

4 October 2021



Events Round-Up

NZ: ANZ Consumer confidence, Sep: vs. 109.6 prev.

JN: Tankan large manufacturing index, Q3: 18 vs. 13 exp.

EC: CPI (y/y%), Sep: 3.4 vs. 3.3 exp.

EC: Core CPI (y/y%), Sep: 1.9 vs. 1.9 exp.

CA: GDP (m/m%), Jul: -0.1 vs. -0.2 exp.

US: Personal income (m/m%), Aug: 0.2 vs. 0.2 exp.

US: Personal spending (m/m%), Aug: 0.8 vs. 0.7 exp.

US: Core PCE deflator (y/y%), Aug: 3.6 vs. 3.5 exp.

US: ISM Manufacturing, Sep: 61.1 vs. 59.5 exp.

Good Morning

After what was a rocky week, market sentiment improved on Friday, with the S&P500 gaining more than 1% and the USD depreciating. The NZD and AUD finished the week on a positive note, with the NZD closing around 0.6940 and the AUD around 0.7262. It's a big week ahead with the RBNZ expected to increase the OCR on Wednesday for the first time since 2014, despite most of the Waikato joining Auckland in Covid alert level 3 today, and the all-important US nonfarm payrolls report on Friday.

It was a positive session on Friday for US equity markets, with decent gains across all the major indices (S&P500 +1.2%, NASDAQ +0.8%, Russell 2000 small cap index +1.7%). Even after Friday's rebound, the S&P500 was still down more than 2% on the week amidst investor worries about the potential hit to global growth from spiralling energy costs in Europe and China, which is helping to fuel an emerging stagflation narrative, and the recent hawkish tilts by the Fed and Bank of England. Against this backdrop, energy stocks on the S&P500 have been the key outperformers (+3.3% on Friday and +5.8% on week) while Utilities, as big energy consumers, were the only sector in the red on Friday, albeit only slightly (-0.05%).

Helping to lift market sentiment on Friday was news from pharmaceutical company Merck that its Covid-19 treatment drug, molnupiravir, reduced the risk of hospitalization or death by 50% in phase 3 trials. The drug, which is taken as a tablet, proved to be effective against all Covid variants, including delta, with US health expert Fauci describing the interim results as "very good news". The company said it intends to seek emergency-use authorisation from the FDA for its drug shortly and expects

to produce 10 million courses of the drug this year. To the extent that hospital (and ICU) capacity is a key constraint to countries removing (or needing to keep in place) Covid-related restrictions, the prospect of a drug that could potentially halve the risk of hospitalisation for those with mild or moderate symptoms would be a major positive. Merck's share price surged over 8% on the news with positive spill over into broader equity markets.

In economic data, the ISM manufacturing index was stronger than expected, at 61.1, one of its highest readings over the past 30 years. New orders remained very high, at 66.7, while supply-chain issues were still prevalent with manufacturers reporting longer supplier delivery times and very elevated prices paid. In Japan, the bellwether Tankan survey showed an unexpected increase in the large manufacturers index, up to 18 in Q3 from 14 in Q2, and its highest level since 2018. Evidently, manufacturing activity remains very strong despite ongoing supply-chain issues and cost pressures.

On the inflation front, European headline CPI hit 3.4% y/y, its highest level since 2008, in part due to the recent surge in gas and energy prices in the region. Core inflation, which hasn't been above the ECB's 2% target for almost 20 years, jumped to 1.9%, although there are question marks around how ending this increase will be. Key on that front will be what happens to wages, which ECB President Lagarde has said the ECB would "look very attentively" at. Investors are watching how wage negotiations play out in Germany as unions lift their demands this year, including IG Metall, the biggest union in the country, which is looking for a 4.5% pay increase for its workers. The European 10-year inflation swap hit its highest level since 2013 on Friday, at 1.91%. The increase in European inflation expectations stands in contrast to the US market, where inflation breakevens have been rangebound for the past three months, albeit at much higher levels than in Europe. The US Core PCE deflator, the Fed's preferred inflation measure, was 3.6% y/y in August, matching its highest level since the early 1990s.

