

Markets Monthly

Sharemarkets remain buoyant in May

- Sharemarkets around the world extended gains posted since the start of the rally in March.
- Government bond yields continue to rise, as investors focus on huge issuance programmes.
- NZD posted strong gains, lifting 6.9% on a trade weighted basis.

The strength in global equity markets continued through early May, with positive economic data driving stocks higher. In particular the data out of the US – home of the world's number one consumers - showed decidedly less pessimism, with sentiment posting the biggest one month increase in over two years. US construction spending recorded the first increase in six months. The US housing sector and labour market figures added to the flow of positive economic indicators over the month. This could be the first sign that the billions of dollars for capital projects included in the US \$787 billion stimulus package are having an impact.

The US banking sector held the limelight in early May. Banking stocks rose as leaks on bank stress tests suggested that banks would not have to raise added capital immediately. Over the first week of May the Dow Jones Industrial Average share index rallied 5% to a near four-month high.

The second half of May was a bit more subdued, with investors taking stock of the recent rally in equity markets. Concerns over rising US Government Bond yields weighed on markets after S&P downgraded the credit outlook for the UK economy saying that Britain's outlook was "negative and no longer stable".

However, equity markets managed to close the month on a positive note with the US S&P 500 up 5.3% for May. In contrast, the Australasian sharemarkets posted more modest gains in May.

The Federal Open Market Committee of the United States did not increase the US\$300bn amount it will purchase of US Treasury securities (initially announced on March 18) at its April 29th meeting. Investor concerns about the huge amount of government bond issuance in the coming years are pushing yields higher globally. A sharp sell-off in Treasuries saw the yield on the US 10-year note peaked 3.75% on 29th May.

The USD weakened over the month, and the NZD posted strong gains on the cross rates we monitor, lifting 6.9% on a trade weighted basis.

The NZ sharemarket lifted a subdued 0.4% in May. The big local event was the Government Budget on 28 May. There was a lot riding on this Budget, particularly whether it would be enough to avoid a potentially expensive sovereign credit rating downgrade. It would appear the Government has been successful, with Standard and Poor's putting NZ's credit rating outlook back to stable.

Date	Instrument	31-May-09	Month %	Quarter %	Year %	5-Year %
Cash	NZ cash rate	2.50	0.00	-1.00	-5.75	-3.00
	NZ 90-day bank bill	2.75	-0.10	-0.44	-5.96	-3.20
	US 90-day bank bill	0.67	-0.36	-0.59	-2.01	-0.63
	NZ - US 90-day bank bill	2.08	0.26	0.15	-3.95	-2.57
Fixed Interest	NZ 5-year gov't stock	4.55	0.30	0.68	-2.02	-1.54
	NZ 10-year gov't	5.77	0.44	1.26	-0.72	-0.48
	NZ 10-year swap	5.95	0.58	1.09	-1.61	-0.90
	AUS 10-year gov't	5.49	0.74	1.14	-1.05	-0.38
	US 10-year gov't	3.61	0.53	0.63	-0.44	-1.05
Equities	NZ - NZX50 (NZ\$)	1888	0.4%	6.8%	-28.2%	-27.3%
	AUS - All Ords (A\$)	3813	1.8%	15.7%	-34.0%	10.3%
	JAP - Nikkei (¥)	9523	7.9%	25.8%	-33.6%	-15.3%
	UK - FT100 (£)	4418	4.1%	15.3%	-27.0%	-0.3%
	US - S&P500 (US\$)	919	5.3%	25.0%	-34.4%	-18.0%
	WORLD - MSCI (US\$)	970	8.6%	29.2%	-36.4%	-7.0%
	MSCI in NZD (NZ\$)	1546	-2.2%	4.0%	-21.0%	-6.4%
Exchange Rates	NZD/USD	0.628	11.0%	24.2%	-19.6%	-0.6%
	NZD/AUD	0.796	2.1%	1.6%	-2.5%	-9.9%
	NZD/JPY	60.6	10.1%	22.9%	-26.3%	-12.4%
	NZD/GBP	0.393	2.9%	11.0%	-0.5%	14.3%
	NZD/EUR	0.449	5.5%	13.0%	-10.7%	-13.1%
	NZ TWI	0.598	6.9%	15.0%	-14.3%	-6.6%
	EUR/USD	1.398	5.3%	9.9%	-9.9%	14.4%

Equity indices are the respective end-of-month closes. Interest rates and exchanges rates are at 5pm NZ.

Chris Tennent-Brown – CBA NZ Economist – 649 374 8819 – chris.tennent-brown@asb.co.nz

General Advice Warning

As this report was prepared without taking into account your objectives, financial situation or particular needs, you should not take any action in reliance of this report without considering your particular circumstances and, if necessary, obtaining professional advice.

Cash

- On 30 April, the RBNZ delivered a 50bp cut to the Official Cash Rate (OCR). The RBNZ said it expects "to keep the OCR at or below the current level through until the latter part of 2010. The OCR could still move modestly lower over the coming quarters."
- 90-day bank bill yield eased during May, but the market pricing at present is consistent with the RBNZ most likely being on hold over the coming months.
- We expect the RBNZ will eventually cut further, with the easing cycle taking the OCR down to 2%. However, the RBNZ will likely keep the Official Cash Rate (OCR) on hold at 2.5% in June, and further cuts will be dependant on events in the coming months.
- Term deposit rates for longer time frames remained high in May.

