

29 October 2021



Events Round-Up

JN: BoJ 10yr yield target (%), Oct: 0 vs. 0 exp.

EC: Economic confidence, Oct: 118.6 vs. 116.7 exp.

EC: ECB deposit facility rate (%), Oct: -0.5 vs. -0.5 exp.

GE: CPI (y/y%), Oct: 4.6 vs. 4.5 exp.

US: Initial jobless claims (k), 23-Oct: 281 vs. 288 exp.

US: GDP (ann'lsd q/q%), Q3: 2 vs. 2.6 exp.

Good Morning

Global bond markets remain very volatile, even though there hasn't been much spill over into other asset classes like equities and currencies at this stage. Yesterday saw a huge move higher in Australian short-end rates after the RBA decided not to enforce its Yield Curve Control target, with NZ short-end rates increasing sharply in response. Overnight, the EUR is higher as President Lagarde stopped short of saying market pricing for rate hikes next year was wrong. Equity markets have increased, the USD has weakened, and the NZD has bounced back to 0.72.

Market focus at present is centred on elevated inflation pressures and central banks' shift towards tighter policy and earlier rate hikes. Yesterday, the Bank of Canada announced a sudden end to QE and signalled rate hikes around the middle of next year. In Australia, there has been a rapid increase in RBA rate hike expectations since the CPI report earlier this week, with the move gaining momentum yesterday after the RBA decided against enforcing its Yield Curve Control target (see more below). Overnight, it was the turn of ECB President Lagarde to face questions around above target inflation and market expectations of rate hikes by the end of next year (17bps of hikes priced by the end of 2022).

Lagarde reaffirmed that the ECB was sticking to its 'transitory' inflation view, expecting inflation to fall back below the 2% inflation target in 2023, although she acknowledged it would "take longer to decline than originally expected", due to ongoing supply chain disruptions. On the basis of these inflation forecasts, Lagarde said the ECB doesn't expect to be raising rates by the end of next year, as markets are pricing, but it was "not for me to say" whether markets were getting ahead of themselves, an admission that the ECB's transitory inflation view could be wrong. Finally, Lagarde all but confirmed that the ECB's pandemic bond buying

programme will finish as scheduled in March, with the governing council to decide at December's meeting whether to beef up its existing asset purchase programme from this point.

The EUR and European bond yields moved higher during Lagarde's press conference, with some describing her pushback against the market's rate hike pricing as 'half hearted'. The EUR is up 0.7% overnight, to a one-month high of 1.1685. The 10-year German yield is 4bps higher, at -0.14%, near a 2½-year high, while the bigger mover has been Italy, which has seen its yields move higher by as much as 12bps. Italy has been a key beneficiary of the ECB's huge bond buying programme.

The US 10-year rate is 3bps higher overnight, to 1.57%, while the 2-year rate is unchanged, at an 18-month high of 0.50%. The US yield curve has reversed some of its recent flattening trend which has been driven by expectations of earlier Fed rate hikes.

Economic data hasn't been the focus overnight. US Q3 GDP was slightly lower than expected (2% annualised q/q% vs. 2.6% expected) with the delta variant outbreak, supply-side constraints, and absence of stimulus cheques among the factors slowing growth over the quarter. The GDP report was not as low as some had feared, given the Atlanta Fed's nowcasting estimate was predicting just 0.2% annualised growth. US initial jobless claims fell to a new post-Covid low, at 281k, with employers reluctant to let go of staff amidst an extremely tight labour market. Ahead of the European CPI release tonight, Spanish CPI was much higher than expected in October, coming in at 5.5% y/y (4.6% expected), while German headline inflation hit its highest level since 1993, at 4.5%, albeit this was close to market expectations.

Equity markets have been resilient to the volatility in bond markets and expectations of earlier central bank tightening. The S&P has increased 0.8% overnight while the NASDAQ has outperformed ahead of the earnings reports from tech heavyweights Amazon and Apple this morning, up 1.2% to a fresh record high. Corporate earnings remain supportive, with more than 80% of companies in the S&P beating analyst expectations, among them industry bellwether Caterpillar and automaker Ford overnight. Ultra-low real interest rates (the 10-year real yield is still below -1%) are another supportive factor for equities.

