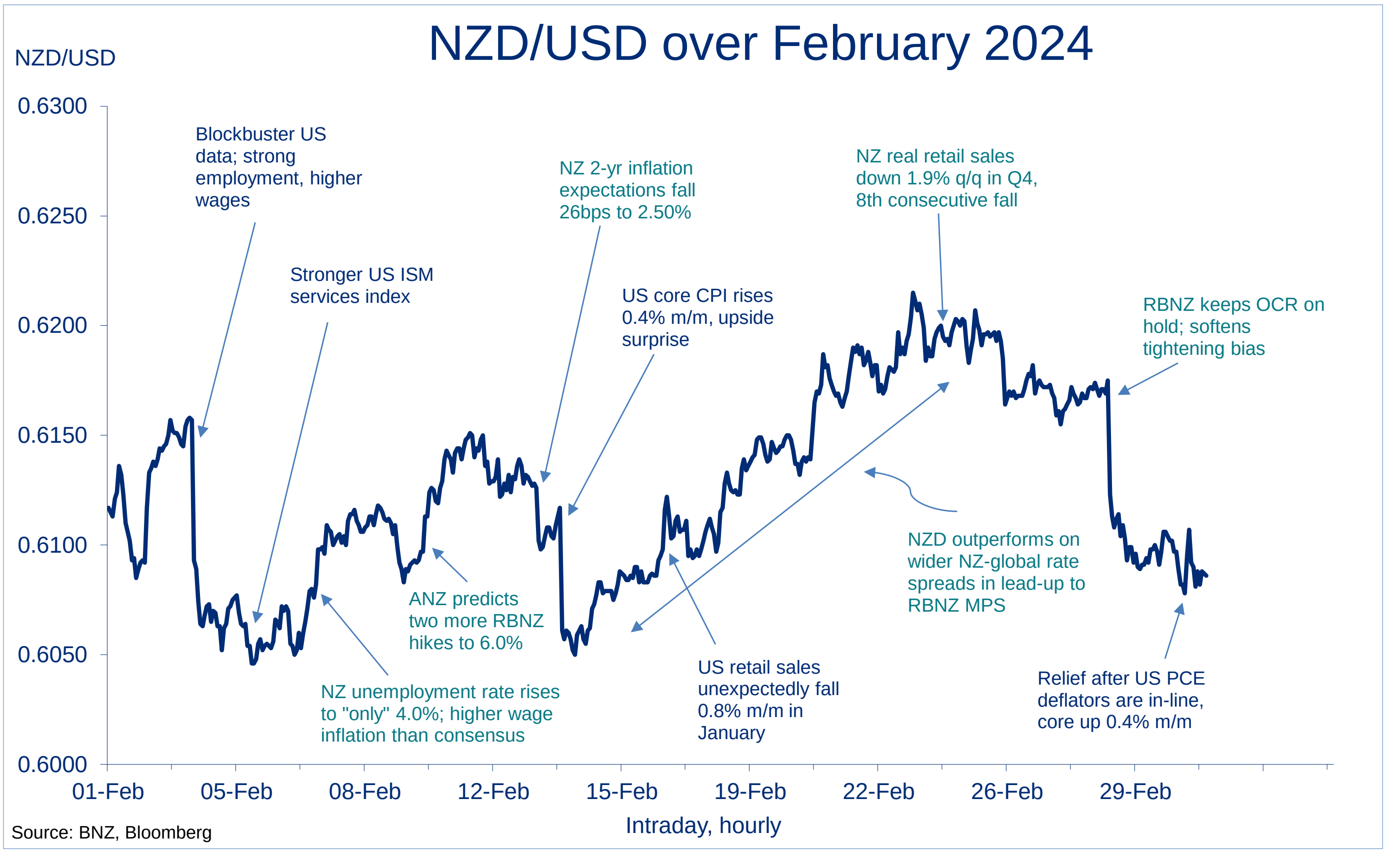
Research

Financial Markets Wrap

1 March 2024

NZD flat in February

- **Timing of policy easing pushed out around the world; Fed speakers united and data non-compliant with an early easing**
- **Global rates push higher and many equity markets reach record highs; Currency markets well-contained**
- **NZD/USD trades less than a 2-cents range, closes month modestly weaker; JPY underperforms**



