surprises. The October US CPI data provided the first tangible sign that core inflation has likely peaked. While central banks will be cautious about reading too much into a single data point – something Boston Fed President Collins noted on Friday night – several leading indicators, including pricing intentions from the ISM surveys, suggest annual core inflation should continue to moderate from here, although the Fed's 2% target is still a long way off. If this is the start of the long-awaited normalisation in inflation, the market figures the Fed won't need to lift interest rates as far, implying less chance of a deep recession.

Meanwhile, China has started to gradually loosen Covid restrictions, fuelling market speculation around a future pivot away from the zero-Covid policy. New guidance released by the Chinese authorities on Friday confirmed that international visitors and close contacts would now need to spend 5 days in a quarantine facility and 3 days at home (down from the current 10-day requirement) while airlines would no longer be penalised for bringing Covid-positive passengers to the country, as foreshadowed by media reports last week. Bloomberg reported that cities were scaling back mass testing and releasing close contacts from quarantine facilities, in response to new guidance. Covid cases continue to rise sharply in the country, including over 2,500 daily new cases in Guangzhou, but the authorities have so far resisted putting the entire city into lockdown, instead imposing restrictions on high-risk areas, another sign that China's approach to zero-Covid is evolving. Analysts don't expect any wholesale changes to the zero Covid policy until after winter, but markets see enough straws in the wind to speculate China could be lining up a pivot to living with Covid from March/April 2023. An eventual shift away from the Covid-zero policy would remove a major headwind to global growth.

Separately, China also series of measures aimed at helping the beleaguered property industry, including reducing deposit requirements for mortgages and easing restrictions on bank lending to developers. Bloomberg reported that an index of Chinese developers' stocks jumped by a record 18% Friday. A turnaround in the property sector would also be supportive of global growth.

US equities continued to roar higher on Friday, with the S&P500 up another 0.9%, bringing its gain on the week to almost 6%, while the interest rate-sensitive NASDAQ was almost 2% higher, leaving it up 8.1% on the week. In addition to the market pricing less risk of global recession, the sharp rebound in equities has likely been exacerbated by market positioning, with BofA's Fund Manager Survey having previously revealed investors were sitting on large cash balances amidst broader caution towards risk assets. Commodities were also significantly higher, helped by the improving sentiment towards China. Copper, often seen as a bellwether of the global economy, was up 2.7% while aluminium was 5.9% higher. Oil prices were 2.5% higher, with Brent crude back up to around $96 per barrel.

The US cash bond market was closed on Friday, but the implied interest rates on Treasury futures were little changed, consolidating after their big falls the previous night. The market is now pricing a 50bps Fed hike next month and around 50bps more tightening in 2023. Boston Fed President Collins, seen as one of the more dovish members of the committee, said she thought the "the risk of overtightening has increased" while acknowledging that more hikes would still be needed.

In contrast, European bond rates reversed most of their falls after the US CPI release, the German 10-year rate increasing 15bps on Friday, to 2.15%, helped by some hawkish comments from Austrian central bank Governor

Holzmann, who noted his concern that core inflation in the region was still accelerating.

The USD was significantly weaker again on Friday, extending its big falls seen after the US CPI data. The BBDXY index was down 1.3%, bringing its cumulative fall over the past six trading sessions to a chunky 5.1%. The USD has been very 'expensive' for some now, but the market has, until now, lacked a genuine catalyst for a reversal. However, with markets growing more confident the Fed is nearing the end of its tightening cycle, risk appetite rebounding sharply, and tentative signs of changes afoot with China's zero-Covid policy, conviction is now growing that the USD has peaked for the cycle.

The Swiss franc and JPY were among the currencies leading the charge on Friday, appreciating by 2.4% and 1.5% respectively. The pullback in US bond yields appears to have bought the BoJ (and Ministry of Finance) some breathing space, as US-Japan interest rate differentials narrow. USD/JPY fell below 140 for the first time since early September, eventually ending the week at 138.80. The EUR was 1.4% higher, closing at its highest level since early July, just below 1.0350, while the CNY increased over 1%, with USD/CNY falling back below the 7.10 mark. The NZD was around 1.5% stronger on Friday, helped by the tailwinds of firmer risk appetite, a stronger CNY and higher commodity prices. On the week, the NZD was up over 3%, ending at a two-month high of around 0.6120.

