

8 February 2018



Events Round-Up

NZ: Unemployment rate, 4Q: 4.5% vs. 4.7% exp.
NZ: Employment change (q/q%), 4Q: 0.5% vs. 0.4% exp.
NZ: Labour Cost Index (q/q%), 4Q: 0.4% vs. 0.5% exp.
GE: Industrial production (y/y%), Dec: vs. 6.8% exp.

Good Morning

Calm has returned to markets the past 24 hours, with stock markets recovering from the big losses earlier this week and bond yields moving higher as well. The VIX is back down to almost 20. The USD is stronger across the board, with the NZD back a little below 0.73. The RBNZ will be the focus today.

At this time yesterday, US S&P500 futures had already pared around half their losses from earlier in the week. After our *Report* went out, US stock index futures rose another ~2% in late US trading yesterday and they have moved higher again overnight. The S&P500 is up almost 1% on the day and is back in positive territory for 2018. As we noted yesterday, even though stock market valuations seem reasonably expensive, the macro backdrop is still generally supportive. As of yesterday, 77% of US companies had beaten analyst expectations for earnings, the highest level since the start of 2010. And just before, media are reporting that a bipartisan agreement has been reached in the US Senate to avert a government shutdown this weekend and suspend the debt ceiling, which is a positive development although not a market mover.

The VIX, which reached a 2½ year high of 50 yesterday, is back down to almost 25 today. Market commentators are blaming the sharp spike in the VIX over the past few days to rebalancing among inverse VIX ETFs (these are ETFs which bet on volatility declining). Several of these inverse VIX ETFs, including one of the most high profile (the XIV), have been redeemed by their issuers after losing most of their value. With most of their assets now wiped out, these products are unlikely to be a catalyst for future bouts of volatility (unless people decide to start putting money in them again, which seems unlikely for some time).

The 10 year Treasury is back to 2.85%, similar levels to late last week. There was no major economic data overnight, but NY Fed President Dudley said he wasn't concerned about the stock market correction and pointed

out that it needs to be seen in the context of the big rises over the past few years. Chicago Fed President Evans (who is a non-voter this year and a renowned dove on the committee) noted that he sees a "hint" of inflation pressures picking up but, in his view, it's prudent to wait until mid-year for the next rate rise. He did caution though that if "*inflation picks up more assuredly, as many expect...then we still could easily raise rates another three or even four times in 2018 if that were necessary.*" The market prices around 2½ Fed hikes for this year and an 85% chance of a March hike.

In FX markets, the USD is stronger across the board. The Bloomberg DXY is up 0.6% on the day and is now up around 2% from the multi-year lows reached in late January. There was no real catalyst for the move although we have been highlighting the very negative sentiment towards the USD of late and the accompanying build-up in short positions (especially against the EUR). It seems reasonable to assume that the dollar is benefitting from short covering.

The EUR has fallen to a 2 week low against the USD, at around 1.2270. The announcement that Merkel's CDU and the SPD had reached a coalition agreement didn't help the EUR. The agreement, which sees the SPD getting the Finance and Foreign Ministry posts, will now be put to the 400,000+ rank and file members of the SPD for a vote. That's not guaranteed, as many SPD party members blamed their poor election result (their worst showing since WWII) on their role as junior coalition partner in the last Grand Coalition.

Against a backdrop of USD strength overnight, the NZD is back down to around 0.7260. Falls in commodity prices overnight (oil is down around 2% and most hard commodities are lower too) probably contributed to NZD's decline (it is the second worst performing currency over the last day).

Yesterday, the NZD had risen to 0.7350, up almost half a cent, after the NZ labour market data showed a small decline in the unemployment rate to 4.5% (in line with our expectations but better than the market consensus). But the NZD gave up those gains over the course of yesterday, with market commentators highlighting the weaker than expected wage data contained in the labour market report (0.4% vs 0.5% expected for 4th quarter). New Zealand, like many countries globally, is experiencing lower wage pressure than historical relationships with unemployment rate would suggest. Local rates markets hardly reacted to the labour market data, and the swaps curve flattened in sympathy with the decline in yields

offshore. Attention now turns to the RBNZ MPS this morning.