In currencies, the USD is broadly weaker on the back of EUR strength and improved risk appetite. The BBDXY USD index is down 0.4% and trading at its lowest level in a month. European currencies have been the major gainers overnight, benefiting from the strength in the EUR, while the NZD has pushed up to 0.72, about 0.3% higher than this time yesterday. The AUD has increased 0.2%, to its highest level in four months, around 0.7540.

Turning to developments in Australia, the RBA decided not to buy the April 2024 Yield Curve Control bond yesterday even though it was trading at around 0.23%, well above its 0.1% target. The RBA's decision not to enforce the target, coming off the back of Tuesday's higher-than-expected core inflation number, led to renewed speculation the RBA may change its forward guidance at next week's meeting and drop the Yield Curve Control policy. With the RBA not defending its yield target yesterday, the April 2024 bond exploded 33bps higher, to 0.54%. The RBA is now in a difficult position, because the market clearly sees its forward guidance, that it is unlikely to raise its cash rate until 2024, as not credible, so even if it defends the target in the future, the market may continue to take it on. All eyes are on today's 1:15pm announcement to see whether the RBA intervenes today, with inaction likely to see another lurch higher in yields.

The volatility in Australia continues to spill over to the domestic rates market, with further sharp increases in short-to-intermediate term interest rates yesterday. The 2-year swap rate was 18bps higher in extremely illiquid market conditions, hitting its highest level since early-2017, at 2.35%. To give some context for the scale of the moves seen this month, the NZ 2-year swap rate is up 92bps this month alone, on track for its biggest monthly increase since June 1994, a time that predates the OCR. Liquidity is woeful.

At face value, the OIS market is pricing the OCR to get to around 3% by the middle of 2023. We don't think this should be read as a pure market expectation of the OCR as it likely reflects a healthy risk premium at present. The yield curve now prices a 25bps OCR rate *cut* between years 2 and 5.

The NZ yield curve continues to aggressively flatten, in line with global trends, with the 10-year swap rate up 'just' 4bps yesterday and the 30-year government bond yield

even managing a 2bps fall. The flattening of the curve is consistent with the market expecting central bank tightening to cause a major growth slowdown down the line.

In other news, Biden set out his plans for his proposed social spending bill, trimming its size to \$1.75tn (much lower than the originally planned \$3.5tn), to satisfy the demands of centrist Democrat senators. It's still unclear whether the bill has the votes to pass both the Senate and Congress.

Following on from yesterday's news that Russian President Putin had ordered state-owned Gazprom to refill European gas storage facilities from early next month, European natural gas futures have fallen 11%, to their lowest level in a month. Oil prices, which have been benefiting from expectations that some gas consumers will switch to oil, are slightly lower, by around 0.2% on Brent crude.

There is a lot of data in the session ahead but the key ones for the market are the inflation numbers in Europe and the US (the core PCE deflator) as well the employment cost index, a measure of US wage growth. The focus in the local session will be the RBA's 1:15pm announcement whether it decides to buy the April 2024 bond or not.

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Coming Up

		Period	Cons.	Prev.	NZT
NZ	ANZ Consumer Confidence (m/m)	Oct	-4.7	10:00	
AU	Retail Sales (m/m%)	Sep	0.4	-1.7	13:30
GE	GDP (q/q%)	3Q P	2.2	1.6	21:00
EC	GDP (q/q%)	3Q P	2.05	2.2	22:00
EC	Core CPI (y/y%)	Oct P	1.9	1.9	22:00
EC	CPI (y/y%)	Oct	3.7	3.4	22:00
US	Employment Cost Index (q/q%)	3Q	0.9	0.7	01:30
US	Personal Income (m/m%)	Sep	-0.2	0.2	01:30
US	Personal Spending (m/m%)	Sep	0.6	0.8	01:30
US	PCE Core Deflator (y/y%)	Sep	3.7	3.6	01:30
US	Chicago PMI	Oct	63.5	64.7	02:45
CH	Non-manufacturing PMI	Oct	53	53.2	14:00
CH	Manufacturing PMI	Oct	49.8	49.6	14:00