In the UK, the Bank of England confirmed it will start the process of selling down the £19b long-end gilts (UK government bonds) it purchased just six weeks ago to prevent the implosion of the pension industry. The pace at which the BoE sells down its 'emergency' holdings will be based on demand, rather than programmatic, so as not to cause a repeat of the big long-end gilt sell-off seen in September and October. The unwind of these emergency purchases, which are scheduled to start from later this month, will run alongside the BoE's existing 'quantitative tightening' which entails it selling around £40b of its QE gilt holdings in the secondary market in the coming year.

Economic data wasn't market moving on Friday but, for the record, the University of Michigan consumer confidence index slumped back to 54.7, back near its recent all-time lows. 5-10-year inflation expectations from the University of Michigan survey nudged higher to 3%, back near the upper-end of the range since the GFC. UK GDP contracted 0.2% in Q2, not as bad as feared, but expected to be the start of what most forecasters think will be a long, drawn-out recession.

In domestic economic data, NZ food prices were up 0.8% in the month of October, surprising us to the upside and lifting the annual rate to 10.1%, a 14 year high. The PMI fell back into contraction for the first time in 2022, with falling new orders and elevated inventories pointing to further weakness in manufacturing activity ahead.

NZ rates experienced big falls on Friday, following the significant repricing of Fed expectations after the US CPI release the previous night. The NZ 2-year swap rate fell 22bps, to 4.94%, with the market figuring that the RBNZ likely has less tightening work to do if we are indeed past the peak in global inflation. The market is now split almost 50-50 between a 50bps hike and a 75bps move. Likewise, the market is pricing a peak in the OCR just above 5%, having been as high as 5.40% earlier in the week. The 10-year NZ bond yield was 19bps lower, significantly outpacing the last 6bps fall in the Australian 10-year rate, helped by lingering post-WGBI demand for NZGBs.

The other big news in the domestic rates market was the government's announcement that Kāinga Ora's funding programme will be folded into NZDM's government bond programme going forward. Kāinga Ora, through its subsidiary Housing New Zealand Limited (HNZL), has been issuing bonds in capital markets since 2018 and now has $7.6b of nominal bonds outstanding, making it the third largest high-grade issuer in the domestic bond market outside the government. Spreads on HNZL bonds collapsed by 30-45bps, reflecting both the complete stop to bond supply (also reflected in LGFA spreads, which were 5-7bps tighter) and the market's perception that the change effectively confirms HNZL as government risk. With NZDM taking on HNZL's borrowing duties, it would imply the government bond programme, currently set at $25b for this fiscal year, will be increased by $2-3b per year, all else equal. On our estimates, this would likely raise the cost of borrowing for the government by 3-5bps, all else equal.

The BNZ PSI index, which was sitting at a relatively healthy 55.8 in September, is released this morning. It's a quieter week for economic data ahead with Aussie employment and wage data and US retail sales among the highlights. There is a bevy of Fed speakers out, including Williams, Brainard, Waller and Bullard, and the market will be focused on how they have interpreted the big downside surprise to US inflation and any clues on the likely path of the policy rate. In the UK, the Chancellor will unveil the Autumn Statement on Thursday night, likely to include £50-60bn in Budget cuts as Rishi Sunak's government goes into damage control to calm markets and restore fiscal credibility.

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Coming Up

		Period	Cons.	Prev.	NZT
NZ	Performance Services Index	Oct		55.8	10:30
EC	Industrial Production (m/m%)	Sep	0.1	1.5	23:00

Source: Bloomberg, BNZ

Foreign Exchange

Indicative overnight ranges (*)

	Last	% Day	Low	High
NZD	0.6119	+1.5	0.6015	0.6130
AUD	0.6707	+1.3	0.6629	0.6717
EUR	1.0355	+1.4	1.0208	1.0364
GBP	1.1835	+1.0	1.1693	1.1855
JPY	138.80	-1.5	138.47	141.71
CAD	1.3254	-0.4		
NZD/AUD	0.9123	+0.1		
NZD/EUR	0.5909	+0.1		
NZD/GBP	0.5170	+0.3		
NZD/JPY	84.92	-0.2		
NZD/CAD	0.8109	+1.0		
NZ TWI	71.17	+0.2		

