

17 December 2021



Events Round-Up

US: Fed Funds Target Rate (%), Dec: 0.25 vs. 0.25 exp.

NZ: GDP (q/q%), Q3: -3.7 vs. -4.1 exp.

NZ: GDP (y/y%), Q3: -0.3 vs. -1.4 exp.

AU: Employment change (k), Nov: 366 vs. 200 exp.

AU: Unemployment rate (%), Nov: 4.6 vs. 5 exp.

GE: Manufacturing PMI, Dec: 57.9 vs. 56.9 exp.

GE: Services PMI, Dec: 48.4 vs. 51 exp.

EZ: Manufacturing PMI, Dec: 58 vs. 57.8 exp.

EZ: Services PMI, Dec: 53.3 vs. 54.3 exp.

NO: Norges Bank Deposit Rate (%), Dec: 0.5 vs. 0.5 exp.

UK: Manufacturing PMI, Dec: 57.6 vs. 57.6 exp.

UK: Services PMI, Dec: 53.2 vs. 57 exp.

UK: BoE Base Rate (%), Dec: 0.25 vs. 0.1 exp.

EZ: ECB Deposit Facility Rate (%), Dec: -0.5 vs. -0.5 exp.

US: Initial jobless claims (k), 11-Dec: 206 vs. 200 exp.

US: Housing starts (k), Nov: 1679 vs. 1567 exp.

US: Philly Fed business outlook, Dec: 15.4 vs. 29.1 exp.

US: Markit Manufacturing PMI, Dec: 57.8 vs. 58.5 exp.

US: Markit Services PMI, Dec: 57.5 vs. 58.8 exp.

Good Morning

A further hawkish shift among central banks has been in evidence over the past 24 hours. The Fed announced an accelerated tapering pace and signalled three rate hikes next year while the BoE surprised markets by raising its cash rate overnight. But bond rates haven't been overly affected (indeed the US rates are lower overnight). The USD is broadly weaker since the Fed update and equity markets higher, albeit with tech stocks underperforming. The NZD is back up to 0.68 amidst the weaker USD and improvement in risk appetite.

There is a lot to cover over the past 24 hours. We'll start off with the FOMC meeting, which took place yesterday morning. As expected, the Fed announced it would double its tapering pace, from \$15b per month to \$30b per month, which will see its bond buying end in March rather than June. All Fed officials now think rate hikes are likely in 2022 with the median official expecting three rate increases next year, three more in 2023 and two further hikes in 2024. This was on the hawkish side of economists'

expectations but relatively close to market pricing, at least for 2022. Powell's comments in the press conference backed up the hawkish shift as he said "there wouldn't be a need for a long delay" between tapering and rate hikes and noted there was a real risk that inflation may be more persistent (further walking away from the previous narrative around inflation being 'transitory').

Looking at market movements, you'd be forgiven for thinking the Fed had delivered a dovish update. US bond yields are lower, with the 2-year rate down about 5bps from its levels yesterday morning, at 0.62%, while the 10-year rate is down 4bps, to 1.42%. Likewise, the USD is broadly weaker over the past 24 hours, by between 0.5%-0.7% in index terms from this time yesterday. This has seen the NZD push up to the 0.68 mark and the AUD to 0.7180, both around 0.9% higher than this time yesterday. The market reaction suggests investors may have been braced for an even more hawkish Fed update, although market positioning (short US bonds and long the USD) is probably as much to blame.

Equity markets reacted positively to the Fed meeting, with investors seemingly comfortable moving back into risk assets now the event risk has passed and with monetary policy set to remain accommodative for some time yet. The S&P500 increased 1.6% yesterday and it has held onto most of those gains overnight, down by just 0.6%. Sector rotation is evident, with cyclicals (such as energy, bank, and industrial stocks) up strongly overnight while tech stocks are down (NASDAQ -2% after yesterday's 2.1% increase).

The Bank of England sprung another surprise on the market overnight, with the MPC voting 8-1 in favour of raising its cash rate from 0.1% to 0.25%. The market had priced around a 40% chance of a hike going into the meeting while the majority of economists thought the BoE would hold off raising rates to give it more time to survey the effects of the Omicron outbreak. In justifying the rate hike, Governor Bailey noted the UK had "a very tight labour market and...more persistent inflation pressures", with inflation set to reach around 6% next year, much higher than the BoE's previous 5% forecast. The Bank said further "modest" tightening was likely to be required over the coming years to hit its inflation target, although it acknowledged there were risks on both sides. UK bond rates were around 2bps higher across the curve overnight, having been up as much as 10bps at one point, with the market pricing around 85bps of rate hikes next year.

