

21 September 2021



Events Round-Up

NZ: Performance of services index, Aug: 35.6 vs. 55.9 prev.

US: NAHB housing market index, Sep: 76 vs. 74 exp.

Good Morning

The new week has begun with a plunge in risk appetite as fears mount of contagion risk from the imminent collapse of Chinese developer Evergrande. Global equity markets have seen some chunky falls, global rates have rallied and commodity prices are weaker. Currency market reaction has been relative contained, with only some modest underperformance by the NZD and AUD and a small gain for the USD.

While the FOMC meeting on Thursday was meant to take centre stage this week, focus recently has been on troubled Chinese property developer Evergrande and how its insolvency might reverberate across the market. Evergrande is a large company with some \$300b of liabilities, equivalent to around 2% of China GDP, and a range of creditors including Chinese banks, offshore bond holders, contractors, suppliers and retail investors. The company also has more than 200 offshore and 2,000 onshore subsidiaries.

On paper, given the contagion risks, the company looks too-big-to-fail and investors await the Chinese government's involvement to avoid a worst-case scenario. Major banks were told last week they wouldn't receive interest payments on loans due yesterday and interest payments on bonds are due this Thursday. As long as uncertainty remains about how much the Chinese government will get involved, what an imminent restructure looks like, and how much of a hair-cut creditors will need to take, fears will continue to reverberate across markets.

Weaker risk sentiment was weaker as soon Asian markets opened yesterday. Hong Kong's Hang Seng index plunged by 3.3%, led by a 6.7% plunge in the real estate index and S&P futures steadily weakened throughout the session. A number of key Asian markets were on holiday yesterday, including China, Japan, and Korea which exacerbated market movements as investors looked to sell proxies. Europe's Stoxx 600 index closed down 1.7% while selling in US equities has been relentless and the S&P500 is currently down 2½%. The question is when will the buy-the-dip brigade step in? Markets will want some clarity on

how much the Chinese government will get involved in any Evergrande structure and what tools might be employed to reduce both market and economic contagion risk. This credit event could all get resolved quickly and from next week we might never be quoting Evergrande again. Who knows?

As investors switch towards safer assets, global bond markets have been well supported. German and UK 10-year rates fell 4-5bps while the US 10-year rate is currently down 5bps to 1.31%, with curves flatter. While Evergrande's issues have dominated market pricing, investors are also attuned to the FOMC update on Thursday. Market pricing of future rate hikes looks fairly light compared to the Fed's June dot-plot of committee member Fed Funds rate expectations and there is a good chance that some members will move their dot forward, suggesting a slightly earlier start to the tightening process as inflation forecasts are ramped higher.

Many key commodity prices have fallen, including a 1½-2% fall in oil prices, with Brent crude trading down to around USD74 per barrel, while copper prices are down about 3%. Iron ore prices continued to tumble, with futures on the Singapore exchange down to just over USD90 per tonne, before settling around USD95.

Considering the move in other assets, movements in the currency market have been well contained. Indeed, the commodity currencies aren't even the worst performing, with GBP taking on that role, down 0.7% to 1.3650 on domestic factors. Some position squaring might be evident ahead of the Bank of England's policy update on Thursday night, while the surge in natural gas prices has continued and has all the makings of an energy crisis, which threatens to stymie the economic recovery. Gas futures are up 16% for the day, taking their gain for the month to almost 50% and their gain for the past six months to over 300%.

The NZD and AUD have underperformed, but falls have been modest considering the backdrop. The NZD found some support just above 0.70 overnight and is currently down only 0.3% from last week's close to 0.7020. The AUD saw some support at 0.7220 and is currently down about ½% from last week's close to 0.7240. NZD/AUD has gravitated to 0.97.

At the top of the leaderboard, JPY has been the strongest, with USD/JPY down ½% to 109.35, while EUR is flat at

1.1720, containing the lift in the USD BBDXY index to only 0.2%.

The domestic rates market was fairly quiet, with NZGB yields ticking a little higher in yield, more reflecting the Friday night selloff of in US Treasuries than the weaker risk backdrop. Rates will likely get re-priced on the open, with the Australian 10-year bond future lower by about 6bps in yield since the NZ close. OIS pricing for coming RBNZ meetings peeled off about 2-3bps, taking the October meeting down to 0.57%, or the implied probability of a 50% hike down from 40% to 28%. This didn't have any impact on the 2-year swap rate, which was unchanged at 1.50%.

The plunge in the performance of services index, which measured actual activity in August, plunged to 36.5, adding to the PMI plunge reported last week, a result of NZ's lockdowns. Economic activity is set to improve, with Auckland's restrictions moving down to Level 3 from tomorrow and increased capacity numbers allowed for indoor activities in the rest of the country in a Level 2 environment.

