NZD mildly weaker through September

- Stronger risk appetite saw higher equities and global rates, but the NZD weakened nevertheless...
- ...with speculators taking net short positions to a record high as NZ economic data underwhelmed

Quick Outlook

<table>
<thead>
<tr>
<th>Currency</th>
<th>Outlook</th>
<th>Sept ranges</th>
</tr>
</thead>
<tbody>
<tr>
<td>NZD/USD</td>
<td>With the ongoing trade war and slower global growth, fundamental headwinds remain and we target a 0.60-0.63 range towards year-end. Heavy speculative net short positioning provides opportunities for short-lived upward blips.</td>
<td>0.6250 – 0.6450</td>
</tr>
<tr>
<td>NZD/AUD</td>
<td>Back to fair value around 0.93 so no strong view from here other than that level should act as a bit of an anchor over coming months.</td>
<td>0.9230 – 0.9405</td>
</tr>
<tr>
<td>NZD/GBP</td>
<td>Prone to remain volatile given political brinksmanship ahead of the 31 Oct Brexit deadline. Our year-end target of 0.51 assumes a further Brexit delay, but a possible November general election would add another risk event before then.</td>
<td>0.5000 – 0.5265</td>
</tr>
<tr>
<td>NZD/EUR</td>
<td>The ECB is doing its best to debase its currency with further rate cuts and QE. But our bias is for a lower cross as global factors predominate and EUR selling pressure moderates.</td>
<td>0.5680 – 0.5880</td>
</tr>
<tr>
<td>NZD/JPY</td>
<td>Remains near a 7-year low, and a violent recovery would be possible under a trade war resolution, but the cross is apt to weaken further as the road to recovery still has a number of potholes to navigate and risk sentiment can easily reverse course (lower)</td>
<td>66.6 – 69.7</td>
</tr>
</tbody>
</table>
Risk appetite was higher in September, seeing gains in global equities and global bond yields, while JPY underperformed. The NZD was also weaker despite that backdrop and printed a fresh 4-year low, although currency movements overall were fairly modest.

The US-China trade war remained a key theme through September. Some “goodwill” measures by both sides were adopted, with the US delaying some fresh punitive tariffs by a couple of weeks (to 15 October), ahead of talks that will restart early October. China exempted some agricultural goods from tariffs that paved the way for some increased purchases of soybeans and pork. But expectations generally remained low for any comprehensive trade deal to be agreed over coming months. Trump suggested that a trade deal with China would be much tougher if he wins the next Presidential election and that he wouldn’t relent without reaching a “complete deal” with China. Near the end of the month a US government official said that the US is unlikely to extend a waiver allowing American firms to supply Huawei, while talk surfaced of new investment restrictions on Chinese companies for US investors.

A new risk emerged after a whistleblower revealed that on a phone call President Trump pushed Ukraine’s President to investigate Joe Biden to help influence the 2020 Presidential election. The Democrats began an inquiry on whether to impeach the President, which revealed a cover-up by White House officials to protect the President’s actions.

On the economic front, US economic data were generally stronger than expected, taking Citigroup’s US economic surprise index from deeply negative to its highest level in 18 months. A couple of notable exceptions were the US ISM index, with new orders plunging to its equal-lowest level since the GFC; and consumer confidence which showed an unusually large decline for the month.

The run of stronger US data supported a stronger USD, with the DXY index making a fresh 2-year high. The positive dataflow also didn’t get in the way of another 25bps cut to the Fed Funds target range to 1.75-2.0%. That said, dissents in both directions and the dotplot of the appropriate pace of €20b per month.

In Japan, Governor Kuroda hinted of further easing measures at next month’s meeting, with the Bank to “re-examine” economic and price developments after the sales tax goes up on 1 October. In Australia, the market brought forward expectations of the next RBA cut to early October, following more dovish than expected minutes of the September meeting and the further increase in the unemployment rate.

