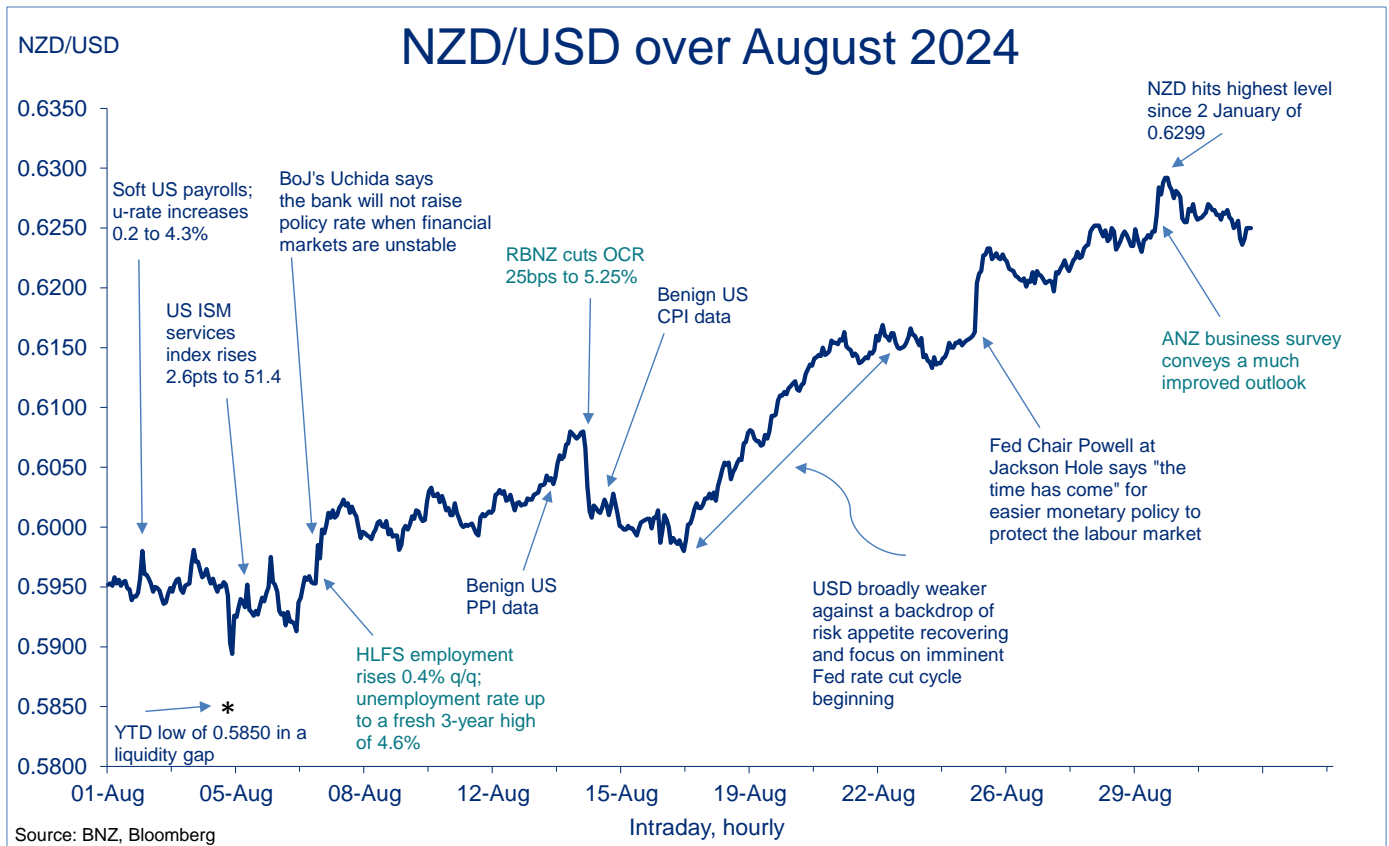


Financial Markets Wrap

31 August 2024

August ascent after July jolt for NZD

- After a volatile start, calm was restored to markets in August; by month-end the episode was long-forgotten.
- Despite the RBNZ significantly bringing forward the rate cutting cycle, the NZD outperformed, rising 5% against the USD.
- NZD crosses were all stronger, making up for the poor performance over July; NZD/JPY traded a range of over 8 big figures.



