

15 December 2017



Events Round-Up

US: FOMC Rate Decision (Upper Bound), Dec: 1.5% vs. 1.5% exp.

AU: Employment Change, Nov: 61.6k vs. 19k exp..

AU: Unemployment Rate, Nov: 5.4% vs. 5.4% exp.

CH: Industrial Production (y/y%), Nov: 6.1% vs. 6.1% exp.

UK: Bank of England Bank Rate, Dec: 0.5% vs 0.5% exp.

EU: ECB Deposit Facility Rate, Dec: -0.4% vs -0.4% exp.

EU: Eurozone Composite PMI, Dec: 58.0 vs 57.2 exp.

US: Retail Sales ex auto & gas (m/m%): 0.8% vs 0.4% exp

Good Morning

The USD is weaker against most currencies over the past 24 hours as the market interpreted the FOMC as more dovish than expected. The ECB raised its growth forecasts but more importantly cut its core inflation forecast for the end of 2018 and that has seen the EUR struggle too. The AUD was the best performing currency after a stellar employment report. The NZD has lagged overnight, with NZD/AUD down almost a cent to 0.91.

Shortly after yesterday's *Report* was sent, the FOMC raised its range for the Fed Funds Target Rate to 1.25% - 1.50%, as expected. Although the Fed cut its unemployment rate forecast for the end of next year to 3.9% and raised its growth forecast, the median Fed 'dot' stayed at 3 hikes for 2018. This disappointed some who were looking for the Fed median to project 4 hikes. There wasn't much new to glean from Yellen's last press conference and we didn't think there was much surprise at all. Either way, the USD and US yields fell in response to the FOMC, with the 2 year yield down around 5 basis points after the decision. The market prices around two hikes in 2018 vs. the three expected by the Fed.

Overnight, US retail sales surprised on the upside, including the important 'Retail Control Group' that is an input to GDP. US front end yields have bounced back, the 2 year rate is up 4 basis points, although most of this move happened before retail sales, supporting our notion that the market overreacted initially to the FOMC. The NZD has traded in a reasonably narrow range the past 24 hours, and is hovering back around 0.70.

Markets are keeping one eye on the ongoing negotiations between House and Senate Republicans, who are attempting to finalise the tax bill for a vote next week. Overnight, media are reporting that Republican leaders

were looking to cut the top marginal tax rate from 39.6% to 37%, against the wishes of two Republican senators whose votes would probably be needed to pass the bill. The S&P has only dropped 0.2%, which suggests the market remains very confident the tax plan will be enacted.

The big mover the past 24 hours has been the AUD, which moved sharply higher after a much stronger than expected employment report. Although the employment numbers can be volatile month-to-month, the survey showed much stronger employment growth, tilted towards full-time workers. Like most central banks though, the RBA is waiting for this pick-up in job growth to translate to higher inflation. The AUD is up almost a percent from this time yesterday and is at its highest level in a month. The NZD/AUD is down almost a cent, to just above 0.91.

The EUR fell overnight after the ECB cut its core inflation projection for the end of 2018 from 1.3% to 1.1%, despite revising up its growth forecasts. Draghi remained cautious about inflation in the press conference. Although the ECB had already decided to halve its QE programme to €30bn per month starting in January, it's hard to imagine the ECB raising rates without a more significant pick-up in inflation. Core inflation in Europe has been stuck around 1% for the past 4 years and the ECB has few policy options left if pre-emptive tightening proves unwise.

The Bank of England also met overnight, although the pound hasn't reacted much. The BoE stuck with its forecast for some "further modest increases" in the bank rate over the next few years. The BoE sounded more upbeat on the UK's prospect for a transitional deal with the EU, which would likely boost confidence. We tend to agree and that's one of the main reasons we see NZD/GBP heading below 0.50 next year, from its current level around 0.52.

The HYEFU was the focus for the local market yesterday, with the Labour coalition government incorporating their proposed policies for the first time. The bond programme was unchanged at \$7bn per year for the next few years (with a small increase from \$6bn to \$7bn in 2021). We had anticipated a rise in the bond programme to fund the new government's spending plans, but a higher nominal GDP forecast and a better fiscal starting point have made that unnecessary, for now. We suspect we weren't the only ones looking for a bigger bond programme, as New Zealand government yields fell, by up to 8 basis points at the long end, despite rising yields in Australia on the back of the employment report. The December 2017 NZGB

matures today, alongside a number of other bonds, which is also supporting demand for New Zealand bonds. There was no impact on the NZD.