Despite this inflationary undercurrent, bond yields were lower on Friday, with the US 10-year rate dropping 3bps, to 1.46%, and European 10-year rates lower by 3-5bps. The US 10-year rate, which hit a 3½ month high of 1.565% on Tuesday night, was essentially unchanged last week. NZ swap rates fell by around 1bp across the curve on Friday although 5 and 10-year rates continue to hover near multi-year highs, at 1.87% and 2.24% respectively.

In currencies, the USD was broadly weaker amidst the improvement in wider risk appetite. The BBDXY index was down 0.4% on Friday, paring its gain on the week to 0.6%. The NOK was well out in front of other currencies, gaining 1.4%, with other commodity currencies performing strongly as well (NZD +0.7%, AUD +0.4%, CAD +0.3%). The AUD ended Friday around 0.7260, essentially unchanged on the week while the NZD rebounded to 0.6950, some 1% lower over the course of the week.

The outperformance of commodity currencies on Friday came against a backdrop of firmer commodity prices, with thermal coal making a new record high of \$203.20, breaking its 2008 record high, Singapore-listed iron ore futures gaining around 3%, and copper up by more than 2%. Brent crude oil ended the week just below \$80, near a three-year high, ahead of tonight's OPEC+ meeting at which the cartel is expected to approve a further increase in supply in November.

The White House delayed a scheduled vote on the \$550b bipartisan infrastructure bill on Friday amidst infighting in the Democrat party. Biden will now aim to pass both the infrastructure bill and the larger spending package together, according to the FT, although the price tag on the latter will need to significantly come down from the original \$3.5tn to win support among centrist Democrats, such as West Virginia senator Manchin (who said last week he could only support a package worth \$1.5tn). Meanwhile, the debt ceiling limit continues to approach with no sign of a compromise solution yet. Treasury bills maturing in mid to late October are trading 5-7bps higher than surrounding months, reflecting the risk of late payment if the debt ceiling limit is not resolved in time.

Domestically, the highlight this week is the Monetary Policy Review on Wednesday where the universal consensus is that the RBNZ will raise the OCR by 25bps, to 0.5%, and signal more hikes to come. As of Friday, the market was pricing an almost 90% chance of a 25bps hike. News yesterday that most of Waikato would enter a snap five-day lockdown, after the discovery of two new cases in

the region, is unlikely to shake this consensus since the RBNZ has been clear that lockdowns won't necessarily prevent rate hikes and an October hike has been strongly signalled. But there could be a small pullback in NZ rates and the NZD when markets open this morning.

The government makes its Covid alert level announcement this afternoon, with most experts arguing for an extension of Auckland's level 3 status for at least a little while longer. The QSBO survey on Tuesday, one of the best indicators of near-term economic activity, will be closely watched for the potential hit to growth in Q3/Q4 as well as the extent of underlying inflationary pressures.

The focus offshore this week is the nonfarm payrolls report on Friday night, with several high frequency indicators suggesting downside risks to the consensus of 470k jobs (one indicator even points to a negative print). Should payrolls disappoint, it might cast doubt around whether the Fed makes a taper announcement in November. The RBA meeting tomorrow should be a non-event, with the focus in Australia on the planned reopening in NSW from October 11th. Finally, expect more headlines around Evergrande, with Bloomberg reporting that the company has guaranteed a USD bond that matures today, with any non-payment potentially leading to a cross default on Evergrande's debt obligations. Unlike Evergrande's USD coupons, which have a 30-day grace period before an event of default is decided to have occurred, there is no grace period for late payment on this maturity except for 5 days for administrative issues.

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Coming Up

		Period	Cons.	Prev.	NZT
US	Factory Orders (m/m%)	Aug	1	0.4	03:00
US	Factory Orders Ex Trans (m/m%)	Aug		0.8	03:00

