

7 May 2018



Events Round-Up

CH: Caixin PMI services, Apr: 52.9 vs. 52.3 exp.
EC: Retail Sales (m/m%), Mar: 0.1% vs. 0.5% exp.
US: Change in non-farm payrolls, Apr: 164k vs. 192k exp.
US: Unemployment rate, Apr: 3.9% vs. 4% exp.
US: Average hourly earnings (m/m%), Apr: 0.149% vs. 0.2% exp.
US: Average hourly earnings (y/y%), Apr: 2.6% vs. 2.7% exp.

Good Morning

The US payrolls report on Friday was mixed, but the drop in the unemployment rate to 3.9% was enough to push the USD higher again. Equities also moved higher after the payrolls report even amid reports that US-China trade talks remained deadlocked. Emerging markets have come back into the market's focus as well, with the Argentinean central bank raising its cash rate to 40%, to combat the decline in the peso. The NZD continues to hover around 0.70 ahead of Adrian Orr's first RBNZ meeting this Thursday.

The non-farm payrolls report was a mixed bag, with the headline jobs number a bit lower than expected (164k v. 192k exp.), wage growth disappointing slightly, but the unemployment rate falling to 3.9% (vs. 4% exp.). Job growth for the previous two months was revised up by 30k, largely offsetting the disappointment in April payrolls relative to economist expectations. There probably wasn't much in the payrolls report to materially change the market's impression that the US labour market remains tight, wage growth is trending gradually higher (but not to the point where inflation is a serious concern), and the Fed remains on course to continue hiking rates this year and next.

The initial market reaction saw around a 2bp decline in US Treasury yields and a modest decline in the USD, but these moves were quickly reversed with the market focusing on the larger than expected fall in the unemployment rate, to 3.9%. The unemployment rate is now within reach of the lows reached in the early 2000s of 3.8% and one has to go back to the late '60s to find a lower unemployment rate than that. The 10 year Treasury yield ended the day unchanged at 2.95%, while the 2 year rate was up around 2bps.

Several Fed officials were out speaking on Friday, with the broad message the Fed's inflation target was "symmetric" and that they didn't intend to overreact to a modest inflation overshoot. Incoming New York Fed President John Williams said "*I am personally comfortable with the fact that inflation may overshoot that 2 percent for a while.*" The market will expect a similar message from Fed Chair Powell when he speaks on Tuesday. US core CPI released on Friday morning NZT is the highlight data-wise this week.

The USD moved higher after payrolls, in tandem with the increase in Treasury yields off the intraday lows, and ended the day modestly stronger against most of the G10 currencies. The Bloomberg DXY was up 0.2% on Friday and near its highest levels for 2018. Besides the increase in interest rate differentials, in favour of the USD, short covering among speculative investors has undoubtedly played a key role in the recent USD resurgence. CFTC data released Friday showed a near 30% reduction in the aggregate USD short position among speculative investors for the week ended Tuesday.

The NZD was one of the underperformers in FX markets on Friday, although this was mostly a reflection of its steady decline from mid-afternoon NZ time (from a high of 0.7053) to around 0.7010 before payrolls was released. The NZD hit a low of 0.6994 after payrolls, before recovering to end the week at 0.7020. An increase in risk appetite during the US session (as reflected in higher equities and the VIX falling below 15) helped support the NZD post-payrolls. The focus for the NZD this week is firmly on the RBNZ meeting on Thursday morning, the first under new Governor Adrian Orr. We don't expect much change from the February MPS – see our RBNZ MPS Preview sent on Friday.

US equity markets ended the week on a strong note (S&P500 +1.3%, NASDAQ +1.7%), with the market seemingly reassured by the modest increase in wage growth in April. In a television interview, Warren Buffett said he had bought an additional 75 million shares in Apple in the first quarter (which would have cost more than \$10b), which helped Apple shares to a new high and contributed to the outperformance of the NASDAQ.

US-China trade tensions threaten to come back on the market's radar this week, with media outlets reporting that the trade talks in China on Thursday and Friday ended deadlocked. While both sides agreed to keep talking, the US delegation's long (and in certain cases, unrealistic) set

of demands doesn't bode well for any near-term agreement. The US reportedly asked China to reduce its bilateral trade surplus with the US by \$200b by the end of 2020 (US administration officials had previously mentioned a figure of \$100b; the US deficit with China stood at \$337b at the end of 2017) and not to retaliate to any of the proposed measures. The problem is that the US trade deficit vis-à-vis China is not just a function of trade policies but also relative macroeconomic conditions and ironically Trump's fiscal plan is, if anything, likely to further boost the US deficit (via increased spending on imports and reduced US national saving). The editorial in the official China Daily said "the developments over the past months show China will not compromise on its core interests no matter how desperately the U.S. tries." The market will hope this is just the opening salvo in negotiations and there was enough progress made to delay Trump's proposed \$150b tariffs on Chinese imports (which can be imposed after public comment closes on May 22nd). The market will be keeping a close eye on the President's twitter feed this week.