Source: BNZ, Bloomberg

	Quick Outlook	February ranges
NZD/USD	We see the NZD contained within 0.60-0.64 until the next downward leg in the USD commences, which will require a dovish pivot from the Fed. Despite a number of ongoing headwinds, we have a constructive outlook, but reliant on the (weaker) USD leg doing most of the work.	0.6040 – 0.6215
NZD/AUD	Still range-bound but we see skewed risks to the downside, based on NZ’s poor economic performance relative to Australia ultimately triggering a weaker cross, as rates converge. With RBNZ reluctant to cut rates, this could well take a few quarters to play out.	0.9295 - 0.9460
NZD/GBP	Both UK and NZ economic outlooks are sluggish and the market sees similar scope for rate cuts in 2024. We don’t have a strong directional bias and see some consolidation in the cross in the high 0.40s.	0.4795 - 0.4905
NZD/EUR	Both euro area and NZ economic outlooks are sluggish. We don’t have a strong directional bias and see some consolidation in the cross near current levels.	0.5605 – 0.5730
NZD/JPY	BoJ policy stance continues to hinder yen performance, but we could be within months of a hawkish pivot, against the grain of other central banks. Cross remains vulnerable to significant downside pressure over the medium-term. Timing remains uncertain.	89.3 – 93.4

The key theme for February was the market paring expectations for policy easing this year, with economic data not generally compliant with an early start to the easing cycle for the major central banks. Global rates increased but this didn't perturb equity markets, which mostly showed strong gains, the NZX an exception as the earnings season highlighted the challenging economic conditions for profitability. Currency movements were well contained, with the range for NZD/USD less than 2 cents. JPY underperformed, given the backdrop of higher global rates and less conviction on an immediate hawkish pivot from the BoJ.

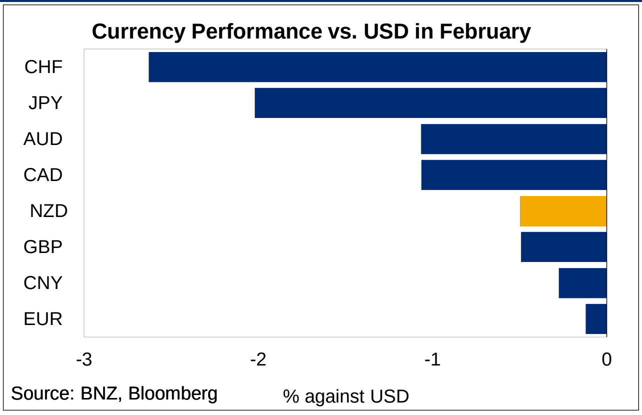
The month kicked off with the Fed's pushback against an early start to the easing cycle at its end-January meeting fresh in the minds of investors. While the Fed officially removed any remnants of its tightening bias, the committee was looking for greater confidence that inflation was moving sustainably toward 2% before cutting rates. Chair Powell pushed back on the likelihood of cutting rates as soon as the March meeting. Through the month, a plethora of FOMC members maintained a united front that supported Powell's view that the central bank was in no rush to ease monetary policy.

Supporting the Fed's view, US labour market data for January were significantly stronger than expected. Nonfarm payrolls increased 353k, close to double the consensus estimate, and with upward revisions to prior data. The unemployment rate was unchanged at 3.7%. Average hourly earnings increased 0.6% m/m, double the median economist forecast. A further blow to any chance of an early easing was provided by stronger than expected CPI and PPI data. The CPI ex food and energy rose 0.4% m/m, leaving the annual increase of 3.9% y/y unchanged from the prior month. The ISM services index rose by 2.9pts to 53.4, with higher new orders, a big jump in employment and, more worryingly, a 7.3pt lift in the prices paid index to 64.0. On the other side of the ledger, US retail sales for January were much weaker than expected, with falls broadly based.