Quick Outlook		August ranges
NZD/USD	After the strong recovery through August, the NZD is due for a breather over the short-term. The US employment report at the end of the first week of September is the next key risk event, which could determine the size of the Fed's first rate cut later in the month.	0.5850 – 0.6300
NZD/AUD	In a consolidation mode but we see risks skewed lower into year-end based on NZ's much weaker economy relative to Australia, manifested in a rising unemployment rate differential and lower NZ-AU rate spreads.	0.9045 – 0.9260
NZD/GBP	Further consolidation expected. Slightly more upside than downside risk over the next six months, given the extent of easing already priced into the NZ curve relative to the UK.	0.4600 – 0.4765
NZD/EUR	Back to mid-range after a wild swing through July/August. We continue to have little conviction on direction and continue to see a range-trading environment.	0.5365 – 0.5665
NZD/JPY	Apt to consolidate further after the tumble through July. Further BoJ tightening likely against the global trend over the coming year is yen supportive. Still look for further downside in the cross over the medium-term. Volatile trading conditions could linger into year-end.	83.1– 91.4

Markets were volatile in August in the wake of the BoJ’s end-July rate hike and some soft US economic data. The NZD traded a wider than usual range of 4½ cents, with a strong performance over the second half leading to an overall gain of 5% against the USD, despite further falls in NZ rates after the RBNZ kicked off the easing cycle earlier than some expected.

August began on a volatile note in the wake of the end-July BoJ rate hike and associated hawkish rhetoric and soft US economic data, with initial jobless claims rising to their highest level in a year, the ISM manufacturing index falling to 48.6, and a particularly meaty 6-point fall in the employment component to 43.4, the worst reading since the GFC, excluding COVID. These raised concerns about a hard economic landing for the US and the Fed being too slow to commence an easing cycle.

During a period of market turmoil, Japan’s Nikkei-225 equity index fell 20% over three days, the VIX index rose above 60 intraday (a level normally associated with a crisis, surpassed only during the GFC and the height of the COVID-shock), and the US 10-year Treasury yield fell as much as 40bps over three trading days. Currency markets were tame by comparison apart from significant volatility in the yen, although during the turmoil, the NZD managed to trade at a year-to-date low of 0.5850 during a liquidity vacuum. Following a week of volatility, market conditions calmed and by month-end the episode was long forgotten.

US economic data releases were mixed overall. Initial jobless claims receded and by month-end the four-week moving average was looking like a plateau rather than suggesting any further deterioration in the labour market. Non-farm payrolls increased by only 114k in July and the unemployment rate increased from 4.1% to 4.3%; above the consensus for no change. The move higher triggered a widely followed recession indicator, the Sahm rule, which occurs when the 3-month average unemployment rate jumps more than 0.5% points in a year. Later in the month, the Bureau of Labor Statistics reported that US payroll growth in the year to March was preliminarily revised down by 818k.

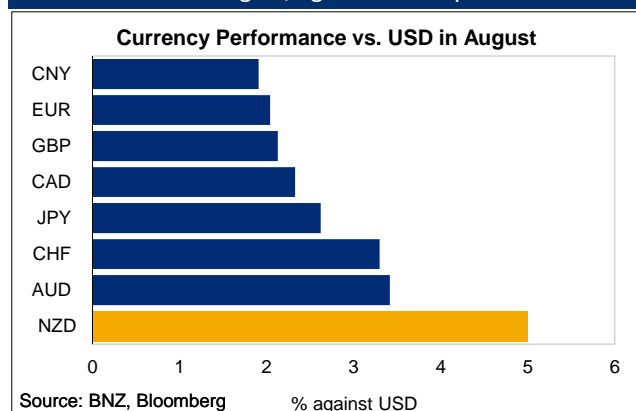
On the positive side of the ledger, the US services ISM rebounded to 51.4 in July from contractionary territory in June, which eased fears about the extent of the economic slowdown and helped to stabilise market sentiment. Stronger than expected US retail sales further dispelled concerns the economy was entering a deeper slowdown. Inflation data were benign, with PPI and CPI data consistent with the disinflationary process continuing. The core CPI increased 3.2% y/y, the slowest annual pace since early 2021.