Finally, the Argentinean central bank raised rates on Friday to 40%, the third increase last week, to combat the weakness in the peso. The Argentinean peso rose around 2.5% on Friday in response to the rate hike, but is down almost 15% this year. The resurgence in the USD and increase in US real rates over the past month has put pressure on emerging market currencies, especially in those countries with high inflation and current account deficits, most notably the Argentinean peso, but also the Turkish Lira (-10% YTD). So far, there has been limited fall-out in other risk-asset markets, and most emerging market currencies are much stronger than they were at the start of 2016 (when concerns about China were at a peak and commodity prices were in free-fall) but it's certainly one to keep an eye on.

nick.smyth@bnz.co.nz

Coming Up

		Period	Cons.	Prev.	NZT
JN	BOJ Minutes of Policy Meeting				11:50
AU	NAB Business Conditions	Apr		14	13:30
AU	NAB Business Confidence	Apr		7	13:30
GE	Factory Orders y/y%	Mar	5	3.5	18:00

Source: Bloomberg, BNZ

Foreign Exchange					Equities				Commodities**				
Indicative overnight ranges (*)					Major Indices				Price				
	Last	% Day	Low	High		Last	% Day	% Year		Last	Net Day		
NZD	0.7020	-0.3	0.6994	0.7034	S&P 500	2,663	+1.3	11.0	Oil (Brent)	74.87	+1.9		
AUD	0.7539	+0.1	0.7492	0.7550	Dow	24,263	+1.4	15.5	Oil (WTI)	69.72	+2.0		
EUR	1.1960	-0.2	1.1911	1.1994	Nasdaq	7,210	+1.7	18.2	Gold	1314.7	+0.3		
GBP	1.3531	-0.3	1.3487	1.3583	Stoxx 50	3,551	+0.6	-3.0	HRC steel	862.0	-0.1		
JPY	109.12	-0.1	108.65	109.27	FTSE	7,567	+0.9	3.7	CRB	203.3	+0.6		
CAD	1.2846	-0.0			DAX	12,820	+1.0	0.8	Wheat Chic.	541.8	-2.0		
NZD/AUD	0.9312	-0.4			CAC 40	5,516	-0.1	1.5	Sugar	11.51	-1.5		
NZD/EUR	0.5870	-0.1			Nikkei	22,473	-0.2	15.6	Cotton	86.90	+2.8		
NZD/GBP	0.5188	+0.0			Shanghai	3,091	-0.3	-0.4	Coffee	122.6	-1.4		
NZD/JPY	76.60	-0.4			ASX 200	6,063	-0.6	3.9	WM powder	3300.0	+0.3		
NZD/CAD	0.9018	-0.3			NZX 50	8,549	+0.0	16.1	Australian Futures				
NZ TWI	73.55	-0.2							3 year bond	97.79	0.01		
									10 year bond	97.22	0.00		
Interest Rates					NZ Government Bonds				NZ Swap Yields				
	Rates				Benchmark 10 Yr Bonds								
	Cash	3Mth	2 Yr	10 Yr	Last	Net Day	Last	Last	Last	Last	Last		
USD	1.75	2.36	2.77	2.98	USD	2.95	0.00	NZGB 6 05/15/21	2.06	-0.01	1 year	2.12	0.00
AUD	1.50	2.02	2.13	2.94	AUD	2.77	-0.04	NZGB 5 1/2 04/15/23	2.35	-0.02	2 year	2.28	0.01
NZD	1.75	2.04	2.27	3.22	NZD	2.79	-0.02	NZGB 2 3/4 04/15/25	2.60	-0.02	5 year	2.74	-0.00
EUR	0.00	0.06	-0.15	0.97	GER	0.54	0.01	NZGB 4 1/2 04/15/27	2.79	-0.02	7 year	2.97	-0.01
GBP	0.50	0.69	1.03	1.56	GBP	1.40	0.01	NZGB 3 04/20/29	2.96	-0.03	10 year	3.22	-0.01
JPY	-0.07	-0.03	0.05	0.26	JPY	0.05	0.00	NZGB 3 1/2 04/14/33	3.16	-0.03	15 year	3.48	-0.01
CAD	1.25	1.17	2.26	2.68	CAD	2.33	0.00	NZGB 2 3/4 04/15/37	3.34	-0.03			

* These are indicative ranges from 5pm NZT; please confirm rates with your BNZ dealer

** All near futures contracts, except CRB. Metals prices are CME.

Rates are as of New York Close

Source: Bloomberg

Contact Details

Jason Wong

Senior Markets Strategist
+64 4 924 7652

Nick Smyth

Interest Rate Strategist
+64 4 924 7653

National Australia Bank

Ray Attrill

Head of FX Strategy
+61 2 9237 1848

Rodrigo Catril

Senior FX Strategist
+61 2 9293 7109

Gavin Friend

Senior Market Strategist
+44 20 7710 1588

Skye Masters

Head of Fixed Income Research
+61 2 9295 1196

Alex Stanley

Senior Interest Rate Strategist
+61 2 9237 8154

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