

15 February 2018



Events Round-Up

NZ: Food prices (m/m%), Jan: 1.2 vs. -0.8 prev.
AU: Westpac consumer confid., Feb: 102.7 vs. 105.1 prev.
JN: GDP (q/q%), Q4: 0.1 vs. 0.2 exp.
NZ: 2yr inflation expectations, Q1: 2.11 vs. 2.02 prev.
GE: GDP (q/q%), Q4: 0.6 vs. 0.6 exp.
EC: Industrial production (y/y%), Dec: 5.2 vs. 4.2 exp.
EC: GDP (q/q%), Q4: 0.6 vs. 0.6 exp.
US: CPI ex food, energy (m/m%), Jan: 0.3 vs. 0.2 exp.
US: CPI ex food, energy (y/y%), Jan: 1.8 vs. 1.7 exp.
US: Retail sales x auto, gas (m/m%), Jan: -0.2 vs. 0.3 exp.

Good Morning

US CPI data were stronger than expected, however the positive impact on the USD quickly faded. US Treasury yields are higher, but that hasn't stopped US equities recovering further.

The core US CPI rose by 0.3% m/m in January, 0.1 percentage points ahead of market expectations and a slither away from being rounded up to 0.4%. The data added to the case that last year's dip in inflation was temporary, with a recovery in some of the components that had held inflation lower. The three-month annualised rate of core inflation is now a hefty 2.9%, the fastest rate since 2011. Released at the same time, US retail sales were much weaker than expected, alongside a downward revision to the previous month.

The market put more weight on the CPI than retail sales data, which saw US Treasury rates higher across the curve and added to the chance that the Fed would revise up its rate projection for this year from three hikes to four at its March update. The market still prices in less than three hikes (67bps) for 2018, albeit higher than the 58bps priced in yesterday. The 2-year rate is up 6bps to 2.16% and the 10-year rate is up 6bps to 2.89%, a fresh four-year high.

US equities (S&P500) opened 0.5% weaker after the inflation and retail sales data but have recovered to be currently up 0.6%, on track to record a fourth consecutive daily increase. Clearly, the buy-the-dip brigade is in charge following the meltdown over the previous couple of weeks, being unperturbed by the higher interest rate outlook.

The USD rose by 0.5% after the CPI data but within 90 minutes had given up all of that gain and more, with no obvious reason for the reversal. One economic reason would be that the USD shouldn't have appreciated in the first place if one takes the view that higher inflation simply offsets higher nominal rates leaving real rates the same or even lower, while the retail sales data portray a softer economic picture.

Despite wider ranges since the NZ close, net currency movements have been modest, with most of the apparent USD weakness for the day as a whole reflecting a swoon late yesterday afternoon. The NZD is currently trading around 0.7340, only a touch higher from the NZ 5pm level yesterday, after falling as low as 0.7240 immediately after the US CPI figure. The high overnight was 0.7351 so the range has been more than one cent. The strong 5pm close yesterday followed a slightly higher 2-year inflation expectations figure from the RBNZ survey, a survey that doesn't deserve the light of day to be frank and one that the RBNZ has recently suggested is now "unreliable". The survey release coincided with a bout of broadly-based USD selling which explains most of the 60pip move leading into that close.

Earlier in the day, NZ food price inflation data for January were much weaker than expected – the 1.2% gain for the month was minus 0.6% after seasonal adjustment. Alongside a fall in petrol prices the data raised the risk that CPI inflation falls to 1.0% in Q1 or even below the bottom of the target band. This could increase chatter about the possibility of a rate cut in the months ahead but we still think that the medium-term outlook for higher inflation would ultimately prevent such a move. However, the stripes of the incoming Governor will matter a great deal. The local rates market was unmoved by the data, with the 2-year rate steady at 2.15% and a modest fall in longer term rates being more a reflection of global forces. The 10-year swap rate fell by 3bps to 3.26%, but higher rates overnight should see that move reversed today.

Looking at other currencies, GBP has been the only notable mover since the NZ close, trading up to 1.3980 on no fresh news. Yesterday afternoon, USD/JPY broke down through the 2017 low of 107.32, largely driven by the aforementioned USD weakness. Overnight it has traded down to 106.72. Japan Q1 GDP data were softer than expected, after a strong run and didn't impact the market. Euro-area GDP for Q4 was strong, in line with the advance estimate. EUR/USD has recovered to trade

above 1.24. NZD/AUD moved up through the 0.93 mark, with the AUD failing to keep pace.