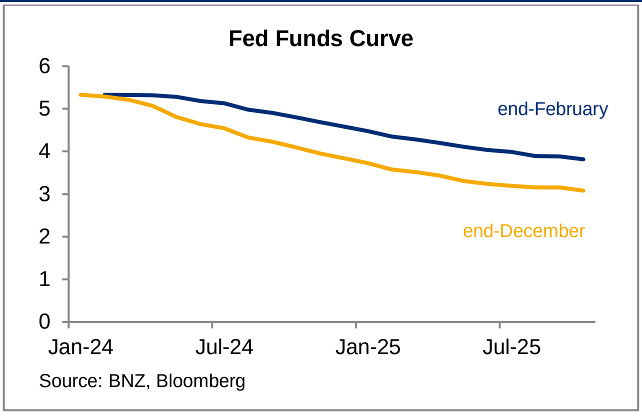
ECB speakers also offered some pushback to an early rate cut, with some lingering concern about still high wage inflation that could cause CPI inflation to hold up higher for longer. The first revision to euro area Q4 GDP was unchanged, confirming that the economy had stagnated at the end of last year, but had narrowly avoided falling into recession. There were signs of green shoots in the region, with the services PMI rising to a seven-month high of 50.0, although the recession in Germany remains a notable drag for the region. Ongoing falls in wholesale gas prices provided a further boost to the region's terms of trade.

The market pared rate cut expectations across major markets and this drove higher rates across the curve. US Treasury yields traded at fresh highs for the year. The 10-year Treasury found some support just under 4.35% and for the month it rose 34bps to 4.25%.

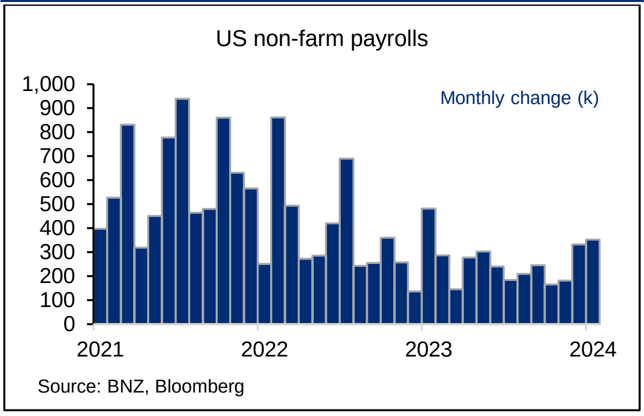
Small net currency movements, JPY and CHF underperform



Market continues to push out timing of easier Fed policy



US employment growth remains resliient



Higher rates were no barrier to global equity markets continuing their strong run, with record highs set across various regions including the US, Europe and Japan, the latter seeing the Nikkei 225 index break above the December 1989 high, something that has been long awaited. The NZX was an exception, with the NZX50 index down over 1% as the earnings season highlighted the challenging domestic economic environment.

On that note, NZ's improving trade balance, driven by a slump in imports, was testament to the recessionary conditions currently facing the economy. Ditto plunging retail sales, which fell 4% y/y in Q4 in real terms or nearly 7% on a per capita basis. NZ labour market data continued to show an easing in pressures. The unemployment rate rose to a 2½ year high of 4.0%. On a more positive note, the PMI and PSI monthly indicators both lifted, even if remaining below average levels.

NZ rates were driven higher by global forces and increased further after ANZ Bank abandoned its call that the RBNZ would be easing in August and predicted two further rate hikes over the next two meetings. That view proved wrong, after the RBNZ left the OCR unchanged at 5.5% and softened its tightening bias, with the MPC noting risks to the outlook for inflation were more balanced than at the time of the November Statement. The MPC was confident that monetary policy was restricting demand and inflation would continue to fall, while agreeing that interest rates need to remain at a restrictive level for a sustained period. The 2-year swap rate traded as high as 5.28% before closing the month up “only” 20bps at 4.98%. There was some modest curve flattening, with the 10-year rate up 15bps to 4.54%. NZGB yields were up 9-19bps across the curve, with a flattening bias. NZDM successfully issued $4b of a new 30-year bond, which met strong demand of $19b for the syndicated issue, suggesting strong appetite for NZ debt with yields above 5%.