Other FX

	Last	% Day
CHF	0.9417	-2.3
SEK	10.373	-2.0
NOK	9.928	-1.5
HKD	7.836	-0.1
CNY	7.097	-1.2
SGD	1.372	-0.8
IDR	15,495	-1.3
THB	36.00	-0.5
KRW	1,319	-4.3
TWD	31.20	-1.9
PHP	57.27	-1.6

Equities

Major Indices

	Last	% Day	% Year
S&P 500	3,993	+0.9	-14.1
Dow	33,748	+0.1	-6.1
Nasdaq	11,323	+1.9	-27.9
Stoxx 50	3,869	+0.6	-11.2
FTSE	7,318	-0.8	-0.9
DAX	14,225	+0.6	-11.6
CAC 40	6,595	+0.6	-6.6
Nikkei	28,264	+3.0	-4.5
Shanghai	3,087	+1.7	-12.8
ASX 200	7,158	+2.8	-3.8
NZX 50	11,312	+2.0	-12.4

Commodities**

Price

	Last	Net Day
Oil (Brent)	95.78	+2.3
Oil (WTI)	88.96	+2.8
Gold	1769.4	+1.2
HRC steel	662.0	+0.6
CRB	285.8	+1.3
Wheat Chic.	835.3	+1.1
Sugar	19.64	+0.9
Cotton	88.20	+1.9
Coffee	168.1	-0.2
WM powder	3350	+1.5

Australian Futures

	Last	Net Day
3 year bond	96.77	-0.09
10 year bond	96.32	-0.11

Interest Rates

	Rates		Swap Yields	
	Cash	3Mth	2 Yr	10 Yr
USD	4.00	4.65	4.71	3.82
AUD	2.85	3.03	3.80	4.41
NZD	3.50	4.13	4.94	4.53
EUR	1.50	1.80	2.91	2.89
GBP	3.00	3.47	4.28	3.53
JPY	-0.07	-0.03	0.14	0.57
CAD	3.75	4.63	4.29	3.65

Benchmark 10 Yr Bonds

	Last	Net Day
USD	3.81	0.00
AUD	3.65	-0.07
NZD	4.20	-0.19
GER	2.16	0.15
GBP	3.36	0.07
JPY	0.24	-0.01
CAD	3.15	0.00

NZ Government Bonds

	Last	
NZGB 0 1/2 05/15/24	4.30	-0.19
NZGB 4 1/2 04/15/27	4.21	-0.20
NZGB 3 04/20/29	4.17	-0.20
NZGB 1 1/2 05/15/31	4.17	-0.20
NZGB 2 05/15/32	4.20	-0.19
NZGB 1 3/4 05/15/41	4.60	-0.15
NZGB 2 3/4 05/15/51	4.57	-0.13

NZ Swap Yields

	Last	
1 year	4.96	-0.18
2 year	4.94	-0.22
5 year	4.58	-0.24
7 year	4.53	-0.22
10 year	4.53	-0.19
15 year	4.57	-0.19

* These are indicative ranges from 5pm NZT; please confirm rates with your BNZ dealer