Source: Bloomberg, BNZ

Foreign Exchange					Equities					Commodities**				
Indicative overnight ranges (*)				Other FX		Major Indices				Price				
	Last	% Day	Low	High		Last	% Day			Last	Net Day			
NZD	0.6940	+0.7	0.6879	0.6951	CHF	0.9311	-0.1	S&P 500	4,357	+1.1	28.9	Oil (Brent)	79.13	-0.2
AUD	0.7262	+0.4	0.7197	0.7276	SEK	8.747	-0.2	Dow	34,326	+1.4	23.4	Oil (WTI)	75.88	+1.1
EUR	1.1596	+0.1	1.1573	1.1607	NOK	8.631	-1.3	Nasdaq	14,567	+0.8	28.6	Gold	1757.0	+0.1
GBP	1.3546	+0.5	1.3434	1.3576	HKD	7.786	-0.0	Stoxx 50	4,035	-0.3	26.3	HRC steel	1916.0	+1.2
JPY	111.05	-0.2	110.91	111.30	CNY	6.445	-0.4	FTSE	7,027	-0.8	19.5	CRB	230.4	+0.6
CAD	1.2648	-0.3			SGD	1.357	-0.0	DAX	15,156	-0.7	19.1	Wheat Chic.	766.0	+4.4
NZD/AUD	0.9557	+0.1			IDR	14,308	-0.0	CAC 40	6,518	+0.1	35.1	Sugar	20.06	+4.7
NZD/EUR	0.5985	+0.5			THB	33.66	-0.1	Nikkei	28,771	-2.3	24.9	Cotton	106.53	+3.7
NZD/GBP	0.5123	+0.1			KRW	1,188	+0.3	Shanghai	3,568	+0.9	10.9	Coffee	204.1	+4.8
NZD/JPY	77.07	+0.5			TWD	27.84	+0.1	ASX 200	7,186	-2.0	24.1	WM powder	3830.0	+1.3
NZD/CAD	0.8778	+0.3			PHP	50.81	-0.4	NZX 50	13,279	+0.0	12.3	Australian Futures		
NZ TWI	74.18	+0.6										3 year bond	99.52	-0.01
												10 year bond	98.49	-0.03
Interest Rates														
Rates		Swap Yields			Benchmark 10 Yr Bonds		NZ Government Bonds			NZ Swap Yields				
	Cash	3Mth	2 Yr	10 Yr		Last	Net Day		Last		Last			
USD	0.25	0.13	0.37	1.48	USD	1.46	-0.03	NZGB 5 1/2 04/15/23	1.00	0.00	1 year	1.08	-0.01	
AUD	0.10	0.02	0.29	1.65	AUD	1.49	0.00	NZGB 0 1/2 05/15/26	1.53	0.01	2 year	1.42	-0.01	
NZD	0.25	0.64	1.42	2.24	NZD	2.01	0.01	NZGB 0 1/4 05/15/28	1.76	0.01	5 year	1.87	-0.00	
EUR	0.00	0.06	-0.44	0.15	GER	-0.22	-0.03	NZGB 1 1/2 05/15/31	2.01	0.01	7 year	2.04	-0.00	
GBP	0.10	0.08	0.71	1.17	GBP	1.00	-0.02	NZGB 2 05/15/32	2.11	0.02	10 year	2.24	-0.01	
JPY	-0.04	-0.08	0.01	0.11	JPY	0.06	-0.01	NZGB 1 3/4 05/15/41	2.62	0.02	15 year	2.45	-0.01	
CAD	0.25	0.45	0.94	1.92	CAD	1.47	-0.04	NZGB 2 3/4 05/15/51	2.81	0.02				

