

# Markets Monthly

## Sharemarkets press higher in July.

- After a weak start, sharemarkets around the world rallied and posted strong returns in July.
- US bond yields rose but remained below the 2009 highpoint reached in June.
- NZD posted gains on most currencies during July, lifting 0.3% on a trade-weighted basis.

Global equity markets dipped lower through the early part of July, with investors spooked by the unexpected drop in US consumer confidence. Consumer spending accounts for almost 70% of US economic activity (GDP) and the weaker reading added to concerns of a prolonged US recovery. Uncertainty over the US earnings season also weighed on markets. Over the first 10 days of July the S&P500 lost 4.4%. The turnaround in global equity markets came as the US reporting season kicked off. The better-than-expected result from Alcoa was the catalyst for earnings upgrades from analysts across an array of sectors. Banking stocks were the first beneficiaries, before resource, industrial and media stocks also received a boost.

The IMF also upgraded its forecasts for the global economy, and reasonable data on the US housing sector was the icing on the cake. The release of figures showing that the Chinese economy expanded 7.9 per cent (year on year) in the June quarter added to the recovery momentum. Interestingly the growth was fuelled by bank lending which hit a record 7.37 trillion Yuan in the first six months of 2009.

A record US\$115 billion auction of US treasuries in the last week of July was well supported, although US bond yields rose over the month. US GDP for the June quarter posted a much better than expected 1% annualised contraction, and investors concluded the US economy has bottomed.

Overall equity markets posted some of the best gains on record in July. The US S&P 500 gained 7.4%. The Australian All Ords index rallied by 7.6% over the month, marking the best monthly gain in almost 16 years. The NZX-50 beat both markets, by lifting 7.8%.

At the end of the month the RBNZ kept the OCR unchanged at 2.5%, and in its statement to the market focused on the downside risks to growth, with most discussion centred on the weakness in the export sector. A key signal from the RBNZ was the explicit willingness to "reassess policy settings" if the NZ dollar and wholesale interest rates remain at current levels.

As confidence in the global economic recovery improved, the NZD ground higher against the USD. The NZD trading around its highest rate since October 2008 towards the end of the month. We continue to expect the NZ dollar will be strong over the next year.

| Date           | Instrument               | 31-Jul-09 | Month % | Quarter % | Year % | 5-Year % |
|----------------|--------------------------|-----------|---------|-----------|--------|----------|
| Cash           | NZ cash rate             | 2.50      | 0.00    | 0.00      | -5.50  | -3.50    |
|                | NZ 90-day bank bill      | 2.79      | -0.03   | -0.06     | -5.53  | -3.54    |
|                | US 90-day bank bill      | 0.48      | -0.11   | -0.54     | -2.32  | -1.17    |
|                | NZ - US 90-day bank bill | 2.31      | 0.08    | 0.48      | -3.21  | -2.37    |
| Fixed Interest | NZ 5-year gov't stock    | 4.77      | 0.00    | 0.52      | -1.35  | -1.47    |
|                | NZ 10-year gov't         | 5.78      | -0.19   | 0.45      | -0.38  | -0.57    |
|                | NZ 10-year swap          | 5.98      | -0.06   | 0.61      | -1.13  | -1.03    |
|                | AUS 10-year gov't        | 5.71      | 0.07    | 0.96      | -0.49  | -0.13    |
|                | US 10-year gov't         | 3.64      | 0.13    | 0.55      | -0.40  | -0.95    |
| Equities       | NZ - NZX50 (NZ\$)        | 2050      | 7.8%    | 9.0%      | -14.9% | -26.5%   |
|                | AUS - All Ords (A\$)     | 4250      | 7.6%    | 13.5%     | -15.9% | 19.8%    |
|                | JAP - Nikkei (¥)         | 10357     | 4.0%    | 17.3%     | -22.6% | -8.6%    |
|                | UK - FT100 (£)           | 4608      | 8.5%    | 8.6%      | -14.8% | 4.4%     |
|                | US - S&P500 (US\$)       | 987       | 7.4%    | 13.1%     | -22.1% | -10.4%   |
|                | WORLD - MSCI (US\$)      | 1045      | 8.4%    | 17.0%     | -23.6% | 1.7%     |
|                | MSCI in NZD (NZ\$)       | 1590      | 7.4%    | 0.7%      | -14.8% | -2.0%    |
| Exchange Rates | NZD/USD                  | 0.657     | 0.9%    | 16.2%     | -10.2% | 3.8%     |
|                | NZD/AUD                  | 0.792     | -1.5%   | 1.7%      | 2.2%   | -12.4%   |
|                | NZD/JPY                  | 62.6      | 0.5%    | 13.8%     | -20.7% | -11.6%   |
|                | NZD/GBP                  | 0.397     | 1.4%    | 4.0%      | 7.4%   | 14.1%    |
|                | NZD/EUR                  | 0.465     | 0.7%    | 9.2%      | -1.0%  | -11.5%   |
|                | NZ TWI                   | 0.614     | 0.3%    | 9.9%      | -6.5%  | -5.3%    |
|                | EUR/USD                  | 1.413     | 0.2%    | 6.4%      | -9.3%  | 17.4%    |

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

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### 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

- The RBNZ delivered the last cut of 50bp cut to the Official Cash Rate (OCR) on 30 April. The RBNZ kept the OCR on hold at 2.5% as widely expected on July 30. The tone of the RBNZ's statement was a little more conservative than many expected.
- The RBNZ reinforced the message of previous OCR announcements, restating "The OCR could still move modestly lower over the coming quarters. We continue to expect to keep the OCR at or below the current level through until the latter part of 2010."
- The 90-day bank bill yield dipped slightly in July, with market pricing at present remaining consistent with the RBNZ on hold over the coming months.
- Term deposit rates for longer time frames remained high in July.

