Research

Financial Markets Wrap

1 May 2024

NZD remained soft in April

- **Positive inflation surprises in the US drove higher rates, spilling into other markets, and a broadly stronger USD**
- **The NZD hit fresh lows against the USD and AUD, but with modest net depreciation overall**
- **JPY was the weakest major by far, following higher global rates and the BoJ remaining dovish; NZD/JPY rose almost 3%**

Quick Outlook		April ranges
NZD/USD	The NZD looks oversold under 0.60 on our models, but it's hard to rule out further modest weakness over the short-term. Fed rate pricing remains a key force. Ultimately, a higher NZD/USD is still projected through the second half of the year and into next year.	0.5855 – 0.6080
NZD/AUD	Despite fresh 10-month lows, we remain bearish for the year ahead, based on NZ's poor economic performance relative to Australia. This will be more obvious as NZ's unemployment rate climbs much faster than Australia's. Targeting a sustained sub-90 cross rate later this year.	0.9080 - 0.9205
NZD/GBP	The BoE could be cutting rates ahead of the RBNZ but we don't have a strong directional bias and continue to see some consolidation in the cross in the high 0.40s.	0.4715 - 0.4800
NZD/EUR	The ECB is likely to be cutting rates ahead of the RBNZ (from June), but we don't have a strong directional bias and see some consolidation in the cross near current levels within its now-familiar range.	0.5515 – 0.5605
NZD/JPY	The BoJ remains overly dovish in our view, contributing to a very weak yen. Cross is subject to large swings as ongoing intervention risk overhangs the market. Ultimately we see the cross heading lower on a sustained basis.	90.0 – 95.4

There were a number of cross currents driving markets in April. Higher than expected US inflation drove a paring of Fed rate cut expectations, which spilled over into other markets. Global rates rose to fresh highs for the year in many nations. In the mix was a rise in Middle East tensions. The USD was broadly stronger, with Fed pricing remaining a key driving force. The NZD closed the month down nearly 1½% after falling to a fresh low for the year. JPY was the weakest major by far, falling over 4%.

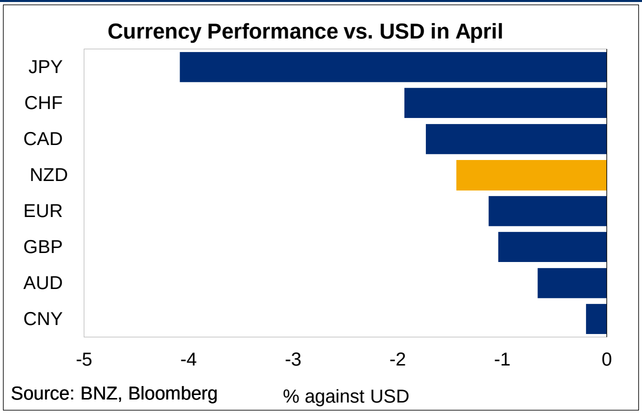
There was increased tension in the Middle East after Israel bombed the Iranian consulate in Syria. This resulted in a tit-for-tat response, with Iran launching a barrage of drones and missiles directly into Israel from Iranian soil, for the first time ever. Israel responded with a few drones launched into Iran. Both latter attacks appeared to have been largely symbolic, with no real intent to inflict serious damage, with neither side seeking a major war. Nevertheless, the tensions caused some market volatility, with Brent crude temporarily trading at a six-month high above USD92 per barrel, before ending the month barely higher just below USD88. The NZD hit a fresh low for the year of 0.5852 amidst the drama.

A fundamental driving force for markets was the reassessment of prospects for easier global monetary policy after US CPI data positively surprised for the third consecutive month, with ongoing signs of persistent inflation pressure in the services sector. The pick-up in inflation in Q1 was evident in the core PCE deflator released near the end of the month, showing inflation running at an annualised 3.7% for the quarter, miles above the 2% target, and the higher employment cost index. These data were a blow for expectations of a Fed rate cut in June or even July. By month-end, not even a full cut was priced for November, with 28bps cumulatively priced for December, the smallest amount all year. US Treasury yields traded at fresh highs for the year, with the 2-year rate closing the month up 41bps to 5.04% and the 10-year rate up 48bps to 4.68%.