Meanwhile, the GBP has outperformed, appreciating by 0.5% since the NZ close to around 1.3320.

At its policy update overnight, the ECB confirmed it would start tapering its QE bond buying from early next year, with President Lagarde citing progress in the economic recovery and inflation towards the central bank's targets. The €1.85tn pandemic bond buying programme will end as planned in March, while its existing Asset Purchase Programme will be beefed up for a period to smooth the adjustment for the market and avoid what Lagarde said would otherwise be a "brutal transition". The Asset Purchase Programme will be increased from the current €20b per month pace to €40b in Q2, reducing to €30b in Q3 and then back to €20b from Q4 next year. That the ECB plans to be buying bonds through next year is a strong signal that it doesn't expect to raise rates in 2022, as markets had recently been speculating. The ECB also said it would be more flexible with reinvestments of its pandemic bond holdings (i.e. giving it the option to skew reinvestments towards vulnerable countries like Greece) if markets came under stress again. European bond rates are higher overnight, by between 1bps for Germany and 5bps for Italy, although most of these moves occurred in response to the Bank of England's surprise rate hike rather than the ECB's announcements. Italian 10-year bonds, which have been a key beneficiary of the ECB's bond buying, are trading around 130bps above Germany, which is close to its highest spread in 18 months. The EUR initially jumped after the ECB decision, before reversing those gains to be back at 1.1320.

Elsewhere, the Norges Bank raised its cash rate 25bps, as expected, and signalled that another rate rise was likely in March.

There is plenty of economic data to cover over the past 24 hours as well, as the data column above illustrates. In Europe, the reimposition of Covid-related restrictions saw the Services PMI fall by more than expected, to an 8-month low of 53.3. Manufacturing remains a bright spot (being less affected by Covid restrictions), with the Manufacturing PMI sitting at a still lofty 58. Pricing gauges in the PMIs eased, albeit to still very high levels, indicating continued inflation pressures. In the US, jobless claims remained at very low levels with firms reluctant to let go of staff amidst an extremely tight labour market while housing starts were much stronger than expected, indicating a pickup in construction activity.

The Australian November employment report was a stonker, with a record 366k increase in employment and a

0.6% fall in the unemployment rate to 4.6%, despite a sharp 1.4% increase in the participation rate. Speaking shortly before the employment report was released, RBA Governor Lowe again pushed back on market pricing for rate hikes next year, claiming Australia was "quite different" to other countries. The market plainly doesn't believe the RBA, with the first hike fully priced for June and almost four hikes priced in by the end of next year. Australia's 3-year bond rate was 6bps higher on the day.

There wasn't much market reaction to the NZ GDP release yesterday, which showed a 3.7% fall in Q3, reasonably close (considering all the disruption from lockdowns) to the -4.1% consensus. The result is much better than the -7% the RBNZ had factored into its MPS projections, although the likelihood is that growth will rebound less strongly in Q4 and Q1, so the monetary policy implications should be limited.

NZ swap rates were higher yesterday on the back of the movements in Australia, with 2 and 5-year rates up by 4bps and the 10-year rate 2bps higher. The yield curve remains under flattening pressure, with the spread between 5 and 10-year swap rates falling back to just 0.25bps. Investors often see an inverted curve, which the 5y10y slope is teetering on, as an indicator of a major future growth slowdown, although its track record in NZ has historically been less reliable than in the US. A day after New Zealand Debt Management slashed its forecast bond issuance, government bonds again performed relatively well, with yields down by 1-2bps at the longer end.

After what has been a frenetic last 24 hours, there is a lot less on the agenda in the session ahead. The ANZ business survey is released this afternoon while the German IFO business survey comes out tonight. With all the key data and central bank decisions now out of the way, trading activity is likely to die down into the Christmas holiday break.