### Fixed interest

- The upward trend for local government bond yields paused in July, with the 10-year yield falling 19 basis points over the month, reversing June's increase.
- NZ 10-year Government Bonds are currently trading with yields around 150 basis points above the lows touched in early 2009. We expect yields to continue to lift as government debt issuance increases over the next few years.
- The US 10-year Treasury yields broke through 4% mid-June, before rallying back to close the month with yields back around 3.5%. In July, US yields rose once again, but remain below the mid-June peak. Concerns over supply continue to worry the market, but the bond tenders since mid June have been well supported, both here and in the USA.

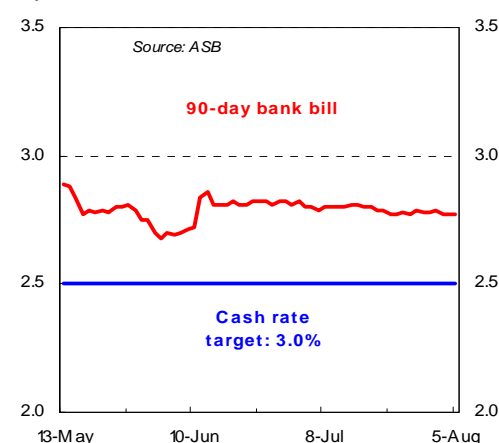
### Equities

- Global equity markets dipped lower through the early part of July, but turned mid month. The turnaround in global equity markets came as the US reporting season kicked off. The better-than-expected result from Alcoa was the catalyst for earnings upgrades from analysts across an array of sectors.
- Overall equity markets posted some of the best gains on record in July. The US S&P 500 gained 7.4%. The Australian All Ords index rallied by 7.6% over the month, marking the best monthly gain in almost 16 years. The NZX-50 beat both markets, lifting 7.8%.
- The UK's FTSE 100 index posted the best return of the markets we monitor, gaining 8.4%. The Japanese market was the laggard, with the Nikkei lifting a more modest 4%.

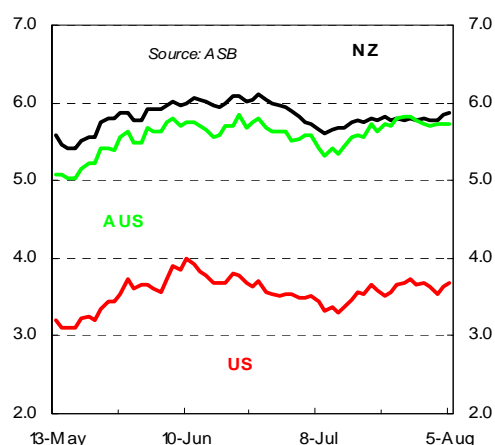
### Exchange rates

- The NZD appreciated strongly against the USD over the month, but made only mild gains in trade-weighted terms.
- As confidence in the global economic recovery improved, the NZD ground higher against the USD, trading around its highest rate since October 2008 towards the end of the month. The NZD broke through US 0.66 and 0.67 in late July/early August.
- The RBNZ spoke out again against the NZD, remarking: "The level of the dollar in particular, is not helping the sustainability of future growth, and brings with it additional economic risks. The forecast [economic] recovery is based on a further easing in financial conditions. If this easing does not occur, the forecast recovery could be put at risk. In these circumstances we would reassess policy settings." In contrast, we expect the NZD will grind higher over the coming months.

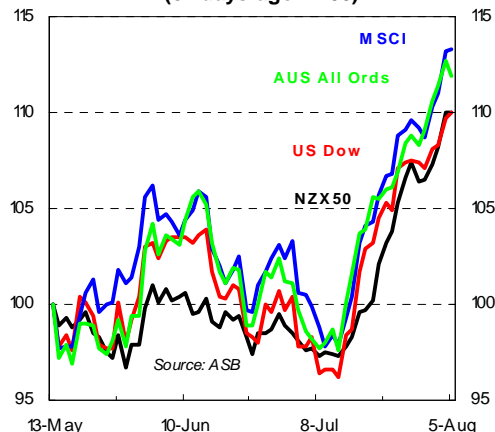
% p.a. **NZ SHORT-TERM RATES**



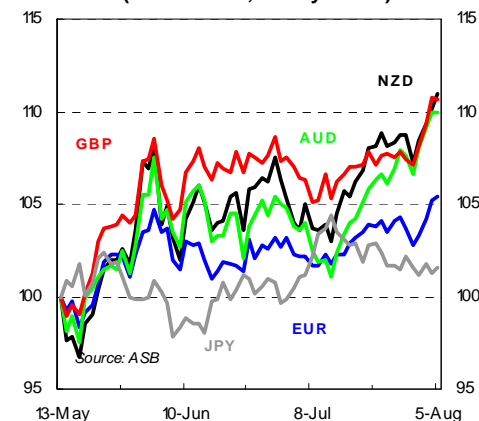
% p.a. **10-YEAR BOND YIELDS**



**SHARE INDICES**  
(84 days ago = 100)



**EXCHANGE RATE INDICES**  
(versus USD, 84 days =100)



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