

# Markets Monthly

## Markets consolidate in September

- Risk aversion eased in September, although investors remain cautious.
- The NZD and AUD bounced in September, after sliding in August.
- Sharemarkets recovered, although the resurgent NZD detracted from offshore returns.

Financial markets in September remained plagued by worries over the fallout from the deterioration in the US sub-prime housing sector. A bigger-than-expected 50bp rate cut from the US Federal Reserve on September 18, however, helped boost sentiment. But Fed's decision weighed on the US dollar, which fell to multi-year lows. Soft US economic data, particularly in the labour and housing markets, also caused the US dollar to fall significantly, generating a lift in all currencies, including the New Zealand dollar. The NZ dollar had fallen heavily against all major currencies during August, dipping to a low of US 0.66 cents briefly mid-month. The NZ dollar strengthened through late August, and September and is trading around US 0.755 at the time of writing. We are unlikely to revisit the previous high of 0.81, but the NZ dollar is looking fairly strong against a weak US dollar, and is likely to trade around the current level for the next few months.

The month was positive overall for global sharemarkets, with all the main sharemarkets posting gains. The resurgent New Zealand dollar detracted, when returns are measured in NZ dollar terms.

Bond yields rose over the month, as some investors sold down bonds and dipped their toes back into equity markets. The RBNZ left the Official Cash rate on hold at its September meeting. Inflation pressures remain intense within the economy, but the economic outlook is clouded somewhat by the current global financial market turbulence. We expect the RBNZ will remain on hold until late 2008.

Although the US economic outlook is mixed, the US sharemarket is performing well. US companies with offshore earnings are benefiting from a lower USD. The economic backdrop in Asia remains very positive, and accordingly the long-term outlook remains positive for regional sharemarkets, despite the financial jitters of the last few months. The security of cash and relatively high yield on many fixed interest investments are attractive for many right now, but our expectation of shares providing the greatest return long term remains in place.

Date	Instrument	30-Sep-07	Month %	Quarter %	Year %	5-Year %
Cash	NZ cash rate	8.25	0.00	0.25	1.00	2.50
	NZ 90-day bank bill	8.79	0.17	0.43	1.18	2.92
	US 90-day bank bill	5.23	-0.35	-0.13	-0.14	3.45
	NZ - US 90-day bank bill	3.56	0.52	0.56	1.32	-0.53
Fixed Interest	NZ 5-year gov't stock	6.68	0.04	-0.46	0.54	0.80
	NZ 10-year gov't	6.29	0.11	-0.45	0.57	0.23
	NZ 10-year swap	7.57	0.13	-0.15	0.90	0.90
	AUS 10-year gov't	6.16	0.24	-0.11	0.65	0.82
	US 10-year gov't	4.57	0.02	-0.53	-0.04	0.86
Equities	NZ - NZX50 (NZ\$)	3199	2.8%	-0.7%	13.6%	63.9%
	AUS - All Ords (A\$)	6581	5.3%	4.3%	28.7%	124.7%
	JAP - Nikkei (¥)	16786	1.3%	-7.5%	4.1%	78.9%
	UK - FT100 (£)	6467	2.6%	-2.1%	8.5%	73.8%
	US - S&P500 (US\$)	1527	3.6%	1.6%	14.3%	87.3%
	WORLD - MSCI (US\$)	1634	4.6%	1.9%	18.9%	121.3%
	MSCI in NZD (NZ\$)	2157	-2.9%	3.5%	2.4%	37.0%
Exchange Rates	NZD/USD	0.757	7.8%	-1.5%	16.1%	61.5%
	NZD/AUD	0.857	0.0%	-5.3%	-1.6%	-0.7%
	NZD/JPY	87.2	6.8%	-8.0%	13.5%	53.0%
	NZD/GBP	0.374	7.3%	-2.5%	7.8%	25.0%
	NZD/EUR	0.535	4.0%	-6.4%	4.3%	12.2%
	NZ TWI	0.712	5.0%	-4.8%	8.4%	32.2%
	EUR/USD	1.416	3.6%	5.3%	11.4%	43.9%

Chris Tennent-Brown – CBA NZ Economist – 649 374 8819 – [chris.tennent-brown@asb.co.nz](mailto:chris.tennent-brown@asb.co.nz)

### General Advice Warning

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### Cash

- The OCR has been hiked 4 times this year, and stands at 8.25%, and was “on hold” at the RBNZ’s September meeting.
- The NZ 90-day rate spiked to over 9% when global credit tightness was at a peak, but has subsequently eased, although the yield remains historically high.
- Central Banks globally, including the RBNZ, have taken measures to ensure liquidity is maintained within the banking system.
- The Federal Reserve Bank cut their Fed Funds Rate on September 18<sup>th</sup>, to 4.75%.
- Other Central Banks remained on hold when they met in September and early October.

### Fixed interest

- Bond yields rose over the month, as some investors sold down bonds and dipped their toes back into equity markets.
- The 10-year NZ Government Bond yield rose 13 basis points. US 10-year yields rose 2 points after falling in July and August.
- A low level of mortgage fixing activity from banks continued in September. Yet wholesale swap rates rose modestly. The one year rate rose 12 points, and the five year rate rose 6 points, reversing some of the previous month’s fall.
- US 10-year Gov’t stock is now trading around 4.52% in early October. The NZ 10-year rate is now trading around 6.27%.
- We expect a period of volatile sideways action in interest rate markets, including NZ rates. Long-term rates eventually should rise from today’s levels, once the current risk aversion subsides.