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	0.7201	+0.5	0.7168	0.7217	CHF	0.9119	-0.7	S&P 500	4,587	+0.8	40.2	Oil (Brent)	84.06	-0.6
AUD	0.7543	+0.4	0.7506	0.7556	SEK	8.519	-0.8	Dow	35,671	+0.5	34.5	Oil (WTI)	82.53	-0.2
EUR	1.1687	+0.7	1.1582	1.1692	NOK	8.328	-1.1	Nasdaq	15,412	+1.1	40.0	Gold	1802.9	+0.3
GBP	1.3795	+0.4	1.3730	1.3815	HKD	7.777	-0.0	Stoxx 50	4,234	+0.3	42.9	HRC steel	1798.0	+1.2
JPY	113.48	-0.3	113.26	113.75	CNY	6.392	-0.0	FTSE	7,249	-0.1	29.9	CRB	238.9	-0.9
CAD	1.2345	-0.1			SGD	1.344	-0.3	DAX	15,696	-0.1	35.8	Wheat Chic.	784.8	+1.5
NZD/AUD	0.9547	+0.1			IDR	14,173	+0.0	CAC 40	6,804	+0.3	48.9	Sugar	19.62	-0.4
NZD/EUR	0.6162	-0.3			THB	33.19	-0.3	Nikkei	28,820	-1.0	23.5	Cotton	113.28	+2.6
NZD/GBP	0.5220	+0.1			KRW	1,170	-0.1	Shanghai	3,518	-1.2	7.5	Coffee	200.0	-1.1
NZD/JPY	81.72	+0.2			TWD	27.80	+0.0	ASX 200	7,430	-0.2	24.7	WM powder	3950.0	+0.5
NZD/CAD	0.8890	+0.3			PHP	50.71	-0.0	NZX 50	12,971	-0.4	6.3	Australian Futures		
NZ TWI	76.13	+0.2										3 year bond	98.64	-0.12
												10 year bond	98.04	-0.14

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	0.68	1.59	USD	1.57	0.03	NZGB 5 1/2 04/15/23	1.60	0.09	1 year	1.64	0.09
AUD	0.10	0.06	1.11	2.11	AUD	1.84	0.03	NZGB 0 1/2 05/15/26	2.38	0.15	2 year	2.35	0.18
NZD	0.50	0.78	2.35	2.75	NZD	2.63	0.02	NZGB 0 1/4 05/15/28	2.49	0.10	5 year	2.70	0.11
EUR	0.00	0.06	-0.25	0.25	GER	-0.14	0.04	NZGB 1 1/2 05/15/31	2.59	0.04	7 year	2.72	0.07
GBP	0.10	0.20	1.22	1.20	GBP	1.01	0.02	NZGB 2 05/15/32	2.63	0.02	10 year	2.75	0.04
JPY	-0.05	-0.08	0.02	0.14	JPY	0.09	-0.01	NZGB 1 3/4 05/15/41	2.91	0.00	15 year	2.85	0.01
CAD	0.25	0.47	1.53	2.13	CAD	1.66	0.05	NZGB 2 3/4 05/15/51	3.01	-0.02			