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

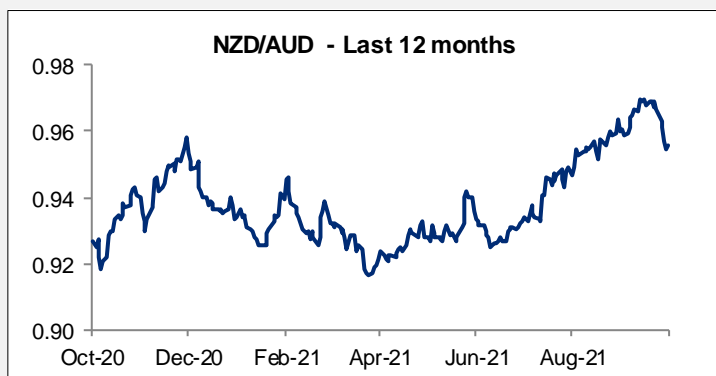
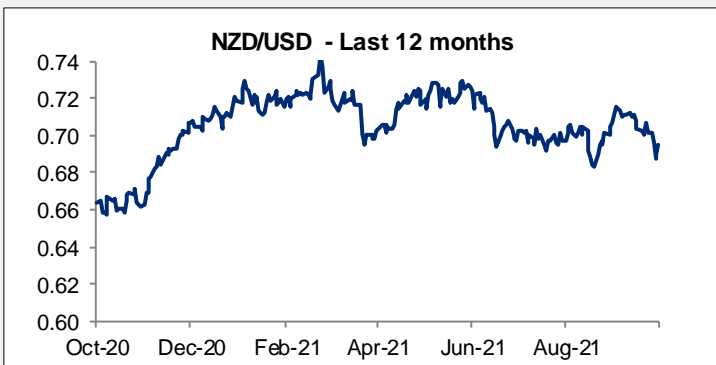
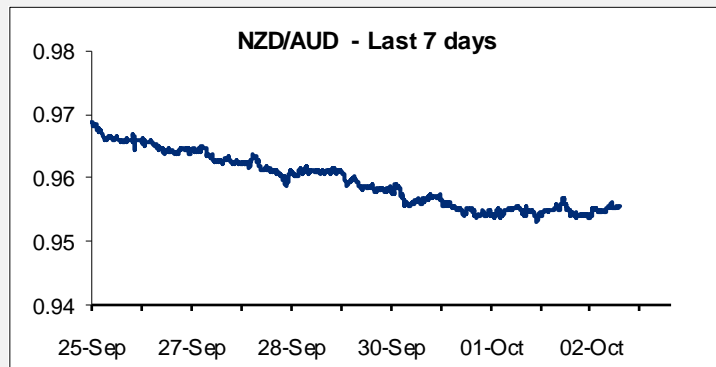
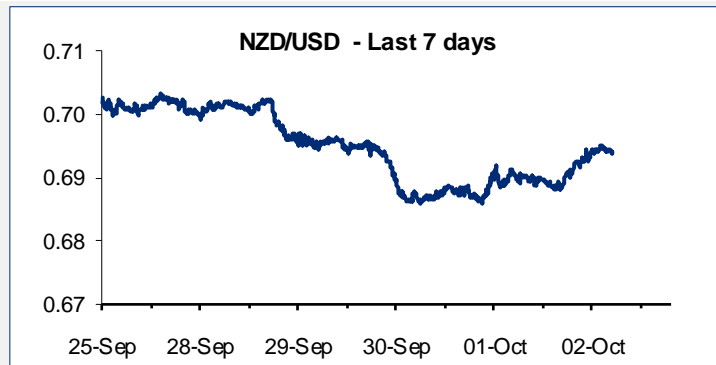
** All near futures contracts, except CRB. Metals prices are CME.

Rates are as of New York close

Source: Bloomberg

NZD exchange rates

2/10/2021	NY close	Prev. NY close
USD	0.6940	0.6899
GBP	0.5129	0.5120
AUD	0.9573	0.9546
EUR	0.5992	0.5958
JPY	77.16	76.78
CAD	0.8788	0.8748
CHF	0.6469	0.6428
DKK	4.4559	4.4307
FJD	1.4671	1.4564
HKD	5.4096	5.3718
INR	51.50	51.16
NOK	5.9965	6.0356
PKR	118.45	117.72
PHP	35.30	35.18
PGK	2.4379	2.4233
SEK	6.0773	6.0449
SGD	0.9429	0.9367
CNY	4.4778	4.4642
THB	23.37	23.34
TOP	1.5677	1.5573
VUV	77.75	77.01
WST	1.7894	1.7888
XPF	71.38	70.98
ZAR	10.3413	10.3956



NZD/USD Forward Points

	BNZ buys NZD	BNZ sells NZD
1 Month	-1.53	-1.19
3 Months	-5.82	-5.34
6 Months	-16.97	-15.97
9 Months	-34.29	-32.29
1 Year	-54.63	-52.69

NZD/AUD Forward points

	BNZ buys NZD	BNZ Sells NZD
1 Month	-3.79	-3.22
3 Months	-13.53	-12.57
6 Months	-31.73	-29.64
9 Months	-57.48	-53.26
1 Year	-86.91	-81.96

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