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Coming Up

		Period	Cons.	Prev.	NZT
NZ	ANZ Business Confidence	Dec		-16.4	13:00
NZ	ANZ Activity Outlook	Dec		15	13:00
GE	IFO Expectations	Dec	93.6	94.2	22:00

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	0.6799	+0.2	0.6760	0.6834	CHF	0.9208	-0.5	S&P 500	4,692	-0.4	26.8	Oil (Brent)	75.15	+1.7
AUD	0.7183	+0.2	0.7153	0.7224	SEK	9.048	-0.4	Dow	35,967	+0.1	19.3	Oil (WTI)	72.43	+2.2
EUR	1.1316	+0.3	1.1284	1.1360	NOK	8.991	-0.3	Nasdaq	15,257	-2.0	20.5	Gold	1788.2	+1.5
GBP	1.3319	+0.4	1.3242	1.3374	HKD	7.804	+0.0	Stoxx 50	4,202	+1.0	18.6	HRC steel	1637.0	+0.4
JPY	113.63	-0.4	113.56	114.22	CNY	6.368	+0.0	FTSE	7,261	+1.3	10.5	CRB	223.8	-0.2
CAD	1.2779	-0.4			SGD	1.364	-0.1	DAX	15,636	+1.0	15.3	Wheat Chic.	771.0	+1.2
NZD/AUD	0.9465	+0.1			IDR	14,362	+0.2	CAC 40	7,005	+0.6	26.3	Sugar	19.42	+0.7
NZD/EUR	0.6008	+0.0			THB	33.41	-0.0	Nikkei	29,066	+2.1	8.4	Cotton	107.71	+1.8
NZD/GBP	0.5105	-0.2			KRW	1,184	-0.2	Shanghai	3,675	+0.8	7.9	Coffee	236.8	-0.2
NZD/JPY	77.26	-0.1			TWD	27.81	-0.0	ASX 200	7,296	-0.4	8.0	WM powder	4105	-0.6
NZD/CAD	0.8688	-0.2			PHP	49.99	-0.6	NZX 50	12,778	-0.7	-0.9	Australian Futures		
NZ TWI	73.05	+0.1										3 year bond	98.755	-0.01
												10 year bond	98.37	0.03
Interest Rates														
	Rates		Swap Yields		Benchmark 10 Yr Bonds		NZ Government Bonds			NZ Swap Yields				
	Cash	3Mth	2 Yr	10 Yr	USD	Last	Net Day		Last		Last			
USD	0.25	0.22	0.86	1.48	USD	1.42	-0.04	NZGB 5 1/2 04/15/23	1.54	0.01	1 year	1.74	0.03	
AUD	0.10	0.07	0.95	1.88	AUD	1.57	0.01	NZGB 0 1/2 05/15/26	2.24	0.01	2 year	2.28	0.04	
NZD	0.75	0.92	2.28	2.59	NZD	2.33	-0.02	NZGB 0 1/4 05/15/28	2.28	0.00	5 year	2.58	0.04	
EUR	0.00	0.06	-0.36	0.11	GER	-0.35	0.01	NZGB 1 1/2 05/15/31	2.28	-0.02	7 year	2.58	0.03	
GBP	0.25	0.10	1.07	1.00	GBP	0.76	0.02	NZGB 2 05/15/32	2.33	-0.02	10 year	2.59	0.02	
JPY	-0.04	-0.08	0.00	0.09	JPY	0.05	-0.01	NZGB 1 3/4 05/15/41	2.71	-0.01	15 year	2.61	0.02	
CAD	0.25	0.50	1.46	1.87	CAD	1.35	-0.06	NZGB 2 3/4 05/15/51	2.77	-0.02				