In the coming day, the BoE releases its Inflation Report and rate decision. While the BoE is universally expected to keep the Bank Rate on hold at 0.5% the market will be focused on any signals on the timing of the next hike (the May meeting is 50% priced by the market). RBA Governor Lowe gives a speech tonight ahead of the Statement of Monetary Policy tomorrow.

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Coming Up

	Period	Cons.	Prev.	NZT
NZ RBNZ Official Cash Rate	Feb	1.75	1.75	09:00
US Fed's Williams Speaks in Hawaii				11:20
AU NAB Business Confidence	4Q		7	13:30
AU RBA Governor Lowe Gives Speech in Sydney				22:00
EC ECB's Praet Speaks in Frankfurt				23:45
UK Bank of England Bank Rate	Feb	0.5	0.5	01:00

Source: Bloomberg, BNZ

Foreign Exchange					Equities				Commodities**		
Indicative overnight ranges (*)					Major Indices				Price		
	Last	% Day	Low	High		Last	% Day	% Year		Last	Net Day
NZD	0.7264	-1.1	0.7263	0.7326	S&P 500	2,711	+0.6	18.2	Oil (Brent)	65.36	-2.2
AUD	0.7827	-1.0	0.7822	0.7889	Dow	25,121	+0.8	25.0	Oil (WTI)	61.53	-2.9
EUR	1.2269	-0.9	1.2256	1.2406	Nasdaq	7,108	-0.1	25.3	Gold	1318.1	-0.8
GBP	1.3871	-0.6	1.3856	1.3994	Stoxx 50	3,455	+1.8	6.8	HRC steel	744.0	+1.5
JPY	109.58	+0.0	108.92	109.68	FTSE	7,279	+1.9	1.3	CRB	192.5	-1.1
CAD	1.2571	+0.6			DAX	12,590	+1.6	9.0	Wheat Chic.	473.8	+3.2
NZD/AUD	0.9281	-0.1			CAC 40	5,256	+2.7	10.5	Sugar	14.02	+1.3
NZD/EUR	0.5921	-0.2			Nikkei	21,645	+0.2	13.9	Cotton	76.07	-0.2
NZD/GBP	0.5237	-0.6			Shanghai	3,309	-1.8	4.5	Coffee	123.0	+0.1
NZD/JPY	79.60	-1.0			ASX 200	5,877	+0.7	4.0	WM powder	3340.0	+3.4
NZD/CAD	0.9132	-0.5			NZX 50	8,195	-0.6	16.0	Australian Futures		
NZ TWI	74.84	-0.8							3 year bond	97.815	0.02
									10 year bond	97.14	0.03

Interest Rates													
	Rates			Swap Yields		Benchmark 10 Yr Bonds		NZ Government Bonds		NZ Swap Yields			
	Cash	3Mth	2 Yr	10 Yr	Last	Net Day		Last		Last			
USD	1.50	1.79	2.35	2.83	USD	2.82	0.02	NZGB 3 04/15/20	1.89	-0.05	1 year	1.98	0.00
AUD	1.50	1.77	2.05	3.02	AUD	2.84	0.02	NZGB 6 05/15/21	2.08	-0.05	2 year	2.17	-0.01
NZD	1.75	1.89	2.18	3.29	NZD	2.96	-0.02	NZGB 5 1/2 04/15/23	2.41	-0.04	5 year	2.74	-0.02
EUR	0.00	0.06	-0.13	1.11	GER	0.75	0.05	NZGB 2 3/4 04/15/25	2.73	-0.02	7 year	3.01	-0.03
GBP	0.50	0.52	0.93	1.61	GBP	1.55	0.03	NZGB 4 1/2 04/15/27	2.96	-0.02	10 year	3.29	-0.03
JPY	-0.04	-0.06	0.06	0.30	JPY	0.08	-0.00	NZGB 3 1/2 04/14/33	3.32	-0.02	15 year	3.53	-0.03
CAD	1.25	1.17	2.21	2.71	CAD	2.36	-0.00	NZGB 2 3/4 04/15/37	3.47	-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: NZT 06:59

Source: Bloomberg

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