

11 August 2017

Events Round-Up

NZ: RBNZ OCR (%), Aug: 1.75 vs. 1.75 exp.
NZ: Card spending retail (m/m%), Jul: -0.5 vs. 0.3 exp.
UK: Manufact. production (m/m%), Jun: 0.0 vs. 0.0 exp.
UK: Construction output (m/m%), Jun: -0.1 vs. 1.4 exp.
US: PPI final demand (m/m%), Jul: -0.1 vs. 0.1 exp.
US: PPI ex food and energy (m/m%), Jul: -0.1 vs. 0.2 exp.

Good Morning

Geo-political tensions focused on North Korea remain forefront of mind, leading to a stronger yen, weaker equity markets and supporting lower global rates. The NZD is at the bottom of the leaderboard after yesterday's MPS.

Key European and US equity indices are down around 1%, a chunky fall considering market movements have been so small of late. The geopolitical risks in the spotlight have provided a good excuse for investors to take profits after the seemingly endless positive run in US equities. South Korea and Japan have joined the US in warning North Korea about the consequences of firing missiles towards Guam.

Military action with likely devastating consequences remains a tail-risk for markets. The VIX index spiked up towards 15, the fifth such move we've seen this year. Previous episodes haven't lasted long but it's a risk factor that needs to be respected. This has seen a safe-haven flow towards the Yen, resulting in USD/JPY falling by 0.7% to 109.30.

A hint of USD strength we saw during Asian trading has been fully unwound, not helped by the US PPI coming in below expectations, with the headline final demand figure showing its first monthly fall in a year while core PPI inflation was also soft. The Fed's Dudley didn't rock the boat with his speech notes that suggested "Our outlook anticipates a continued moderate growth trend, with some further strengthening in the labour market and an increase in inflation over the medium term toward our objective of 2 percent". Bloomberg's weekly consumer comfort index showed confidence rising to its highest level in 16 years, but this survey gets little attention.

Outside of the Yen and NZD, currency movements have been modest. GBP has been on the soft side, with the soft run of UK economic continuing, with manufacturing

output stagnating despite the weaker currency. GBP is down 0.2% to 1.2980 while the EUR and AUD are steady at 1.1770 and just below 0.79 respectively.

The NZD has traded in a tight range overnight, with the damage being done in the Asian session. The RBNZ's MPS was broadly as expected and resulted in little market reaction. The Statement reiterated familiar messages, with the Bank's policy guidance unchanged from recent Statements and the projected rate track unchanged from May. This disappointed some in the market who expected a more dovish tone to emerge, but the tick up in rates was not significant.

The only surprise to us was Governor Wheeler upping the rhetoric on the NZD indicating a lower NZD is "needed" compared to "would help" more balanced growth. This was a deliberate change in tone as when it came to the press conference, rather than shut down questions on currency intervention, he played his trump card and ran through the RBNZ's intervention capability. After the local close, Assistant Governor McDermott reiterated the point, suggesting that the subtle change in language was a first step towards possible intervention. "The markets should notice. It's not a slap across the face, it's a little nudge."

Such jaw-boning makes no sense to us, with the TWI sitting below its average for the past year alongside record terms of trade. In terms of the Bank's "traffic light" system, the criteria for intervention are far from being met. Nevertheless, the market took notice, although history shows such jawboning only has a temporary impact.

After drifting lower in afternoon trading on geo-political forces, the NZD fell from 0.7315 to 0.7280 after McDermott's comments and has settled at that level, after reaching a low of 0.7252 last evening.

The NZD is down on all the crosses, with the biggest change being a 1.3% fall on NZD/JPY to 79.7. NZD/EUR is now sub-0.62 while NZD/AUD is back down to 0.9235, a full cent lower from its level in the hours after the MPS.

We believed that the NZD was overdue for a downward correction after positioning data showed record net long positions by speculative accounts and risk appetite that could only head lower from elevated levels. McDermott's comments helped encourage that move. While we might well see a pause for breath over the near-term, we'd argue the NZD has more downside risk through to year-end,

particularly if the USD can stage an overdue recovery.

Global rates edged lower, given the risk-off tone but falls have been fairly modest under the circumstances. UST 10-year yields got a further nudge lower following the soft PPI data and are down 4bps on the day to 2.21%.

With the MPS not as dovish as some expected, the 2-year swap rate rose by nearly 3bps to 2.185%. But half of that gain was before the statement, as prices were marked higher following moves in the offshore session the previous evening. The overall rates market reaction to the Statement was modest. Market pricing for the first rate hike remains well into the back end of next year, around September-November 2018. With the hiking cycle seemingly so distant, the short end of the curve should be well underpinned close to current rates for some time.