Minutes of the end-July FOMC meeting suggested several Fed officials saw a case for cutting at the meeting before unanimously voting to keep them steady. The ‘vast majority’ of policy makers observed that if the data continued to evolve as expected, then it would be appropriate to ease at

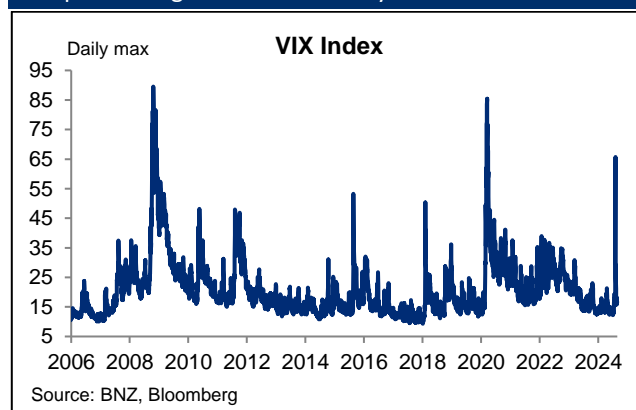
the September meeting. Chair Powell’s Jackson Hole speech will be remembered for him giving the all-clear to begin the easing cycle in September, viz “the time has come for policy to adjust” and realigning the focus of monetary policy on the protection of the labour market rather than concern about inflation.

As noted, US Treasuries traded wide ranges over the month, most of that being in the first few trading days. The 10-year rate closed the month down 13bps at 3.90% with a steeper curve, with the 2s10s gap narrowing towards zero. By month-end, the market was pricing in 100bps of rate cuts through the remaining three meetings of the year, implying a high likelihood of a jumbo 50bps cut at one of the meetings.

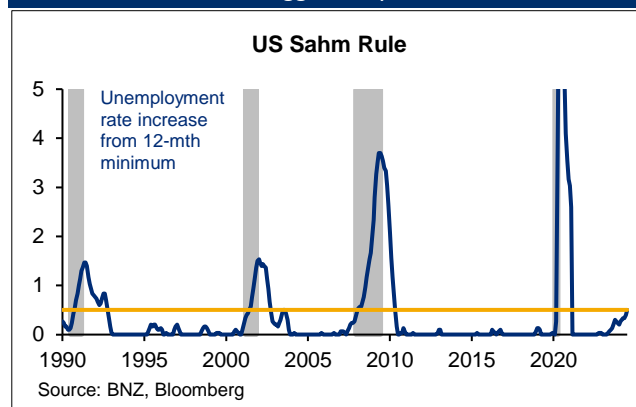
NZD stands out in August, against broadly weaker USD



VIX spike in August was historically extreme



US recession indicator triggered by Sahm Rule



In domestic economic news, NZ's PMI and PSI both rose in July, but from rock-bottom levels and still signalling that NZ's economic recession continues unabated. Retail sales data confirmed the dire conditions facing the sector, with real sales down 1.2% q/q, making it nine contractions out of the past ten quarters. The Household Labour Force Survey showed the unemployment rate rising to a fresh three-year high of 4.6%. While employment surprisingly rose by 0.4% q/q, the first quarterly contraction in hours worked in almost three years – down a notable 1.2% q/q – and a 0.5% fall in filled jobs measured by the separate QES both seemed more consistent with the message from previously released labour market indicators. At the end of the month, the ANZ's business outlook survey showed a further lift in forward-looking indicators, providing some hope that the economy will be out of recession towards the end of the year.

The RBNZ cut the OCR by 25bps to 5.25%, with the statement noting headline inflation is returning to the Bank's target band and weak activity is contributing to rising spare capacity in the economy. The Bank's projections showed a steady fall in the OCR towards neutral, around 3%. Given uncertainty about the RBNZ's reaction function, the move wasn't fully priced, and it paved the way for lower NZ rates and NZ-global rate spreads.

NZ's 2-year swap rate closed the month down 29bps to 3.94%, while the 10-year rate fell 6bps to 4.01%. At month-end, the market was pricing in 73bps of cuts over the remaining two meetings of the year and cumulatively over 200bps of rate cuts through to the end of 2025.