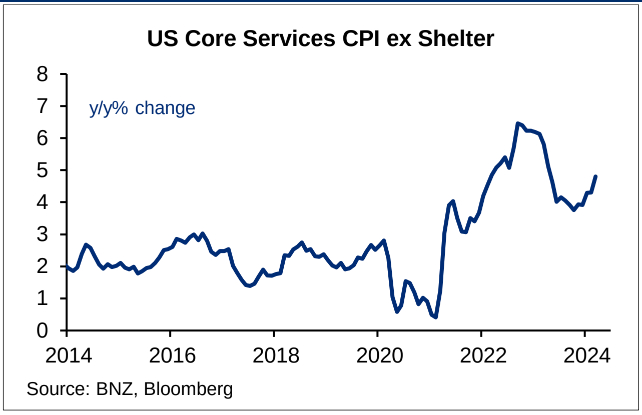
US economic activity data were mixed. On the strong side were another blockbuster non-farm payrolls gain of +303k, the ISM manufacturing index rising to an 18-month high of 50.3 and much stronger than expected retail sales. On the weak side, the ISM services index fell, small business optimism was at its weakest in more than 11-years, and US Q1 GDP rose an annualised 1.6%, the softest quarter in nearly two years. The US composite PMI for April fell to 50.9, against a backdrop of stronger composite PMIs across Europe. These data suggested a closing of relative growth performance between the US and Europe.

While there was no Fed policy meeting during the month, there was plenty of hawkish Fed-speak to absorb. Chair Powell said recent data showed a lack of further progress on inflation and therefore it was appropriate to let restrictive policy take further time to work. A couple of Fed speakers weren't shy about raising the possibility – however remote – of another policy rate increase.

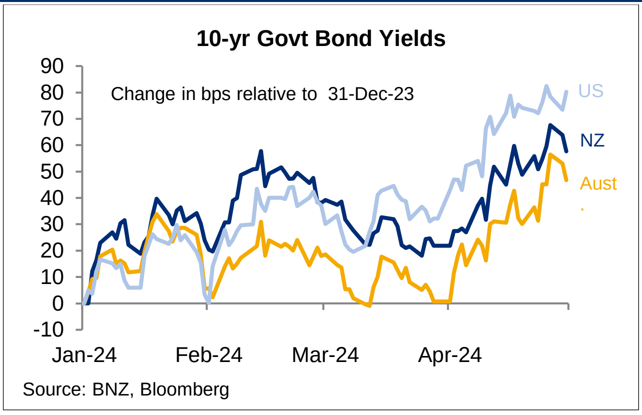
USD broadly stronger in April; JPY clearly underperformed



US inflation heading in the wrong direction again



Higher rates across the world, new highs for the year



Higher US rates spilled over into other markets, with investors paring rate cut expectations elsewhere across the world – the logic being that other major central banks would be factoring in the timing and scope of Fed easing into their own policy deliberations. Higher rates were a headwind for global equity market performance, with the MSCI World Index breaking a run of strong gains to post a loss of 3.2% for the month.

In domestic economic news, NZ CPI inflation data were in line with expectations, up 0.6% q/q and 4.0% y/y, with further progress in getting annual headline and core inflation down to 2½ to 3-year lows. However, the market took notice of higher services and non-tradeables inflation.

There was nothing in the data that would have the RBNZ scurrying to bring forward its rate cut agenda.

The real side of the economy remained very weak. The QSBO showed broadly weaker activity indicators, consistent with recessionary conditions, and rising slack in the economy that should ultimately lead to much weaker inflation pressure. Inflation gauges continued to move in the right direction, albeit remaining higher than would be consistent with annual inflation at the RBNZ's target midpoint. NZ's performance of services index slumped by an unusually large 5.1pts to 47.5, the weakest level outside of the COVID lockdowns since 2009, consistent with economic recession conditions lingering into Q1. ANZ's monthly surveys showed weaker business and consumer confidence, both consistent with growth well below trend.

The RBNZ kept the OCR on hold at 5.5% and delivered a message that there was little change from its economic outlook and assessment of risks compared to February. This cut and paste view was widely anticipated by most, but the update disappointed some offshore players who were looking for a dovish pivot.

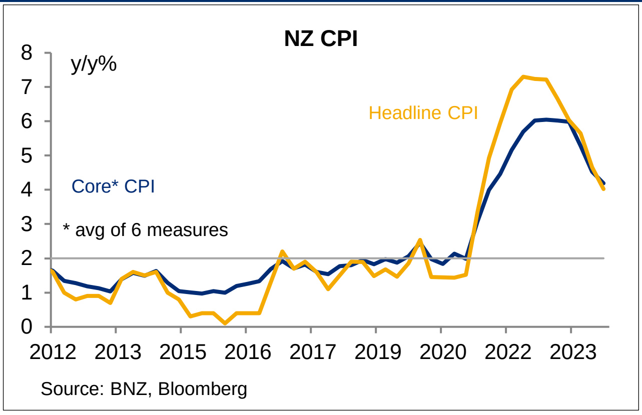
Global forces were the main force driving NZ rates higher. At month end, some 35bps of rate cuts were cumulatively priced by the last meeting of the year (November), compared to 70bps of easing priced at the start of the month. Swap rates closed the month 30-40bps higher, while the 10-year NZGB yield was 30bps higher at 4.90%.

