10 December 2018

Events Round-Up

GE: Industrial production (m/m%), Oct: -0.5 vs. 0.3 exp.

US: Change in non-farm payrolls (k), Nov: 155 vs. 198 exp.

US: Unemployment rate (%), Nov: 3.7 vs. 3.7 exp.

US: Average hourly earnings (m/m%), Nov: 0.2 v. 0.3 exp.

US: Average hourly earnings (y/y%), Nov: 3.1 vs. 3.1 exp.

CA: Unemployment rate (%), Nov: 5.6 vs. 5.8 exp.

US: Uni. Michigan consumer sentiment, Dec: 97.5 vs. 97 exp.

CH: Imports (y/y%), Nov: 3 vs. 14 exp.

CH: Exports (y/y%), Nov: 5.4 vs. 9.4 exp.

CH: CPI (y/y%), Nov: 2.2 vs. 2.4 exp.

Good Morning

US equities fell sharply again on Friday amid a renewed bout of risk aversion. The risk-off backdrop pushed US bond yields lower, with a weaker-than-expected payrolls report and dovish comments from Fed Governor Brainard adding to the downward pressure. Currencies saw relatively little movement, although the NZD drifted lower on the day. Finally, OPEC announced a larger than expected 1.2m barrels per day supply cut, which boosted oil prices.

The S&P500 fell a hefty 2.3% on Friday, taking its weekly decline to almost 5%, and putting the index in negative territory for 2018. The S&P has now declined more than 10% from the recent peak in October, a commonly-used definition of a "correction." There was no obvious catalyst for the sharp decline in equities, although some commentators pointed to renewed concerns about US-China trade tensions, with White House advisor Peter Navarro (a China 'hawk') saying that the President was willing to follow through with more tariffs if the two sides couldn't come to an agreement in the next 90 days. President Trump tweeted that "*China talks are going very well*", although this did little to stem the equity market decline, with the market concerned that the arrest of Huawei's CFO on Wednesday is likely to escalate the tensions and could see retaliation for US firms operating in China. Over the weekend, China summoned the US ambassador to protest the arrest. In addition to market concerns on US-China trade talks, there is an underlying nervousness about the slowing the global economy. Thin liquidity, with investors reluctant to establish new positions ahead of year-end, may have exacerbated the market moves.

In economic news, the non-farm payrolls report was weaker than expected, with the US economy adding 155,000 new jobs in November (198k expected). Other aspects of the report were also on the weak-side. While the unemployment rate was unchanged at 3.7%, the underemployment rate ticked up. And average hourly earnings were less than expected on the month (0.2% vs. 0.3% expected), although revisions to prior months meant year-on-year wage growth met expectations at 3.1%.

The three-month moving average of payrolls growth was still a respectable 170,000, which is still more than sufficient to keep downward pressure on the unemployment rate over time. The broad take-away appears to be that the pace of US job growth has started to slow from earlier in the year, consistent with some slowing in the US economy, and wage growth is gradually trending higher. While there have been concerns about a coming US economic slow-down, it's worth pointing out that the US economy was never going to maintain the 3%+ rate seen over the past few quarters, and a slowing towards trend later next year should be entirely expected, and welcomed by the Fed (although the market is, of course, worried about a more pronounced slowing). The University of Michigan consumer confidence index beat expectations and remained near 15-year highs, suggesting the US consumer is still in good spirits, despite the recent stock market wobbles.

There was little immediate reaction in the US bond market to the payrolls release, but US rates subsequently tracked equities lower through the New York trading session. The 10 year yield fell 5bps to 2.85%, its closing lowest level in three months, while the 2 year yield also fell 5bps to 2.71%. Comments from Fed Governor Brainard added some downward pressure to short-end Fed rate expectations. She noted that "*the gradual path of increases in the federal funds rate…remains appropriate in the near term*", a slight dovish shift her previous comments in September that gradual rate hikes were likely to be appropriate "*over the next year or two.*" The market continued to pare back Fed expectations for 2019 (there is only 20bps priced-in for next year now) while retaining a high probability of a December rate rise. It will likely take a far more meaningful correction in equities for the Fed to consider not hiking in December, given that economic data remains reasonably strong overall and the Fed still considers rates to be below neutral.

Elsewhere, oil prices spiked higher after OPEC+ announced that it would cut production by 1.2m barrels per day (equivalent to around 1% of global oil production), larger than what analysts had expected. Saudi Arabia's decision to press ahead with the supply cut, despite pressure from President Trump not to do so, should help maintain OPEC's credibility in managing prices. Brent crude initially rose almost 6% on the announcement, although it later pared those gains to end around 2.5% higher on the day. Brent crude is still 30% lower than the recent peak at the start of October.

The USD indices were close to flat on the day, having initially moved lower after the weaker payrolls release. The DXY was down 0.8% on the week, but continues to hover near 18-month highs. Despite the turbulence in other markets, volatility in FX markets remains relatively contained.

Individual currency performance was mixed, with the rise in oil prices driving appreciation in the CAD (+0.45%) and NOK (+0.2%). A very strong Canadian employment report added upward pressure to the CAD. At the other end, the GBP continued to underperform ahead of the parliamentary vote on Theresa May's Brexit deal on Tuesday night; the GBP was down 0.4% to 1.2730. The market expects the bill to be voted down, and there are a number of possible outcomes that could eventually follow, ranging from a no-deal Brexit to a new referendum. There was little movement in the JPY despite the equity market volatility.