Further easing or expectations of further policy easing was a feature for other major central banks. The ECB announced a multitude of fresh stimulus measures, including 10bp rate cut to the deposit rate to minus 0.5%, (the first rate cut in 3½ years) and the resumption of its QE programme at a pace of €20b per month. In Japan, Governor Kuroda hinted of further easing measures at next month’s meeting, with the Bank to “re-examine” economic and price developments after the sales tax goes up on 1 October. In Australia, the market brought forward expectations of the next RBA cut to early October, following more dovish than expected minutes of the September meeting and the further increase in the unemployment rate.

Financial Markets Wrap

1 October 2019
In NZ, after the shock 50bps cut to the OCR to 1.0% in August, the RBNZ left the OCR unchanged, while an easing bias remained evident. The uncertainties the Bank outlined in the minutes of the meeting were weighed to the downside. In a later speech, Governor Orr toned down his rhetoric on unconventional monetary policy. Whereas in August he was keen to play up the possibility of negative rates and unconventional monetary policy, he gave a more circumspect perspective, saying “we are currently thinking hard about these questions...as a precaution. Our current view is that we are unlikely to need ‘unconventional’ monetary policy tools.”

US Treasury yields traded a wide range following the massive fall in rates through August. The 10-year rate reached a low of 1.43% early in the month, before surging to 1.90% mid-month, and then falling to close the month at 1.67%, up 17bps for the month. The market continued to price in another rate cut by the end of the year, but trimmed almost a full rate cut from next year’s policy track.

Elsewhere, the rise in bond rates was more moderate, with a weaker dataflow evident. Key August monthly economic activity indicators for China were all below market expectations, providing further evidence of the trade war driving weaker growth and the economy showing a lack of response so far to a range of policy easing measures. The economic surprise index for the euro area dived to a 7-month low. Within the mix, euro area PMI manufacturing data continued to lurch deeper into contractionary territory, while the Bundesbank warned that Germany’s economy had likely entered an economic recession.

NZ’s economic dataflow remained soggy. Q2 GDP was 0.5% q/q, not as bad as some feared. The ANZ business outlook survey showed a further slump in business confidence, activity indicators and inflation expectations. The survey added to evidence that the RBNZ’s shocking 50bps cut in August spooked businesses (and consumers) rather than supported confidence about the outlook. Early in the month, NZ rates reached fresh record lows, with the 2-year swap rate trading below 0.90% and 5-year swap down to 0.91%. For the month overall, NZ rates were slightly higher across the curve.

Currency markets showed fairly modest movements through the month. The NZD was generally weaker, egged on by some speculative selling pressure, with CFTC data showing a record number of net short contracts. The NZD made a fresh 4-year low of 0.6250 soon after the publication of the ANZ business outlook survey.

GBP was the most volatile and strongest currency of the majors, as Brexit remained in the headlines. A no-deal Brexit looked increasingly unlikely as Parliament took control of the process and PM Boris Johnson’s role was very much diminished. UK’s Supreme Court unanimously ruled that Boris Johnson’s suspension of parliament was unlawful.
JPY was the weakest of the majors reflecting higher risk appetite, higher UST yields and the BoJ Governor’s easier policy guidance. Other “safe-haven” currencies such as EUR and CHF also underperformed, with the former not helped by the continuing run of weak data in the euro-area.

AUD and CNY were fairly flat for the month against the USD. The former weakened in the second half after expectations for RBA policy easing were brought forward. The PBoC actively set the CNY reference rate on the strong side of the ledger, wanting to keep the currency well under control ahead of the next round of US trade talks.

In commodity markets, a drone attack on Saudi Arabia oil production facilities saw the country’s production temporarily cut in half, and Brent oil prices spiked up as much as 20%. However, a quick recovery in production levels and a lack of retaliatory action saw Brent crude end the month barely higher.