In currency markets, the largest mover was the yen. The backdrop of higher US Treasury yields resulted in further yen depreciation and a dovish BoJ update towards the end of the month was another factor. The Bank didn't signal a reduction of its bond purchases, saying its stance was largely unchanged from March, and there was some determination to keep policy highly accommodative. Governor Ueda seemed unbothered by JPY weakness, adding to selling pressure. USD/JPY effortlessly charged higher, with no effort by the MoF to intervene until USD/JPY breached 160, the highest level since 1990. Intervention helped the yen recover, but USD/JPY still ended the month up over 4% to 157.80. NZD/JPY breached 95 for the first time since 2007 and closed the month nearly 3% higher at 92.8.

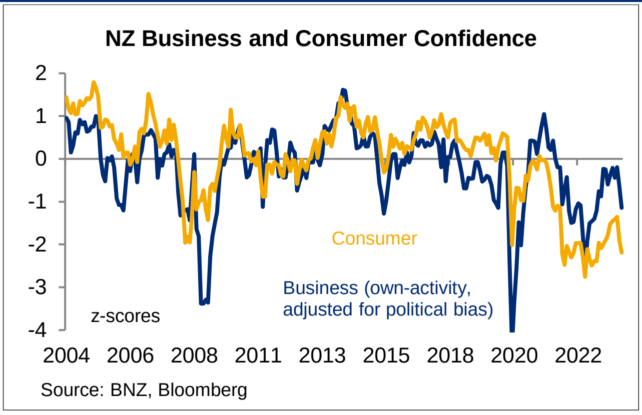
There were various conflicting forces in play affecting the NZD during April. On the positive side, a global reflation trade of sorts was in action, associated with higher global yields and commodity prices. Data showed a decisive lift in global manufacturing PMIs around the world, suggesting an upswing for the economic cycle in play, a supporting factor for the NZD that helped limit losses against a broadly stronger USD for the month. Bloomberg's spot commodity price index rose nearly 6% in April, adding to the 3% gain in March.

NZD/USD traded a high of 0.6083 on 10-April, just ahead of the positive US CPI print and thereafter heightened

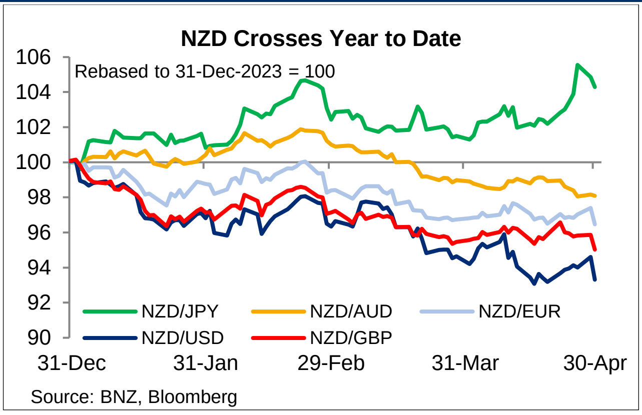
NZ CPI inflation high still high, but heading lower



NZ business and consumer confid. remain well below par



NZD up vs. JPY year-to-date, down versus the others



tensions in the Middle East were a drag. The NZD traded a fresh low for the year of 0.5852 on 19-April when Middle East tensions were at their peak. After staging a modest recovery, strong US wages data near month-end sent the NZD down again and it closed the month around 0.5890, down 1.4%.

The AUD showed a more modest fall against the USD. In addition to the factors that affected the NZD noted above, Australian CPI data were hotter than expected, raising a debate of whether the RBA might have to hike rates again this cycle. The market moved from pricing in rate cuts later in the year to some chance that the next move could actually be a hike. NZD/AUD fell to a 10-month low of

0.9080, before closing the month down nearly 1% to just under 0.91.