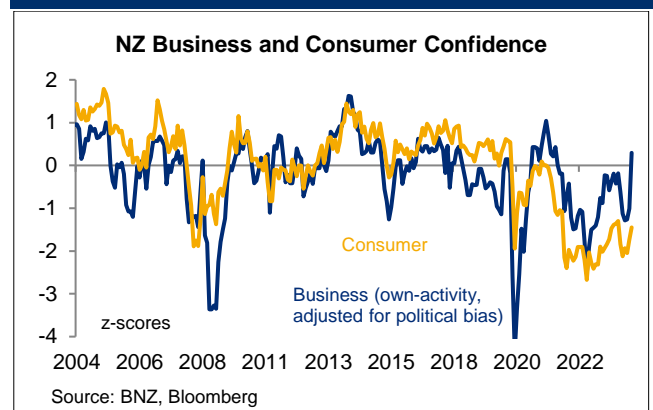
A key theme for the currency market was a broad-based fall in the USD in anticipation of the Fed's rate cutting cycle, seeing the DXY index down 2.3% for the month, trading at its lowest level this year towards the end of the month. The NZD was the strongest of the majors, with NZD/USD up 5% to 0.6250. Its outperformance looks odd in the face of the RBNZ significantly bringing forward its rate cutting cycle, but global forces predominated, and it followed the NZD's underperformance during July. The low for the month (and year) was 0.5850 on 5 August during a liquidity vacuum, while the high of 0.6299 was recorded on 29 August, in the wake of risk appetite recovering, Fed Chair delivering his "the time has come" speech at Jackson Hole, and a strong ANZ business outlook survey.

NZD/AUD rose by over 1½% to 0.9240. The RBA delivered a more hawkish policy update than widely anticipated, maintaining previous language that data "have reinforced the need to remain vigilant to upside risks to inflation" and the Board "is not ruling anything in or out". Governor Bullock pushed back against market pricing of near-term risk of rate cuts, saying that it "doesn't align with the Board's current thinking" and that markets "are a bit ahead of themselves". The RBA minutes said that the Board was "placing somewhat greater-than-usual weight on the flow of data, relative to the forecasts", opening the

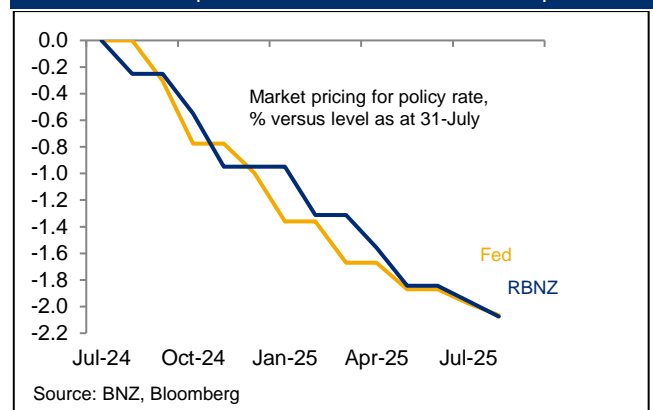
door to a dovish pivot on cooperative inflation data and signs of a weaker than expected economy.

The NZD rose nearly 3% against the EUR and GBP. The Bank of England kicked off an easing cycle with a 25bps cut to the policy rate to 5.0%, but it was a finely balanced decision with a 5-4 vote by MPC to cut rates. The Bank said it was now appropriate to slightly reduce the degree of policy restrictiveness, and it maintained the line that policy "will need to continue to remain restrictive for sufficiently long...". Governor Bailey didn't offer any view on the rate path ahead and said it will take a meeting-by-meeting approach, noting that they will be careful not to cut interest rates too quickly or too much.

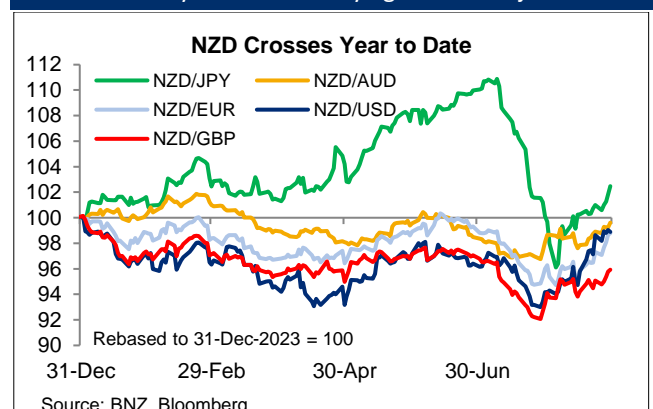
A notable lift in NZ business confidence



RBNZ and Fed expected to be on similar rate cut paths



Decent recovery in NZD recently against all majors



Euro area data continued to show that Germany's economy was struggling to grow. ECB's survey of wages showed negotiated pay rose by only 3.6% y/y in Q2, down from 4.7% in Q1. CPI data showed annual inflation falling to a three-year low of 2.2%. The market fully priced a second 25bps rate cut by the ECB in September.