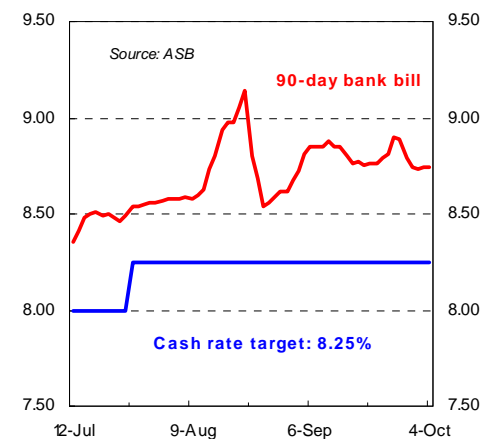
### Equities

- September was positive overall for global sharemarkets, with the main markets all posting gains.
- Concerns about the US housing market, sub prime mortgages, and indeed the health of the overall US economy all weighed heavily on US shares in July and early August.
- The market has regained more confidence when the US Fed cut their Fed Funds Rate, and shares have now largely recovered from the August slump.
- The NZD appreciation over September had a major impact on offshore investment returns, eroding gains when measured in NZD terms.
- The MSCI index of world shares posted a 4.6% gain in US dollars and a 2.9% loss in New Zealand dollar terms for the month.

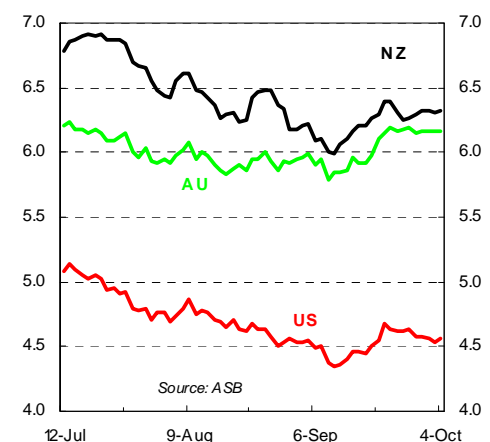
### Exchange rates

- The NZ dollar set a post float high of US \$0.8112 on July 24<sup>th</sup>.
- The NZ dollar lost 5 cents US in the last week of July, and the slide continued through August, with the NZD dipping to a low of US 0.66 cents briefly mid-month.
- The NZD has subsequently recovered in late August and September, and is back trading around US 0.755 at the time of writing.
- Global investors’ are regaining confidence and buying the currencies of high yielding economies such as New Zealand.
- The NZD resurgence has been matched by Aussie dollar strength, with the NZD/AUD cross rate flat for the month. NZD has strengthened on the other cross rates, and is up 5% on a trade weighted basis.

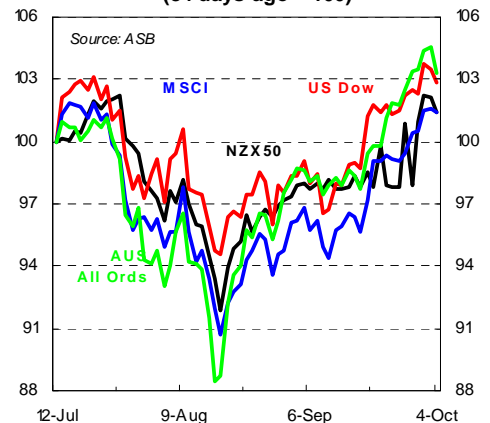
% p.a. **NZ SHORT-TERM RATES**



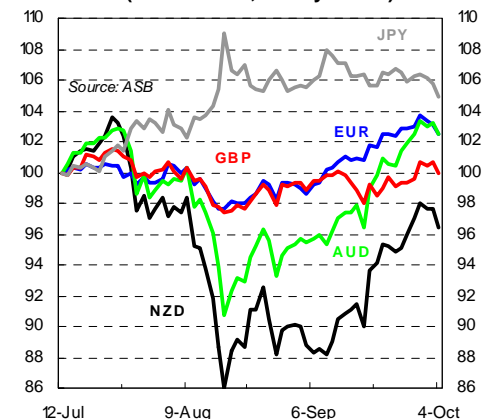
% p.a. **10-YEAR BOND YIELDS**



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



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



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ASB ECONOMICS  
Level 9, 135 Albert Street, Auckland

ASB GROUP ECONOMICS			PHONE	FAX
Chief Economist	Nick Tuffley	<a href="mailto:nick.tuffley@asb.co.nz">nick.tuffley@asb.co.nz</a>	(649)374 8604	
Treasury Economist	Daniel Wills	<a href="mailto:daniel.wills@asb.co.nz">daniel.wills@asb.co.nz</a>	(649) 374 8185	
CBA NZ Economist	Chris Tennent-Brown	<a href="mailto:chris.tennent-brown@asb.co.nz">chris.tennent-brown@asb.co.nz</a>	(649) 374 8819	(649) 302 0992

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