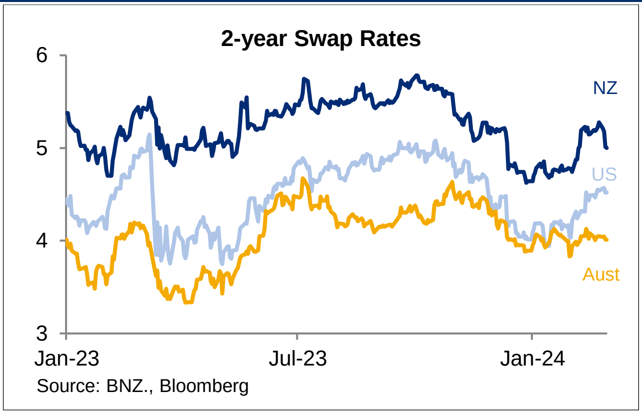
Net currency movements for the month were modest. The NZD traded a less than 2-cents range. The low for the month of 0.6038 was on the 6th, following the blockbuster US employment report and backed up by the stronger US ISM services data. The high of 0.6218 was reached on the 22nd, which followed a period of NZD outperformance as NZ-global rate spreads widened on nerves that the RBNZ could hike at the end of the month. The NZD ended the month down ½% at 0.6087.

JPY was the weakest of the major currencies, driven by the higher global rates backdrop and not helped by domestic factors. Japan Q4 GDP data showed a surprising 0.1% q/q contraction following a 0.8% contraction in the prior quarter. Domestic demand components drove the weaker result and raised a question mark over the timing of the BoJ’s abandonment of its negative short-term policy rate. Earlier in the month BoJ Deputy Governor Uchida said it’s hard to imagine the central bank will be raising its policy rate continuously and rapidly, even after the negative interest rate is ended. At the end of the month, BoJ board member Takata said the Bank needed to consider flexible and nimble steps including an exit from the yield curve control framework and ending negative rates. USD/JPY rose 2% for the month and NZD/JPY rose 1½% to 91.25 after trading at a fresh nine-year high of 93.45.

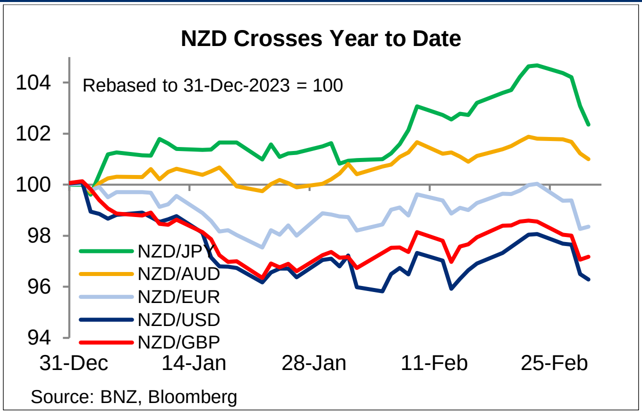
NZD/AUD traded at a fresh nine-month high near 0.9460, driven by wider NZ-Australia rate spreads, before easing back after the less hawkish RBNZ update. The cross ended the month up ½% at 0.9365. Early in the month, the RBA kept policy unchanged and further softened the mild tightening bias with “The Board expects that it will be some time yet before inflation is sustainably in the target range…a further increase in interest rates cannot be ruled out.” Australia’s labour market report was weaker than expected, with the unemployment rate rising two-tenths to 4.1%, its highest level in two years.

NZ retail sector in big trouble

NZ, US 2-year swap rates push higher this year



NZD up vs AUD, JPY YTD, down versus the others



USD/CNY was remarkably stable through the month, but this reflected the heavy hand of the PBoC to keep it that way. In the face of significant macro headwinds caused by the slump in the property market, the government continued with some incremental policy measures to support growth. Chinese banks unexpectedly cut their 5-year loan prime rate by 25bps to 3.95%, the largest move in five years, while the 1-year rate was left unchanged at 3.45%. The 5-year rate is the important one for mortgages and, while the move is designed to help support the housing market, there has been little sign of traction from the previous mortgage cuts of nearly 200bps. The CPI fell 0.8% y/y, the most deflationary environment since 2009.

NZD/EUR and NZD/GBP showed small net movements for the month, with the crosses weaker post the RBNZ update, wiping out earlier gains. Like the euro area, in the UK there were economic green shoots, with plunging inflation helping support real incomes. The PMI services index was steady on 54.3, the fourth consecutive month above 50 and consistent with modest GDP growth. Core retail sales rebounded 3.2% on the month following a slump in December. The data helped to dispel some of the gloom around the economy, which was confirmed to be in a technical recession in 2H23. Other forward-looking indicators suggested the UK economy has started the year on a firmer footing. The Bank of England left its policy rate at 5.25% in a 6-3 decision, with the MPC remaining split. Remarkably, two MPC members continued to vote for a 25bps hike, while one member continued to prefer a 25bps cut. Like the Fed, the BoE removed reference to any tightening bias in the official statement and ended with "…the Committee will keep under review for how long Bank Rate should be maintained at its current level".