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**Monthly Performance Table**

<table>
<thead>
<tr>
<th>Currencies</th>
<th>end-Sep</th>
<th>end-Aug</th>
<th>Change</th>
<th>NZ Rates</th>
<th>end-Sep</th>
<th>end-Aug</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>NZD/USD</td>
<td>0.6264</td>
<td>0.6309</td>
<td>-0.7%</td>
<td>OCR</td>
<td>1.00</td>
<td>1.00</td>
<td>0.00</td>
</tr>
<tr>
<td>NZD/AUD</td>
<td>0.9280</td>
<td>0.9364</td>
<td>-0.9%</td>
<td>NZ 90day BB</td>
<td>1.15</td>
<td>1.20</td>
<td>-0.05</td>
</tr>
<tr>
<td>NZD/EUR</td>
<td>0.5747</td>
<td>0.5739</td>
<td>0.1%</td>
<td>NZ 2yr sw ap</td>
<td>0.94</td>
<td>0.91</td>
<td>0.03</td>
</tr>
<tr>
<td>NZD/GBP</td>
<td>0.5095</td>
<td>0.5187</td>
<td>-1.8%</td>
<td>NZ 5yr sw ap</td>
<td>0.94</td>
<td>0.94</td>
<td>0.00</td>
</tr>
<tr>
<td>NZD/JPY</td>
<td>67.71</td>
<td>66.85</td>
<td>1.3%</td>
<td>NZ 10yr sw ap</td>
<td>1.21</td>
<td>1.20</td>
<td>0.01</td>
</tr>
<tr>
<td>NZD/CNY</td>
<td>4.478</td>
<td>4.515</td>
<td>-0.8%</td>
<td>NZ Govt (4/23)</td>
<td>0.79</td>
<td>0.77</td>
<td>0.02</td>
</tr>
<tr>
<td>TWI</td>
<td>70.2</td>
<td>70.9</td>
<td>-1.1%</td>
<td>NZ Govt (4/27)</td>
<td>0.99</td>
<td>0.96</td>
<td>0.03</td>
</tr>
<tr>
<td>AUD/USD</td>
<td>0.6750</td>
<td>0.6733</td>
<td>0.3%</td>
<td>NZ Govt (4/29)</td>
<td>1.09</td>
<td>1.07</td>
<td>0.02</td>
</tr>
<tr>
<td>NZD/CAD</td>
<td>1.3241</td>
<td>1.3311</td>
<td>-0.5%</td>
<td>Global 10 year bond rates</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>USD/CNY</td>
<td>7.15</td>
<td>7.16</td>
<td>-0.1%</td>
<td>US</td>
<td>1.67</td>
<td>1.50</td>
<td>0.17</td>
</tr>
<tr>
<td>USD/CAD</td>
<td>1.3241</td>
<td>1.3311</td>
<td>-0.5%</td>
<td>Canada</td>
<td>1.36</td>
<td>1.16</td>
<td>0.20</td>
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<tr>
<td>USD TWI major</td>
<td>121.22</td>
<td>120.83</td>
<td>0.3%</td>
<td>UK</td>
<td>0.48</td>
<td>0.48</td>
<td>0.01</td>
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<tr>
<td>Asia DXY</td>
<td>103.09</td>
<td>102.29</td>
<td>0.8%</td>
<td>Ireland</td>
<td>-0.04</td>
<td>-0.09</td>
<td>0.05</td>
</tr>
<tr>
<td>Equity Markets</td>
<td></td>
<td></td>
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<td>Italy</td>
<td>0.82</td>
<td>1.00</td>
<td>-0.18</td>
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<tr>
<td>MSCI AC Wld. loc.</td>
<td>1.275</td>
<td>1.247</td>
<td>2.3%</td>
<td>Spain</td>
<td>0.14</td>
<td>0.10</td>
<td>0.04</td>
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<tr>
<td>MSCI World. loc.</td>
<td>7.060</td>
<td>6.915</td>
<td>2.4%</td>