The NZD was down a modest 0.2% on Friday, closing the week at 0.6860. NZD/AUD pushed slightly higher once again to 0.9524, its highest level (on a closing basis) since mid-2017. We expect NZD/AUD to sustain a higher trading range through mid-2019, given softness in Australian housing, and some improvement in NZ's commodity terms of trade relative to Australia (given the big fall in oil prices). See Jason Wong's note from Friday for more on the outlook for the cross.

NZ swaps continued their grind lower on Friday, driven by global forces. The 10 year swap rate fell 1bp to 2.79%, close to its lowest level since October-2016. The domestic focus for the rates market this week is the release of the HYEFU, in which New Zealand Debt Management will update the bond programme, although we're not expecting any major changes. The limited supply of government bonds, a reflection of the strong fiscal position of the government, has been one factor keeping NZ government bond yields at relatively low levels. The last NZ government bond tender of the year is on Friday.

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Coming Up

		Period	Cons.	Prev.	NZT
AU	RBA's Kent gives speech in Sydney				10:30
NZ	Mfg Activity Volume (q/q%)	3Q		-1.2	10:45
JN	GDP (q/q%)	3Q F	-0.5	-0.3	12:50
UK	Industrial Production (y/y%)	Oct	-0.1	0	22:30
UK	Monthly GDP (3m/3m%)	Oct	0.4	0.7	22:30
US	JOLTS Job Openings	Oct		7009	04:00

Source: Bloomberg, BNZ.

Foreign Exchange

Indicative overnight ranges (*)	Last	% Day	Low	High	Other FX	Last	% Day
NZD	0.6859	-0.2	0.6847	0.6898	CHF	0.9920	-0.1
AUD	0.7202	-0.4	0.7198	0.7242	SEK	9.046	+0.6
EUR	1.1396	+0.0	1.1360	1.1423	NOK	8.506	-0.2
GBP	1.2732	-0.4	1.2711	1.2790	HKD	7.816	+0.1
JPY	112.69	+0.0	112.56	112.93	CNY	6.874	-0.1
CAD	1.3322	-0.5			SGD	1.370	+0.0
NZD/AUD	0.9524	+0.2			IDR	14,480	-0.3
NZD/EUR	0.6019	-0.4			THB	32.83	-0.1
NZD/GBP	0.5387	+0.1			KRW	1,120	-0.1
NZD/JPY	77.29	-0.1			TWD	30.84	-0.0
NZD/CAD	0.9138	-0.6			PHP	52.74	-0.1
NZ TWI	74.97	-0.1					

Equities

Major Indices	Last	% Day	% Year
S&P 500	2,633	-2.3	-0.7
Dow	24,389	-2.2	0.2
Nasdaq	6,969	-3.0	1.9
Stoxx 50	3,059	+0.4	-14.8
FTSE	6,778	+1.1	-8.3
DAX	10,788	-0.2	-18.0
CAC 40	4,813	+0.3	-10.9
Nikkei	21,679	+0.8	-5.0
Shanghai	2,606	+0.0	-20.8
ASX 200	5,681	+0.4	-5.2
NZX 50	8,767	+0.1	6.5

Commodities**

Price	Last	Net Day
Oil (Brent)	61.67	+2.7
Oil (WTI)	52.61	+2.2
Gold	1252.6	+0.7
HRC steel	750.0	-0.7
CRB	184.2	+1.6
Wheat Chic.	536.0	+2.9
Sugar	12.87	+1.8
Cotton	80.23	+1.5
Coffee	104.1	-1.7
WM powder	2790.0	+0.0
Australian Futures		
3 year bond	98.08	0.00
10 year bond	97.57	0.02

Interest Rates

	Rates		Swap Yields		Benchmark 10 Yr Bonds		
	Cash	3Mth	2 Yr	10 Yr		Last	Net Day
USD	2.25	2.77	2.86	2.89	USD	2.85	-0.05
AUD	1.50	1.99	1.93	2.63	AUD	2.45	-0.01
NZD	1.75	1.99	2.05	2.79	NZD	2.29	0.00
EUR	0.00	0.06	-0.14	0.85	GER	0.25	0.01
GBP	0.75	0.91	1.15	1.46	GBP	1.27	0.02
JPY	-0.07	-0.11	0.01	0.20	JPY	0.06	-0.01
CAD	1.75	1.17	2.40	2.63	CAD	2.07	-0.02

NZ Government Bonds	Last	
NZGB 6 05/15/21	1.76	0.00
NZGB 5 1/2 04/15/23	1.93	0.00
NZGB 2 3/4 04/15/25	2.13	0.00
NZGB 4 1/2 04/15/27	2.29	0.00
NZGB 3 04/20/29	2.45	0.00
NZGB 3 1/2 04/14/33	2.62	0.00
NZGB 2 3/4 04/15/37	2.77	0.00

NZ Swap Yields	Last	
1 year	1.99	-0.00
2 year	2.06	-0.00
5 year	2.36	-0.01
7 year	2.56	-0.01
10 year	2.79	-0.01
15 year	3.05	-0.01

* 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

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