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Monthly Performance Table

Currencies	end-Feb	end-Jan	Change
NZD/USD	0.6087	0.6117	-0.5%
NZD/AUD	0.9367	0.9313	0.6%
NZD/EUR	0.5633	0.5654	-0.4%
NZD/GBP	0.4821	0.4821	0.0%
NZD/JPY	91.27	89.85	1.6%
NZD/CNY	4.376	4.385	-0.2%
TWI	71.5	71.4	0.2%
AUD/USD	0.6498	0.6568	-1.1%
EUR/USD	1.0805	1.0818	-0.1%
GBP/USD	1.2625	1.2687	-0.5%
USD/JPY	149.99	146.96	2.1%
USD/CNY	7.19	7.17	0.3%
USD/CAD	1.3580	1.3435	1.1%
USD DXY	104.16	103.27	0.9%
Asia dollar index	91.56	91.82	-0.3%

Equity Markets	end-Feb	end-Jan	Change
MSCI AC Wrld, loc.	2,096	2,002	4.7%
MSCI World, loc.	12,054	11,519	4.6%
MSCI EM, USD	2,639	2,518	4.8%
US S&P 500	5,096	4,846	5.2%
Euro STOXX 600	494.6	485.7	1.8%
Germany DAX	17,678	16,904	4.6%
France CAC 40	7,927	7,657	3.5%
UK FTSE 100	7,630	7,631	0.0%
Aust S&P/ASX 200	7,699	7,681	0.2%
Japan Topix	2,676	2,551	4.9%
China CSI 300	3,516	3,215	9.4%
NZX50	11,741	11,872	-1.1%
Volatility: VIX	13.40	14.35	-6.6%

3-mth Bill Futures	end-Feb	end-Jan	Change
NZD Jun-24	94.39	94.60	-0.21
AUD Jun-24	95.73	95.87	-0.14
USD Jun-24	94.89	95.39	-0.50
EUR Jun-24	96.35	96.75	-0.41
GBP Jun-24	94.98	95.27	-0.29
CAD Jun-24	94.95	95.00	-0.06

NZ Rates	end-Feb	end-Jan	Change
OCR	5.50	5.50	0.00
NZ 90day BB	5.65	5.67	-0.02
NZ 2yr swap	4.98	4.78	0.20
NZ 5yr swap	4.47	4.31	0.16
NZ 10yr swap	4.54	4.40	0.15
NZ Govt (5/26)	4.78	4.61	0.17
NZ Govt (4/29)	4.55	4.37	0.19
NZ Govt (5/34)	4.75	4.60	0.15
NZ Govt (5/41)	4.96	4.85	0.10

Global 10 year bond rates	end-Feb	end-Jan	Change
US	4.25	3.91	0.34
Canada	3.49	3.32	0.17
UK	4.12	3.79	0.33
France	2.88	2.66	0.22
Germany	2.41	2.17	0.25
Italy	3.84	3.73	0.12
Spain	3.29	3.09	0.20
Portugal	3.11	2.96	0.16
Ireland	2.81	2.59	0.22
Japan	0.70	0.73	-0.02
Australia	4.14	4.01	0.12

Commodities (USD)	end-Feb	end-Jan	Change
WTI Crude	78.26	75.85	3.2%
Brent Crude	83.62	81.71	2.3%
R/B CRB Index	275.1	272.4	1.0%
Gold spot	2,044	2,040	0.2%
Silver spot	22.68	22.96	-1.2%
Copper	383.5	390.6	-1.8%
Iron Ore	114.57	128.71	-11.0%
Thermal coal	131.00	116.50	12.4%
Corn	429.5	458.5	-6.3%
Wheat	576.3	605.3	-4.8%
SGX-NZX Dairy WMP	3,255	3,365	-3.3%
SGX-NZX Milk Price '24	7.89	7.83	0.8%

Source: BNZ, Bloomberg

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