The local trading session sees the release of REINZ housing market data and Australian employment data, where the unemployment rate is expected to be steady at 5.5%. There are a number of US economic releases but none of them top-tier. Further pondering over the impact of the US inflation data is likely to be the key driver of markets.

jason.k.wong@bnz.co.nz

Coming Up

		Period	Cons.	Prev.	NZT
NZ	REINZ house sales (y/y%)	Jan		-10.1	09:00
AU	Employment change ('000)	Jan	15	34.7	13:30
AU	Unemployment rate (%)	Jan	5.5	5.5	13:30
NZ	NZ to sell \$200m 2025 bonds				14:05
US	PPI ex food and energy (y/y%)	Jan	2	2.3	02:30
US	Philly Fed business outlook	Feb	21.6	22.2	02:30
US	Industrial production (m/m%)	Jan	0.2	0.9	03:15
US	NAHB housing market index	Feb	72	72	04:00

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	0.7345	+1.0	0.7240	0.7351	CHF	0.9302	-0.5	S&P 500	2,678	+0.6	14.6	Oil (Brent)	63.20	+0.8
AUD	0.7894	+0.4	0.7773	0.7894	SEK	7.994	-0.4	Dow	24,672	+0.2	20.3	Oil (WTI)	59.53	+0.6
EUR	1.2418	+0.5	1.2276	1.2420	NOK	7.834	-0.6	Nasdaq	7,084	+1.0	22.5	Gold	1348.0	+1.5
GBP	1.3982	+0.6	1.3800	1.3984	HKD	7.822	-0.0	Stoxx 50	3,370	+0.9	1.8	HRC steel	745.0	+0.1
JPY	107.03	-0.7	106.72	107.54	CNY	6.342	+0.0	FTSE	7,214	+0.6	-0.8	CRB	191.2	+0.7
CAD	1.2548	-0.3			SGD	1.316	-0.5	DAX	12,339	+1.2	4.8	Wheat Chic.	468.3	-1.2
NZD/AUD	0.9305	+0.5			IDR	13,629	-0.2	CAC 40	5,165	+1.7	5.5	Sugar	13.55	+0.5
NZD/EUR	0.5915	+0.4			THB	31.35	-0.4	Nikkei	21,154	-0.4	8.8	Cotton	75.41	-1.2
NZD/GBP	0.5253	+0.4			KRW	1,077	-0.7	Shanghai	3,199	+0.4	-0.4	Coffee	125.3	+0.2
NZD/JPY	78.61	+0.2			TWD	29.27	-0.3	ASX 200	5,841	-0.3	0.6	WM powder	3190.0	-0.3
NZD/CAD	0.9217	+0.6			PHP	52.06	-0.0	NZX 50	8,059	-0.8	12.2	Australian Futures		
NZ TWI	75.39	+0.6										3 year bond	97.83	-0.04
												10 year bond	97.08	-0.07

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	1.84	2.43	2.91	USD	2.89	0.07	NZGB 3 04/15/20	1.86	-0.00	1 year	1.98	-0.00
AUD	1.50	1.76	2.05	3.08	AUD	2.85	-0.03	NZGB 6 05/15/21	2.05	-0.01	2 year	2.15	-0.00
NZD	1.75	1.89	2.17	3.30	NZD	2.94	-0.04	NZGB 5 1/2 04/15/23	2.39	-0.01	5 year	2.71	-0.02
EUR	0.00	0.06	-0.13	1.16	GER	0.76	0.01	NZGB 2 3/4 04/15/25	2.70	-0.03	7 year	2.99	-0.02
GBP	0.50	0.54	1.02	1.71	GBP	1.64	0.02	NZGB 4 1/2 04/15/27	2.94	-0.04	10 year	3.26	-0.03
JPY	-0.03	-0.07	0.05	0.29	JPY	0.07	-0.01	NZGB 3 1/2 04/14/33	3.30	-0.04	15 year	3.51	-0.03
CAD	1.25	1.17	2.18	2.71	CAD	2.36	0.04	NZGB 2 3/4 04/15/37	3.45	-0.04			

* 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 06:50

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

ANALYST DISCLAIMER: The person or persons named as the author(s) of this report hereby certify that the views expressed in the research report accurately reflect their personal views about the subject securities and issuers and other subject matters discussed. No part of their compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in the research report. Research analysts responsible for this report receive compensation based upon, among other factors, the overall profitability of the Markets Division of National Australia Bank Limited, a member of the National Australia Bank Group ("NAB"). The views of the author(s) do not necessarily reflect the views of NAB and are subject to change without notice. NAB may receive fees for banking services provided to an issuer of securities mentioned in this report. NAB, its affiliates and their respective officers, and employees, including persons involved in the preparation or issuance of this report (subject to the policies of NAB), may also from time to time maintain a long or short position in, or purchase or sell a position in, hold or act as advisors, brokers or commercial bankers in relation to the securities (or related securities and financial instruments), of companies mentioned in this report. NAB or its affiliates may engage in these transactions in a manner that is inconsistent with or contrary to any recommendations made in this report.

NEW ZEALAND DISCLAIMER: This publication has been provided for general information only. Although every effort has been made to ensure this publication is accurate the contents should not be relied upon or used as a basis for entering into any products described in this publication. Bank of New Zealand strongly recommends readers seek independent legal/financial advice prior to acting in relation to any of the matters discussed in this publication. Neither Bank of New Zealand nor any person involved in this publication accepts any liability for any loss or damage whatsoever may directly or indirectly result from any advice, opinion, information, representation or omission, whether negligent or otherwise, contained in this publication.

USA DISCLAIMER: If this document is distributed in the United States, such distribution is by nabSecurities, LLC. This document is not intended as an offer or solicitation for the purchase or sale of any securities, financial instrument or product or to provide financial services. It is not the intention of nabSecurities to create legal relations on the basis of information provided herein.

National Australia Bank Limited is not a registered bank in New Zealand.