

11 December 2018



Events Round-Up

NZ: Manufacturing activity volume (q/q%), Q3: -1.6 vs. -1.2 prev.

UK: Industrial production (y/y%), Oct: -0.8 vs. -0.1 exp.

UK: GDP (3m/3m%), Oct: 0.4 vs. 0.4 exp.

US: JOLTS job openings (k), Oct: 7079 s. 7100 exp.

Good Morning

The British pound was hammered overnight after Theresa May unexpectedly postponed the parliamentary vote on her Brexit deal. With the clock ticking to the March 29th exit date, the market is concerned about the growing risk that the UK could slide into a no-deal Brexit. The news exacerbated already fragile risk sentiment, with US equities falling again, although they have recovered somewhat over the past hour or so. The NZD has outperformed amidst the risk-off backdrop, and the NZD/AUD has made a fresh 18-month high.

The big news overnight is Theresa May's decision to postpone the parliamentary vote on her Brexit deal. May admitted the bill was likely to be defeated by a "significant margin", mainly due to MPs' concerns about the Northern Irish backstop. She will meet EU leaders in Brussels on Thursday and hope to extract some more concessions on the backstop. A European Commission spokeswoman said the EU was not willing to renegotiate the agreement, although Bloomberg reported that EU was prepared to publish a declaration over the backstop, clarifying the EU's position. Such a declaration seems unlikely to convince enough MPs to vote for the deal however, given it would not be legally binding. May did not set a date for when the new vote might take place. The market is concerned that the postponement uses up valuable time before the 29th March exit date, and the risk of a no-deal scenario is growing.

The GBP fell sharply after news that the vote would be delayed, and made an 18-month low against the USD. The GBP fell as much as 1.7% to just above 1.25, although it has since recovered slightly to trade at 1.2560 as we write. UK gilt yields fell sharply in sympathy, with the 10 year rate down 7bps to 1.2% and the 30 year rate down 12bps.

The political situation in the UK is fluid and there remain a large number of permutations that could take place from

here. Labour MP Chris Leslie said the party could table a vote of no confidence tomorrow, and while May would likely survive this, the threat of new elections and a Corbyn-led Labour government remains. A second referendum is also a growing possibility, despite May's insistence that this was off the table. Overnight, the ECJ ruled that the UK could unilaterally withdraw its Article 50 request to leave the EU, which has given hope to Remain supporters that Brexit could yet be reversed. A second referendum appears to be one of the few ways to break the impasse in the divided UK parliament.

The fall in the GBP added to the undercurrent of nervousness in global markets. US equity markets followed on from their sharp falls last week by moving lower once again. The S&P500 was down almost 2% at one stage, but it has recovered over the past hour or so to be down only 0.5% on the day. The cumulative decline in the S&P500 from the peak at the start of October is around 11%. The VIX has moved close to 25, near its highest level since the market meltdown in early-February.

Most sectors of the S&P500 were down on the day, with the energy (-2.2%) and financials (-1.6%) sectors the biggest fallers. Energy sector stocks were hit by a fall in oil prices, with West Texas intermediate falling 2% to pre-OPEC meeting levels (WTI has now fully reversed the gains seen after the OPEC+ announcement that it would reduce oil supply by 1.2m barrels per day). The pressure on US bank equities (the S&P banks index is now down almost 20% from early August) likely stems from a perception that the recent flattening in the yield curve will negatively affect net interest margins and also concerns about the US growth outlook (banks are often seen as a leveraged play on the economy). US economic data continues to paint a more healthy view of the economic outlook than the negative signals implied by the market; overnight, US job openings remained near multi-decade highs.

US rates moves were calm in comparison to the volatility in the GBP and equity markets. The 10 year Treasury yield is actually marginally higher on the day, up 2bp to 2.86%. The 2s10s yield curve steepened up slightly to 15bps. The yield curves that investors commonly refer to when looking for an early warning indicator of US recession (the 90 day-10 year spread and the 2 year-10 year spread) remain in positive territory. The market continues to price 18bps for a December rate hike by the Fed, which is close to fully-priced on the basis the Fed raises interest on excess reserves by only 20bps. There are 18bps of hikes

priced for the Fed in 2019 and 7bps of cuts priced for 2020.

In FX markets, the sharp sell-off in the GBP triggered a smaller decline in the EUR, which fell 0.2% to 1.1360. The USD has strengthened in this environment, with the DXY index moving 0.5% higher to 97.1, and close to its recent 18 month highs. As long as Brexit-related nervousness continues to weigh on the GBP, and by association the EUR, the USD is likely to remain relatively strong. The JPY was 0.4% weaker on the day, and has displayed little of its traditional "safe haven" correlation with equities over the past few weeks.

The NZD is actually slightly higher than Friday night's close and is 0.6875 as we write. After opening softer on Monday morning after the release of much weaker than expected Chinese trade data over the weekend, the NZD moved sharply higher in the NZ afternoon, to almost 0.69, amidst intraday weakness in the USD. The NZD has moved lower over recent hours, in sympathy with the falls in the GBP and EUR, but has outperformed most other currencies. The NZD/AUD has pushed on to a fresh 18-month high at 0.9565.