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

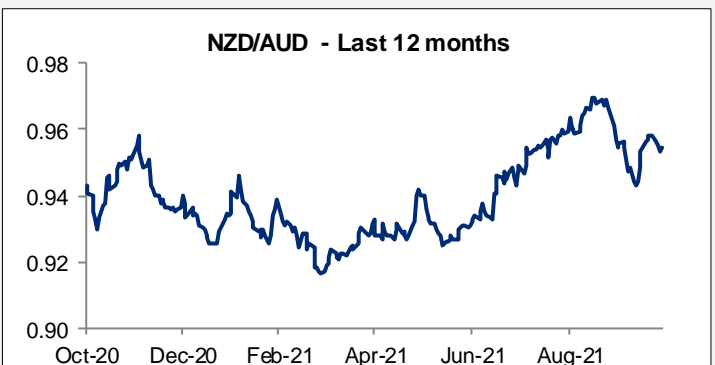
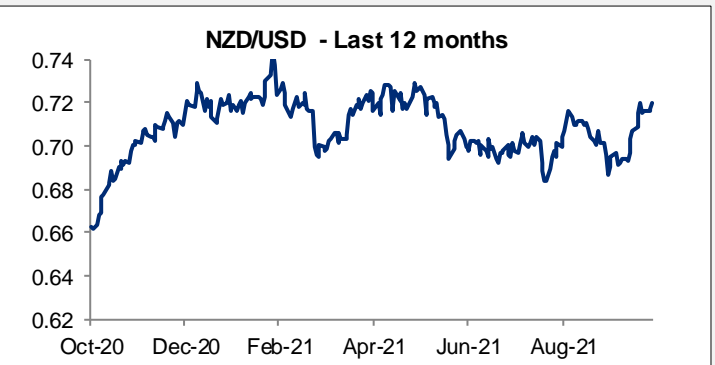
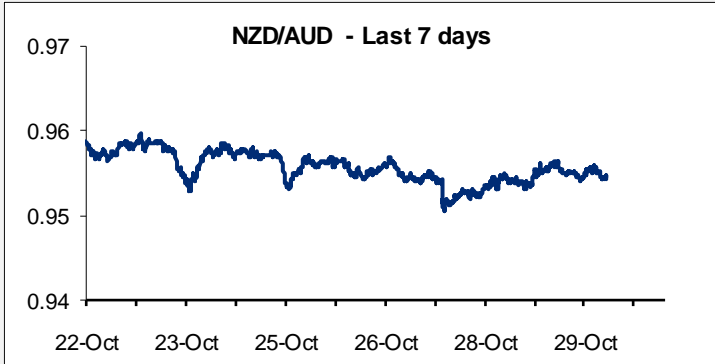
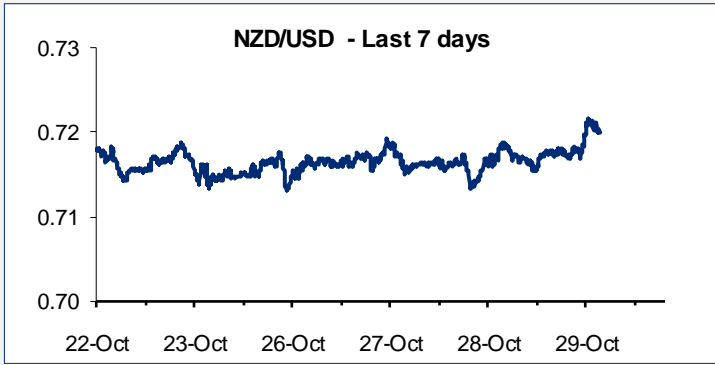
** All near futures contracts, except CRB. Metals prices are CME.

Rates are as of: NZT 06:51

Source: Bloomberg

NZD exchange rates

29/10/2021 6:50 a.m.		Prev. NY close
USD	0.7201	0.7168
GBP	0.5220	0.5215
AUD	0.9547	0.9536
EUR	0.6162	0.6178
JPY	81.72	81.59
CAD	0.8890	0.8859
CHF	0.6567	0.6582
DKK	4.5837	4.5956
FJD	1.4875	1.4841
HKD	5.6004	5.5750
INR	53.95	53.73
NOK	5.9967	6.0360
PKR	123.85	125.58
PHP	36.52	36.36
PGK	2.5356	2.5186
SEK	6.1343	6.1537
SGD	0.9680	0.9665
CNY	4.6027	4.5821
THB	23.97	23.92
TOP	1.5896	1.5876
VUV	78.93	78.63
WST	1.8210	1.8140
XPF	73.92	73.66
ZAR	10.8972	10.8116



NZD/USD Forward Points

	BNZ buys NZD	BNZ sells NZD
1 Month	-3.17	-2.82
3 Months	-12.45	-11.94
6 Months	-31.72	-30.46
9 Months	-60.56	-58.56
1 Year	-94.85	-92.85

NZD/AUD Forward points

	BNZ buys NZD	BNZ Sells NZD
1 Month	-5.40	-4.65
3 Months	-17.82	-16.39
6 Months	-33.62	-30.45
9 Months	-58.61	-53.42
1 Year	-82.14	-77.03

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