** All near futures contracts, except CRB. Metals prices are CME.

Rates are as of: New York close

Source: Bloomberg

NZD exchange rates

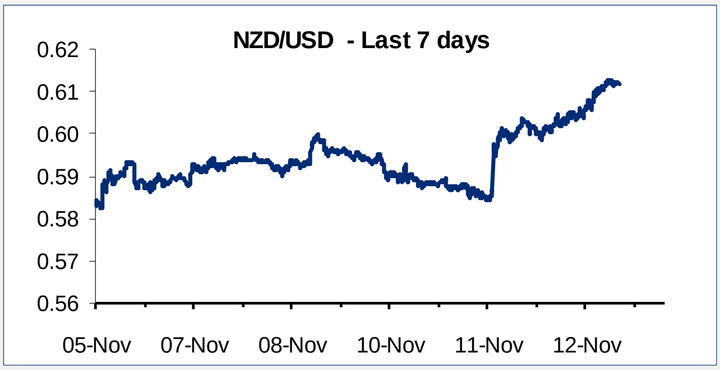
12/11/2022	NY close	Prev. NY close
USD	0.6119	0.6025
GBP	0.5170	0.5143
AUD	0.9123	0.9103
EUR	0.5909	0.5902
JPY	84.92	84.94
CAD	0.8109	0.8028
CHF	0.5748	0.5807
DKK	4.3868	4.3904
FJD	1.3668	1.3634
HKD	4.7833	4.7262
INR	49.33	49.29
NOK	6.0599	6.0738
PKR	135.31	133.56
PHP	34.95	35.06
PGK	2.1448	2.1155
SEK	6.3316	6.3776
SGD	0.8373	0.8329
CNY	4.3322	4.3299
THB	21.94	22.22
TOP	1.4458	1.4270
VUV	73.89	73.66
WST	1.6930	1.6762
XPF	72.96	71.95
ZAR	10.5231	10.4611

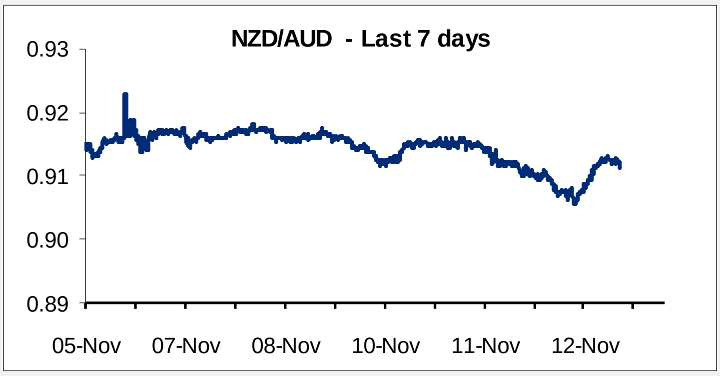
NZD/USD Forward Points

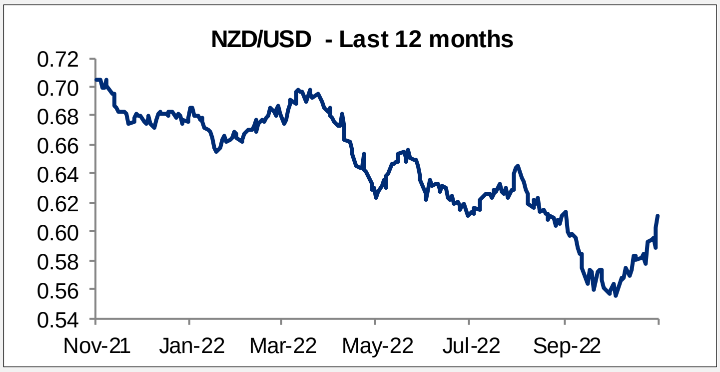
	BNZ buys NZD	BNZ sells NZD
1 Month	1.89	2.48
3 Months	9.92	10.78
6 Months	11.74	17.73
9 Months	13.55	17.59
1 Year	10.60	16.55

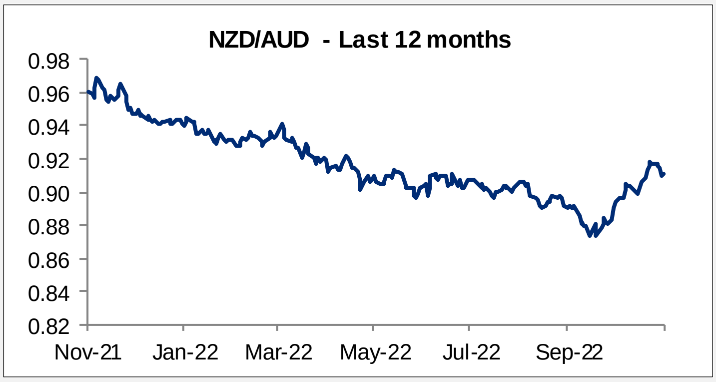
NZD/AUD Forward points

	BNZ buys NZD	BNZ Sells NZD
1 Month	-5.17	-3.89
3 Months	-18.91	-16.96
6 Months	-46.88	-36.67
9 Months	-69.67	-60.87
1 Year	-93.33	-80.47









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