Longer term swap rates rose by about 4bps but we expect much of that to be unwound today on the

overnight moves. US CPI data tonight will be keenly anticipated although hopes for a positive surprise have been dashed by the weak PPI data.

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Coming Up

	Period	Cons.	Prev.	NZT
NZ Manufacturing PMI	Jul		56.2	10:30
NZ Food prices (m/m%)	Jul		0.2	10:45
AU RBA's Lowe Before House Economics Committee				11:30
NZ NZ plans to Sell \$100m 2040 I/L Bonds				14:05
US CPI (m/m%)	Jul	0.2	0	00:30
US CPI ex food and energy (m/m%)	Jul	0.2	0.1	00:30
US CPI (y/y%)	Jul	1.8	1.6	00:30
US CPI ex food and energy (y/y%)	Jul	1.7	1.7	00:30
US Fed's Kaplan speaks in Arlington, Texas				01:40
US Fed's Kashkari speaks in Minn.				03:30

Source: Bloomberg, BNZ

Foreign Exchange					Equities				Commodities**						
Indicative overnight ranges (*)					Other FX				Major Indices			Price			
	Last	% Day	Low	High		Last	% Day	% Year		Last	Net Day				
NZD	0.7289	-0.7	0.7252	0.7316	CHF	0.9633	-0.0		S&P 500	2,451	-0.9	12.7	Oil (Brent)	51.87	-1.5
AUD	0.7893	+0.1	0.7867	0.7902	SEK	8.131	-0.5		Dow	21,939	-0.5	18.6	Oil (WTI)	48.59	-1.9
EUR	1.1771	+0.1	1.1704	1.1774	NOK	7.946	-0.1		Nasdaq	6,260	-1.5	20.3	Gold	1283.6	+0.8
GBP	1.2980	-0.2	1.2952	1.3014	HKD	7.817	+0.0		Stoxx 50	3,434	-1.0	13.8	HRC steel	619.0	+0.0
JPY	109.29	-0.7	109.19	110.06	CNY	6.647	-0.4		FTSE	7,390	-1.4	7.6	CRB	178.9	-1.5
CAD	1.2718	+0.1			SGD	1.362	-0.1		DAX	12,014	-1.1	12.8	Wheat Chic.	468.8	-3.7
NZD/AUD	0.9235	-0.8			IDR	13,333	+0.0		CAC 40	5,115	-0.6	14.9	Sugar	13.24	-2.9
NZD/EUR	0.6192	-0.8			THB	33.24	-0.0		Nikkei	19,730	-0.0	17.9	Cotton	69.26	-3.6
NZD/GBP	0.5616	-0.4			KRW	1,142	+0.6		Shanghai	3,262	-0.4	8.6	Coffee	142.0	-2.8
NZD/JPY	79.66	-1.3			TWD	30.32	+0.3		ASX 200	5,761	-0.1	4.6	WM powder	3300.0	+0.0
NZ TWI	76.97	-0.8			PHP	50.77	+0.2		NZX 50	7,790	-0.1	5.9	Australian Futures		
Interest Rates					Benchmark 10 Yr Bonds				NZ Government Bonds			NZ Swap Yields			
Rates		Swap Yields			Last		Net Day		Last			Last			
	Cash	3Mth	2 Yr	10 Yr	USD	2.21	-0.04		NZGB 3 04/15/20	2.01	0.03	1 year	2.02	0.00	
USD	1.25	1.31	1.59	2.17	AUD	2.66	0.02		NZGB 6 05/15/21	2.15	0.02	2 year	2.19	0.03	
AUD	1.50	1.69	1.90	2.80	NZD	2.83	0.03		NZGB 5 1/2 04/15/23	2.45	0.03	5 year	2.67	0.04	
NZD	1.75	1.97	2.18	3.19	GER	0.42	-0.01		NZGB 2 3/4 04/15/25	2.68	0.03	7 year	2.93	0.04	
EUR	0.00	0.06	-0.17	0.82	GBP	1.08	-0.03		NZGB 4 1/2 04/15/27	2.83	0.03	10 year	3.19	0.04	
GBP	0.25	0.28	0.55	1.16	JPY	0.06	0.01		NZGB 3 1/2 04/14/33	3.21	0.03	15 year	3.45	0.04	
JPY	-0.04	-0.02	0.03	0.25	CAD	1.86	-0.05		NZGB 2 3/4 04/15/37	3.45	0.03				
CAD	0.75	1.17	1.57	2.16											

* 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 06:55

Source: Bloomberg

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