<td>Portugal</td>
<td>0.16</td>
<td>0.12</td>
<td>0.04</td>
</tr>
<tr>
<td>MSCI EM. USD</td>
<td>2.298</td>
<td>2.253</td>
<td>2.0%</td>
<td>Ireland</td>
<td>-0.04</td>
<td>-0.09</td>
<td>0.05</td>
</tr>
<tr>
<td>US S&amp;P 500</td>
<td>2.977</td>
<td>2.926</td>
<td>1.7%</td>
<td>Japan</td>
<td>-0.22</td>
<td>-0.28</td>
<td>0.06</td>
</tr>
<tr>
<td>Euro STOXX 600</td>
<td>393.2</td>
<td>379.5</td>
<td>3.6%</td>
<td>Australia</td>
<td>1.02</td>
<td>0.89</td>
<td>0.13</td>
</tr>
<tr>
<td>Germany DAX</td>
<td>12.428</td>
<td>11.939</td>
<td>4.1%</td>
<td>Germany</td>
<td>-0.57</td>
<td>-0.70</td>
<td>0.13</td>
</tr>
<tr>
<td>France CAC 40</td>
<td>5.678</td>
<td>5.480</td>
<td>3.6%</td>
<td>Japan</td>
<td>-0.22</td>
<td>-0.28</td>
<td>0.06</td>
</tr>
<tr>
<td>UK FTSE 100</td>
<td>7.408</td>
<td>7.207</td>
<td>2.8%</td>
<td>Australia</td>
<td>1.02</td>
<td>0.89</td>
<td>0.13</td>
</tr>
<tr>
<td>Aust S&amp;P/ASX 200</td>
<td>6.688</td>
<td>6.604</td>
<td>1.3%</td>
<td>Germany</td>
<td>-0.57</td>
<td>-0.70</td>
<td>0.13</td>
</tr>
<tr>
<td>Japan Topix</td>
<td>1.588</td>
<td>1.512</td>
<td>5.0%</td>
<td>UK</td>
<td>0.48</td>
<td>0.48</td>
<td>0.01</td>
</tr>
<tr>
<td>China CSI 300</td>
<td>3.815</td>
<td>3.800</td>
<td>0.4%</td>
<td>Ireland</td>
<td>-0.04</td>
<td>-0.09</td>
<td>0.05</td>
</tr>
<tr>
<td>NZX50</td>
<td>10.926</td>
<td>10.757</td>
<td>1.6%</td>
<td>Japan</td>
<td>-0.22</td>
<td>-0.28</td>
<td>0.06</td>
</tr>
<tr>
<td>Volatility: VIX</td>
<td>16.24</td>
<td>18.98</td>
<td>-14.4%</td>
<td>Australia</td>
<td>1.02</td>
<td>0.89</td>
<td>0.13</td>
</tr>
<tr>
<td>3-mth Bill Futures</td>
<td></td>
<td></td>
<td></td>
<td>Commodities (USD)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>NZD Dec-19</td>
<td>98.95</td>
<td>98.99</td>
<td>-0.4%</td>
<td>WTI Crude</td>
<td>54.07</td>
<td>55.10</td>
<td>-1.9%</td>
</tr>
<tr>
<td>AUD Dec-19</td>
<td>99.06</td>
<td>99.15</td>
<td>-0.9%</td>
<td>Brent Crude</td>
<td>60.78</td>
<td>60.43</td>
<td>0.6%</td>
</tr>
<tr>
<td>USD Dec-19</td>
<td>98.04</td>
<td>98.14</td>
<td>-0.10</td>
<td>R/B CRB Index</td>
<td>173.9</td>
<td>170.4</td>
<td>2.1%</td>
</tr>
<tr>
<td>EUR Dec-19</td>
<td>100.46</td>
<td>100.57</td>
<td>-0.11</td>
<td>Gold spot</td>
<td>1.472</td>
<td>1.520</td>
<td>-3.1%</td>
</tr>
<tr>
<td>GBP Dec-19</td>
<td>99.27</td>
<td>99.32</td>
<td>-0.05</td>
<td>Silver spot</td>
<td>17.00</td>
<td>18.38</td>
<td>-7.5%</td>
</tr>
</tbody>
</table>
| Source: BNZ, Bloomberg

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Financial Markets Wrap

1 October 2019

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