Fixed interest

- The upward drift in government bond yields continued in May. There has been upward pressure on bond yields globally as markets anticipate a large increase in the supply of bond issuance from both corporates and governments.
- NZ 10-year Gov't Bond yields leapt a staggering 0.76% higher in March. In April the movement was a more modest 0.06% lift. In May, the 10-year yield lifted another 0.44%, to yield 5.74%.
- There was a lot riding on the New Zealand Government's Budget on May 28th, particularly whether it would be enough to avoid a potentially expensive sovereign credit rating downgrade. It would appear the Government has been successful, with Standard and Poor's putting NZ's credit rating outlook back to stable.
- S&P downgraded the credit outlook for the UK economy saying that Britain's outlook was "negative and no longer stable".
- The yield on the US 10-year note rose a huge 0.53% over May.

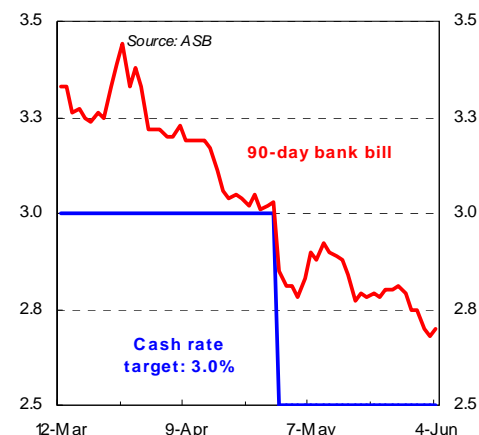
Equities

- The strength in global equity markets continued through early May, with positive economic data driving stocks higher.
- The US banking sector held the limelight in early May. Banking stocks rose as the bank stress tests results suggested that US banks would not have to raise added capital immediately.
- US equity markets managed to close the month on a positive note with the S&P 500 up 5.3% for May.
- The NZ sharemarket lifted a modest 0.4% in May. The local market peaked on 8th May, and shed most of the early gains by month-end. However, sentiment in the local market has been positive, and a number of successful capital raisings took place in the month.

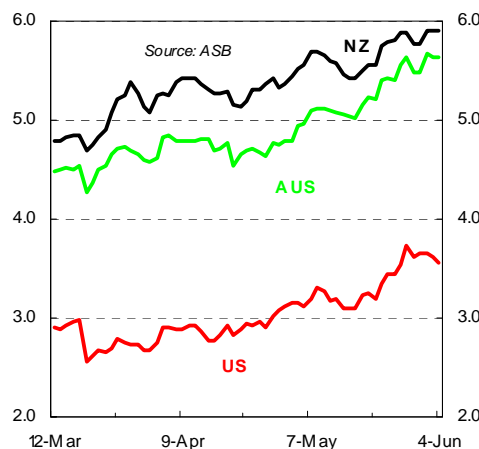
Exchange rates

- The USD continued in a downward trend over the month losing 4.9% on a major-currency TWI
- The New Zealand dollar (NZD) posted a solid 11% appreciation against the USD over the month, reaching its highest level since October 2008. In trade-weighted terms, the NZD appreciated 6.9%.
- The NZD outperformed all major currencies over the month.
- As with the AUD, the NZD received support from the combination of a softening USD and rising investor appetite for risk.
- The S&P sovereign credit rating outlook change from negative back to stable was unexpected and guided the NZD higher.
- As is the trend when markets become more confident, the NZD outperformed the AUD over the month of May, despite interest rate differentials remaining in Australia's favour.

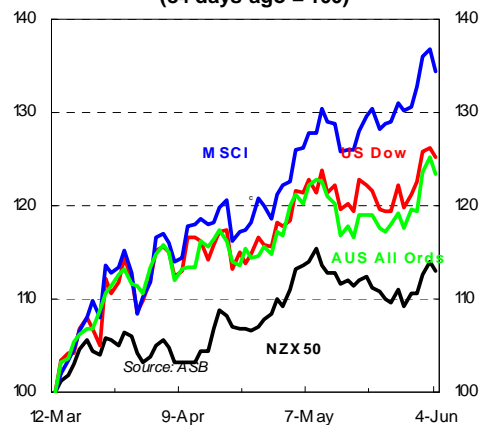
% p.a. NZ SHORT-TERM RATES



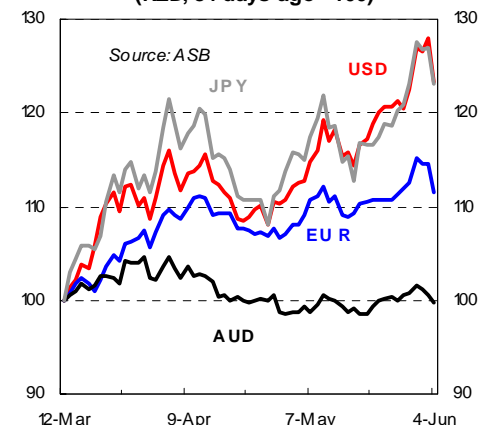
% p.a. 10-YEAR BOND YIELDS



SHARE INDICES
(84 days ago = 100)



EXCHANGE RATE INDICES
(NZD, 84 days ago = 100)



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ASB ECONOMICS
Level 9, 135 Albert Street, Auckland

ASB GROUP ECONOMICS			PHONE	FAX
Chief Economist	Nick Tuffley	nick.tuffley@asb.co.nz	(649)374 8604	
Economist	Jane Turner	jane.turner@asb.co.nz	(649) 374 8185	(649) 302 0992
CBA NZ Economist	Chris Tennent-Brown	chris.tennent-brown@asb.co.nz	(649) 374 8819	

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