Yesterday BNZ lifted its fixed-term mortgage rates by about 30bps across the curve, taking the popular 2-year rate up to 3.25%, now up some 75bps over the past couple of months. Business lending rates are up over 100bps over that time. The point is that a significant tightening in

monetary policy is underway, even if the RBNZ hasn't yet officially begun to lift the OCR rate. Expectations of a series of OCR hikes and the associated lift in wholesale rates has been enough to drive up lending rates.

In the day ahead, domestically there will be some interest in speech notes being released by RBNZ Assistant Governor Hawkesby at 9am. These will cover off the RBNZ's "least regrets" approach to setting monetary policy. The speech could provide some insights into how the RBNZ will weigh up its forthcoming decision on 6 October, in particular how the Bank might judge the merits of a 25bps move versus a 50bps increase.

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Coming Up

	Period	Cons.	Prev.	NZT
NZ	RBNZ's Hawkesby releases speech notes			09:00
NZ	Westpac consumer confid.	Q3	107.1	09:00
AU	RBA minutes of Sep. meeting			13:30
US	Building permits (k)	Aug	1600	1635 00:30
US	Housing starts (k)	Aug	1550	1534 00:30

Source: Bloomberg, BNZ

Foreign Exchange					Equities			Commodities**					
Indicative overnight ranges (*)					Major Indices			Price					
	Last	% Day	Low	High		Last	% Day	% Year		Last	Net Day		
NZD	0.7022	-0.3	0.7006	0.7041	S&P 500	4,313	-2.7	29.9	Oil (Brent)	74.06	-1.7		
AUD	0.7242	-0.3	0.7220	0.7263	Dow	33,669	-2.6	21.7	Oil (WTI)	70.45	-2.2		
EUR	1.1727	+0.0	1.1700	1.1737	Nasdaq	14,554	-3.3	34.8	Gold	1761.1	+0.7		
GBP	1.3654	-0.6	1.3641	1.3700	Stoxx 50	4,044	-2.1	23.1	HRC steel	1935.0	+0.1		
JPY	109.33	-0.5	109.32	109.85	FTSE	6,904	-0.9	14.9	CRB	222.1	-0.8		
CAD	1.2822	+0.5			DAX	15,132	-2.3	15.4	Wheat Chic.	711.0	-1.2		
NZD/AUD	0.9696	+0.2			CAC 40	6,456	-1.8	29.7	Sugar	18.86	-1.7		
NZD/EUR	0.5988	-0.3			Nikkei	30,500	+0.6	30.6	Cotton	89.89	-2.5		
NZD/GBP	0.5143	+0.4			Shanghai	3,614	+0.2	8.3	Coffee	182.6	-2.0		
NZD/JPY	76.77	-0.8			ASX 200	7,248	-2.1	24.5	WM powder	3710.0	-0.4		
NZD/CAD	0.9004	+0.2			NZX 50	13,179	-0.4	14.2	Australian Futures				
NZ TWI	74.96	-0.1							3 year bond	99.645	0.03		
									10 year bond	98.74	0.08		
Interest Rates					NZ Government Bonds			NZ Swap Yields					
	Rates				Benchmark 10 Yr Bonds		Last			Last			
	Cash	3Mth	2 Yr	10 Yr	Last	Net Day							
USD	0.25	0.12	0.33	1.34	USD	1.31	-0.06	NZGB 5 1/2 04/15/23	1.11	0.00	1 year	1.17	-0.02
AUD	0.10	0.01	0.20	1.41	AUD	1.30	0.00	NZGB 0 1/2 05/15/26	1.57	0.01	2 year	1.50	-0.00
NZD	0.25	0.67	1.50	2.13	NZD	1.89	0.02	NZGB 0 1/4 05/15/28	1.74	0.01	5 year	1.82	0.00
EUR	0.00	0.06	-0.45	0.07	GER	-0.32	-0.04	NZGB 1 1/2 05/15/31	1.89	0.02	7 year	1.95	0.01
GBP	0.10	0.07	0.56	0.98	GBP	0.79	-0.05	NZGB 2 05/15/32	1.96	0.02	10 year	2.13	0.01
JPY	-0.04	-0.08	0.00	0.10	JPY	0.05	0.00	NZGB 1 3/4 05/15/41	2.53	0.02	15 year	2.33	0.02
CAD	0.25	0.45	0.84	1.70	CAD	1.22	-0.07	NZGB 2 3/4 05/15/51	2.76	0.01			