NZ rates were lower, and the curve flatter yesterday, following on from the decline in Treasury yields on Friday night. The 2 year swap rate was 1bp lower to 2.045% while the 10 year rate fell 3bps to 2.755%, its lowest level since late-2016. NZ manufacturing data released yesterday was weaker than we had anticipated, and we shaved our Q3 GDP forecast from 0.7% to 0.6% as a result. There was no market reaction to the data however.

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Coming Up

		Period	Cons.	Prev.	NZT
NZ	ANZ Truckometer Heavy (m/m%)	Nov		4.6	10:00
NZ	Retail Card Spending (m/m%)	Nov	0.3	0.1	10:45
AU	NAB Business Conditions	Nov		12	13:30
AU	House Price Index (q/q%)	3Q	-1.6	-0.7	13:30
UK	Unemployment Rate	Oct	4.1	4.1	22:30
UK	Employment Change (3m/3m%)	Oct	25	23	22:30
GE	ZEW Survey Expectations	Dec	-25	-24.1	23:00
US	NFIB Small Business Optimism	Nov	107	107.4	00:00
US	PPI Ex Food and Energy (y/y%)	Nov	2.5	2.6	02:30

Source: Bloomberg, BNZ.

Foreign Exchange							Equities				Commodities**					
Indicative overnight ranges (*)					Other FX		Major Indices				Price					
	Last	% Day	Low	High		Last	% Day			Last	Net Day					
NZD	0.6876	+0.1	0.6870	0.6905	CHF	0.9900	-0.2			S&P 500	2,606	-0.8	-1.7	Oil (Brent)	60.89	-1.3
AUD	0.7188	-0.3	0.7180	0.7227	SEK	9.084	+0.4			Dow	24,224	-0.7	-0.4	Oil (WTI)	51.69	-1.8
EUR	1.1363	-0.1	1.1357	1.1440	NOK	8.549	+0.5			Nasdaq	6,992	+0.3	2.2	Gold	1249.4	-0.2
GBP	1.2562	-1.3	1.2507	1.2760	HKD	7.815	-0.0			Stoxx 50	3,017	-1.4	-16.0	HRC steel	746.0	-0.5
JPY	113.16	+0.4	112.35	113.16	CNY	6.912	+0.5			FTSE	6,722	-0.8	-9.1	CRB	182.7	-0.8
CAD	1.3388	+0.5			SGD	1.374	+0.3			DAX	10,622	-1.5	-19.2	Wheat Chic.	532.0	-0.7
NZD/AUD	0.9566	+0.5			IDR	14,553	+0.5			CAC 40	4,742	-3.0	-12.2	Sugar	12.74	-1.1
NZD/EUR	0.6051	+0.5			THB	32.89	+0.2			Nikkei	21,220	-2.1	-7.5	Cotton	79.75	-0.7
NZD/GBP	0.5474	+1.6			KRW	1,127	+0.6			Shanghai	2,585	-0.8	-22.2	Coffee	104.4	+0.2
NZD/JPY	77.81	+0.5			TWD	30.87	+0.1			ASX 200	5,552	-2.3	-7.4	WM powder	2805.0	+0.5
NZD/CAD	0.9206	+0.6			PHP	52.80	+0.1			NZX 50	8,660	-1.2	4.6	Australian Futures		
NZ TWI	75.49	+0.5											3 year bond	98.06	-0.02	
													10 year bond	97.54	-0.02	
Interest Rates							NZ Government Bonds				NZ Swap Yields					
	Rates		Swap Yields		Benchmark 10 Yr Bonds		Last			Last						
	Cash	3Mth	2 Yr	10 Yr	Last	Net Day										
USD	2.25	2.77	2.86	2.90	USD	2.86	0.02	NZGB 6 05/15/21	1.76	0.00	1 year	2.00	0.00			
AUD	1.50	1.99	1.96	2.66	AUD	2.44	-0.00	NZGB 5 1/2 04/15/23	1.92	-0.01	2 year	2.05	-0.01			
NZD	1.75	1.98	2.05	2.76	NZD	2.28	-0.02	NZGB 2 3/4 04/15/25	2.11	-0.02	5 year	2.34	-0.02			
EUR	0.00	0.06	-0.14	0.86	GER	0.25	-0.00	NZGB 4 1/2 04/15/27	2.28	-0.02	7 year	2.53	-0.03			
GBP	0.75	0.91	1.12	1.41	GBP	1.20	-0.07	NZGB 3 04/20/29	2.43	-0.02	10 year	2.76	-0.03			
JPY	-0.07	-0.11	0.00	0.19	JPY	0.04	-0.02	NZGB 3 1/2 04/14/33	2.61	-0.01	15 year	3.01	-0.03			
CAD	1.75	1.17	2.41	2.61	CAD	2.06	-0.01	NZGB 2 3/4 04/15/37	2.76	-0.02						

* 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 06:52

Source: Bloomberg

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