The NZD fell slightly against the EUR and GBP, down less than ½%. The ECB kept policy rates on hold and still seemed comfortable in signalling a June rate cut, following an updated assessment of the inflation outlook, even if the official line is that the Bank is not pre-committing to any particular rate view. GDP grew 0.3% q/q in Q1, breaking a string of negative to zero growth quarters while CPI inflation continued to head lower.

The UK economy showed similar dynamics, with signs of improved economic momentum and lower inflation. BoE Governor Bailey said the UK is still in the midst of a “pronounced period” of disinflation and the UK remained “pretty much on track” compared with the BoE’s February inflation forecast. He reiterated that each policy meeting is “in play” as policymakers judge progress towards the BoE’s 2% target each time it meets.

CNY only fell slightly against the USD with the PBOC active in preventing further yuan weakness. Chinese activity data were mixed, consistent with sluggish growth by usual Chinese standards.

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Monthly Performance Table

	end-Apr	end-Mar	Change
Currencies			
NZD/USD	0.5887	0.5973	-1.4%
NZD/AUD	0.9094	0.9166	-0.8%
NZD/EUR	0.5519	0.5537	-0.3%
NZD/GBP	0.4712	0.4732	-0.4%
NZD/JPY	92.83	90.38	2.7%
NZD/CNY	4.264	4.310	-1.1%
TWI	70.0	70.3	-0.5%
AUD/USD	0.6473	0.6516	-0.7%
EUR/USD	1.0666	1.0788	-1.1%
GBP/USD	1.2492	1.2623	-1.0%
USD/JPY	157.82	151.38	4.3%
USD/CNY	7.24	7.23	0.2%
USD/CAD	1.3779	1.3541	1.8%
USD DXY	106.22	104.49	1.7%
Asia dollar index	90.18	91.03	-0.9%
Equity Markets			
MSCI AC Wrld, loc.	2,108	2,168	-2.7%
MSCI World, loc.	12,072	12,470	-3.2%
MSCI EM, USD	2,718	2,705	0.5%
US S&P 500	5,036	5,254	-4.2%
Euro STOXX 600	504.9	512.7	-1.5%
Germany DAX	17,932	18,492	-3.0%
France CAC 40	7,985	8,206	-2.7%
UK FTSE 100	8,144	7,953	2.4%
Aust S&P/ASX 200	7,664	7,897	-2.9%
Japan Topix	2,743	2,769	-0.9%
China CSI 300	3,604	3,537	1.9%
NZX50	11,958	12,105	-1.2%
Volatility: VIX	15.65	13.01	20.3%
3-mth Bill Futures			
NZD Sep-24	94.47	94.78	-0.31
AUD Sep-24	95.53	95.86	-0.33
USD Sep-24	94.80	95.14	-0.34
EUR Sep-24	96.50	96.68	-0.19
GBP Sep-24	95.07	95.32	-0.25
CAD Sep-24	95.07	95.17	-0.09

	end-Apr	end-Mar	Change
NZ Rates			
OCR	5.50	5.50	0.00
NZ 90day BB	5.63	5.64	0.00
NZ 2yr swap	5.11	4.80	0.31
NZ 5yr swap	4.69	4.30	0.40
NZ 10yr swap	4.77	4.37	0.40
NZ Govt (5/26)	4.92	4.60	0.32
NZ Govt (4/29)	4.72	4.37	0.35
NZ Govt (5/34)	4.90	4.60	0.30
NZ Govt (5/41)	5.16	4.88	0.28
Global 10 year bond rates			
US	4.68	4.20	0.48
Canada	3.82	3.47	0.35
UK	4.35	3.93	0.41
France	3.05	2.81	0.25
Germany	2.58	2.30	0.29
Italy	3.92	3.68	0.24
Spain	3.35	3.16	0.19
Portugal	3.20	2.99	0.21
Ireland	2.96	2.74	0.22
Japan	0.87	0.72	0.15
Australia	4.42	3.96	0.46
Commodities (USD)			
WTI Crude	81.93	83.17	-1.5%
Brent Crude	87.86	87.48	0.4%
R/B CRB Index	291.5	290.3	0.4%
Gold spot	2,286	2,230	2.5%
Silver spot	26.29	24.96	5.3%
Copper	456.5	400.7	13.9%
Iron Ore	117.47	100.78	16.6%
Thermal coal	142.25	129.10	10.2%
Corn	446.8	454.5	-1.7%
Wheat	603.3	575.8	4.8%
SGX-NZX Dairy WMP	3,125	3,150	-0.8%
SGX-NZX Milk Price '24	7.84	7.81	0.4%

Source: BNZ, Bloomberg

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