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

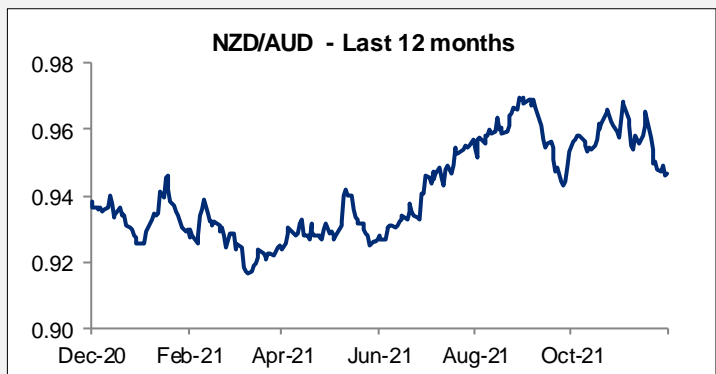
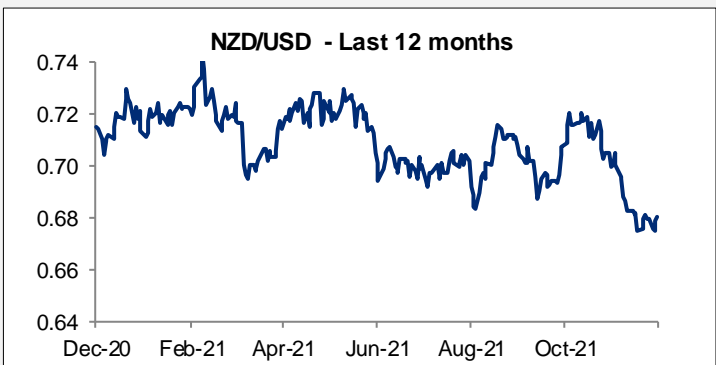
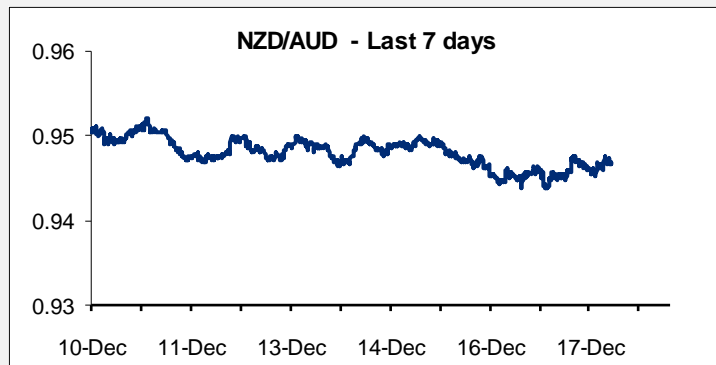
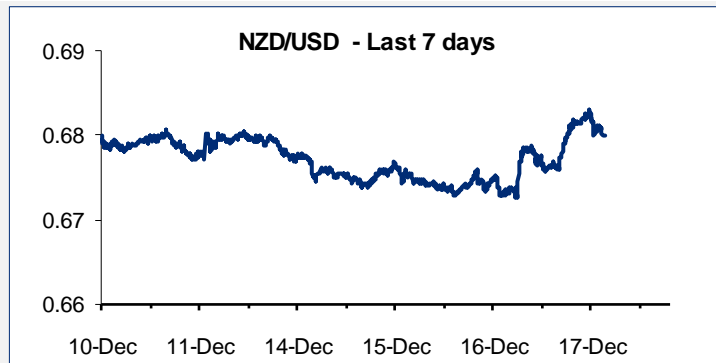
** All near futures contracts, except CRB. Metals prices are CME.

Rates are as of: NZT 06:48

Source: Bloomberg

NZD exchange rates

17/12/2021	6:49 a.m.	Prev. NY close
USD	0.6799	0.6784
GBP	0.5105	0.5115
AUD	0.9465	0.9463
EUR	0.6008	0.6009
JPY	77.26	77.36
CAD	0.8688	0.8707
CHF	0.6261	0.6276
DKK	4.4678	4.4686
FJD	1.4518	1.4465
HKD	5.3061	5.2931
INR	51.74	51.72
NOK	6.1127	6.1146
PKR	120.91	120.64
PHP	33.98	34.12
PGK	2.3856	2.3837
SEK	6.1519	6.1624
SGD	0.9272	0.9262
CNY	4.3298	4.3197
THB	22.72	22.67
TOP	1.5344	1.5415
VUV	76.64	76.92
WST	1.7566	1.7551
XPF	72.01	71.87
ZAR	10.8545	10.8354



NZD/USD Forward Points

	BNZ buys NZD	BNZ sells NZD
1 Month	-3.34	-2.84
3 Months	-11.68	-11.08
6 Months	-30.75	-29.75
9 Months	-55.56	-53.81
1 Year	-82.97	-80.97

NZD/AUD Forward points

	BNZ buys NZD	BNZ Sells NZD
1 Month	-8.13	-6.93
3 Months	-20.59	-18.99
6 Months	-48.37	-45.83
9 Months	-79.80	-76.04
1 Year	-111.17	-106.38

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