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

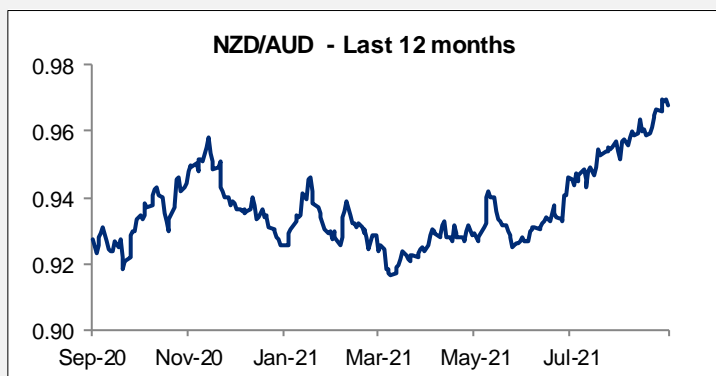
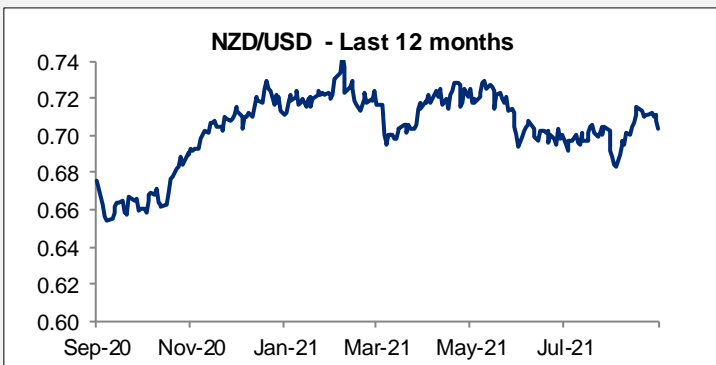
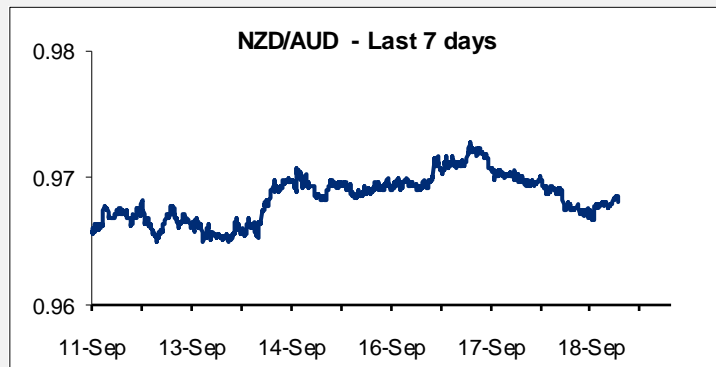
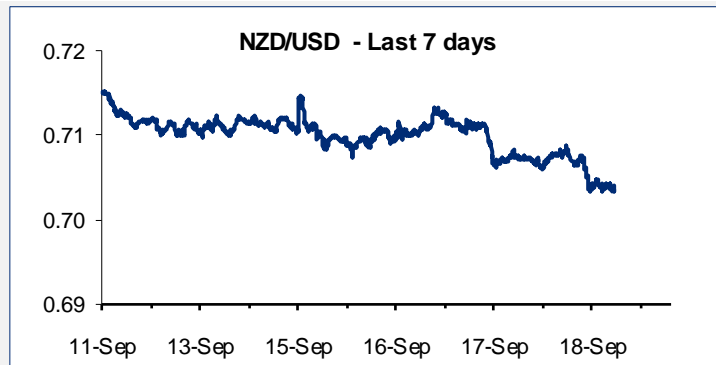
** All near futures contracts, except CRB. Metals prices are CME.

Rates are as of: NZT 06:54

Source: Bloomberg

NZD exchange rates

18/09/2021	NY close	Prev. NY close
USD	0.7040	0.7075
GBP	0.5123	0.5129
AUD	0.9672	0.9702
EUR	0.6004	0.6013
JPY	77.39	77.63
CAD	0.8986	0.8973
CHF	0.6563	0.6563
DKK	4.4644	4.4710
FJD	1.4688	1.4789
HKD	5.4791	5.5064
INR	51.73	52.01
NOK	6.1322	6.1049
PKR	118.36	118.99
PHP	35.17	35.35
PGK	2.4710	2.4609
SEK	6.1129	6.0999
SGD	0.9493	0.9515
CNY	4.5521	4.5688
THB	23.39	23.37
TOP	1.5802	1.5677
VUV	78.12	78.23
WST	1.8110	1.8158
XPF	71.27	71.51
ZAR	10.3615	10.3279



NZD/USD Forward Points

	BNZ buys NZD	BNZ sells NZD
1 Month	-0.56	-0.23
3 Months	-6.26	-5.81
6 Months	-19.52	-18.52
9 Months	-39.70	-37.80
1 Year	-63.15	-61.15

NZD/AUD Forward points

	BNZ buys NZD	BNZ Sells NZD
1 Month	-2.22	-1.55
3 Months	-12.50	-11.46
6 Months	-35.68	-33.44
9 Months	-65.28	-60.99
1 Year	-99.05	-93.85

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