Nick.Smyth@bnz.co.nz

Coming Up

		Period	Cons.	Prev.	NZT
NZ	BusinessNZ Manufacturing PMI	Nov		57.2	10:30
JN	Tankan Large Mfg Outlook	4Q	22	19	12:50
US	Industrial Production MoM	Nov	0.3	0.9	03:15

Source: Bloomberg, BNZ

Foreign Exchange								Equities				Commodities**			
Indicative overnight ranges (*)					Other FX			Major Indices				Price			
	Last	% Day	Low	High		Last	% Day		Last	% Day	% Year		Last	Net Day	
NZD	0.6998	-0.4	0.6978	0.7012	CHF	0.9893	+0.4		S&P 500	2,663	-0.0	18.2	Oil (Brent)	62.83	+0.6
AUD	0.7673	+0.5	0.7651	0.7675	SEK	8.418	+0.1		Dow	24,570	-0.1	24.1	Oil (WTI)	56.84	+0.4
EUR	1.1786	-0.3	1.1771	1.1863	NOK	8.280	-0.5		Nasdaq	6,880	+0.1	26.6	Gold	1257.5	+0.7
GBP	1.3436	+0.1	1.3393	1.3466	HKD	7.808	+0.1		Stoxx 50	3,556	-0.7	10.7	HRC steel	640.0	-0.3
JPY	112.37	-0.2	112.34	112.88	CNY	6.609	-0.2		FTSE	7,448	-0.6	7.2	CRB	184.0	+0.4
CAD	1.2787	-0.2			SGD	1.346	-0.0		DAX	13,068	-0.4	16.2	Wheat Chic.	431.3	+0.5
NZD/AUD	0.9120	-0.8			IDR	13,576	-0.1		CAC 40	5,357	+0.0	12.3	Sugar	13.77	-0.5
NZD/EUR	0.5938	-0.1			THB	32.50	-0.1		Nikkei	22,694	-0.3	17.7	Cotton	74.91	+1.1
NZD/GBP	0.5208	-0.5			KRW	1,089	-0.2		Shanghai	3,292	-0.3	5.6	Coffee	120.3	+0.1
NZD/JPY	78.64	-0.5			TWD	30.01	-0.1		ASX 200	6,011	-0.2	8.5	WM powder	2975.0	-0.5
NZD/CAD	0.8948	-0.6			PHP	50.48	+0.1		NZX 50	8,324	+0.5	23.3	Australian Futures		
NZ TWI	73.93	-0.5											3 year bond	97.95	-0.05
													10 year bond	97.45	-0.03
Interest Rates								NZ Government Bonds				NZ Swap Yields			
	Rates				Benchmark 10 Yr Bonds		Last				Last				
	Cash	3Mth	2 Yr	10 Yr	Last	Net Day									
USD	1.50	1.59	2.01	2.35	USD	2.35	0.01	NZGB 3 04/15/20	1.93	-0.02		1 year	1.99	-0.00	
AUD	1.50	1.77	1.95	2.70	AUD	2.56	0.03	NZGB 6 05/15/21	2.09	-0.01		2 year	2.18	0.00	
NZD	1.75	1.86	2.18	3.10	NZD	2.76	-0.06	NZGB 5 1/2 04/15/23	2.35	-0.03		5 year	2.63	-0.02	
EUR	0.00	0.06	-0.19	0.79	GER	0.32	0.00	NZGB 2 3/4 04/15/25	2.62	-0.05		7 year	2.85	-0.02	
GBP	0.50	0.52	0.79	1.26	GBP	1.17	-0.04	NZGB 4 1/2 04/15/27	2.76	-0.06		10 year	3.10	-0.02	
JPY	-0.03	-0.02	0.04	0.25	JPY	0.05	0.00	NZGB 3 1/2 04/14/33	3.10	-0.06		15 year	3.34	-0.02	
CAD	1.00	1.17	1.88	2.21	CAD	1.85	0.01	NZGB 2 3/4 04/15/37	3.29	-0.08					

* 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 07:01

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

Currency Strategist
+61 2 9293 7109

Gavin Friend

Senior Markets Strategist
+44 20 7710 2155

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