The yen remained volatile in the wake of the BoJ's end of July rate hike and guidance for further hikes. While BoJ deputy Governor Uchida's comments got the market's attention when he said, "the bank will not raise its policy interest rate when financial and capital markets are unstable", later comments by other key BoJ policy makers stuck to the game plan, expressing the likely need for

further policy normalisation. NZD/JPY rose 2½% to 91.4, to the top of a massive range for the month of 83.1-91.4.

Against the backdrop of a weaker USD, USD/CNY fell nearly 2% to 7.09 and the prior significant downward pressure on the yuan was extinguished, requiring no further work by the PBoC to actively manage the pressure. Key monthly indicators continued to point to sluggish activity in the Chinese economy with weak domestic demand amid a prolonged downturn in the housing market.

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Monthly Performance Table							
	end-Aug	end-Jul	Change		end-Aug	end-Jul	Change
Currencies				NZ Rates			
NZD/USD	0.6249	0.5951	5.0%	OCR	5.25	5.50	-0.25
NZD/AUD	0.9237	0.9096	1.6%	NZ 90day BB	5.23	5.46	-0.23
NZD/EUR	0.5656	0.5495	2.9%	NZ 2yr sw ap	3.94	4.23	-0.29
NZD/GBP	0.4759	0.4629	2.8%	NZ 5yr sw ap	3.75	3.89	-0.14
NZD/JPY	91.35	89.23	2.4%	NZ 10yr sw ap	4.01	4.07	-0.06
NZD/CNY	4.432	4.301	3.1%				
TWI	71.8	69.9	2.7%	NZ Govt (5/26)	4.10	4.34	-0.24
AUD/USD	0.6765	0.6542	3.4%	NZ Govt (4/29)	3.87	4.03	-0.16
EUR/USD	1.1048	1.0827	2.0%	NZ Govt (5/34)	4.27	4.34	-0.07
GBP/USD	1.3129	1.2855	2.1%	NZ Govt (5/41)	4.65	4.73	-0.09
USD/JPY	146.19	150.03	-2.6%				
USD/CNY	7.09	7.23	-1.9%	Global 10 year bond rates			
USD/CAD	1.3493	1.3807	-2.3%	US	3.90	4.03	-0.13
USD DXY	101.70	104.10	-2.3%	Canada	3.16	3.16	0.00
Asia dollar index	92.78	90.72	2.3%	UK	4.01	3.97	0.05
				France	3.02	3.01	0.01
Equity Markets				Germany	2.30	2.30	0.00
MSCI AC Wrld, loc.	2,310	2,271	1.8%	Italy	3.70	3.65	0.05
MSCI World, loc.	13,278	13,030	1.9%	Spain	3.13	3.11	0.02
MSCI EM, USD	2,901	2,854	1.6%	Portugal	2.90	2.92	-0.01
US S&P 500	5,648	5,522	2.3%	Ireland	2.67	2.69	-0.02
Euro STOXX 600	525.1	518.2	1.3%	Japan	0.89	1.05	-0.16
Germany DAX	18,907	18,509	2.2%	Australia	3.97	4.12	-0.15
France CAC 40	7,631	7,531	1.3%				
UK FTSE 100	8,377	8,368	0.1%	Commodities (USD)			
Aust S&P/ASX 200	8,092	8,092	0.0%	WTI Crude	73.55	77.91	-5.6%
Japan Topix	2,713	2,794	-2.9%	Brent Crude	78.80	80.72	-2.4%
China CSI 300	3,321	3,442	-3.5%	R/B CRB Index	277.0	278.1	-0.4%
NZX50	12,448	12,405	0.3%	Gold spot	2,503	2,448	2.3%
Volatility: VIX	15.00	16.36	-8.3%	Silver spot	28.86	29.01	-0.5%
				Copper	414.5	417.7	-0.8%
3-mth Money Market Futures				Iron Ore	101.03	100.63	0.4%
NZD Mar-25	95.86	95.66	0.20	Thermal coal	146.20	140.10	4.4%
AUD Mar-25	96.13	95.94	0.19	Corn	401.0	399.8	0.3%
USD Mar-25	96.25	95.80	0.45	Wheat	551.5	552.0	-0.1%
EUR Mar-25	97.39	97.22	0.17	SGX-NZX Dairy WMP	3,595	3,030	18.6%
GBP Mar-25	95.85	95.69	0.16	SGX-NZX Milk Price '25	8.90	8.45	3.6%
CAD Mar-25	96.67	96.45	0.23				
Source: BNZ, Bloomberg							

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