

15 January 2018



Events Round-Up

NZ: Building permits (m/m%), Nov: 10.8 vs. -10.4 prev.
US: CPI ex food and energy (m/m%), Dec: 0.3 vs. 0.2 exp.
US: CPI ex food and energy (y/y%), Dec: 1.8 vs. 1.7 exp.
US: Retail sales ex auto,gas (m/m%), Dec: 0.4 vs. 0.4 exp.

Good Morning

On Friday, political developments saw a surge in EUR and GBP, while the USD and the NZD underperformed. Stronger US inflation and retail sales data saw only a temporary move up in US 10-year Treasury yields.

On Friday evening news came through that German Chancellor Merkel might finally be in a position to form a government. Merkel's CDU, its sister party the CSU and the left-leaning SPD released a 28-page document outlining some common ground and will recommend to their party members to back the formation of another German Grand Coalition. The main hurdle now seems to be the SPD endorsing the move at its conference this weekend. The market took the news positively, sending the EUR on a higher plane. EUR/USD closed near its high for the day just above 1.22, up 1.4% for the day and its highest level in three years.

This news had a positive spillover for GBP which itself was later boosted by reports that Spanish and Dutch finance ministers had agreed to push for a Brexit deal that keeps Britain as close to the European Union as possible. GBP also ended the day up 1.4% to 1.3730, its highest level since the Brexit referendum.

These moves came even as US data surprised on the upside. While core US retail sales growth for December was in line, revisions were positive that will lead to upward revisions to Q4 GDP estimates. The Atlanta Fed's GDPNow estimate for Q4 GDP growth rose from 2.8% to 3.3%. Importantly, for a change, core US CPI data surprised to the upside at 0.3% m/m, lending some weight to Fed Chair Yellen's view that last year's inflation weakness was temporary in nature. The implied probability of another rate hike by March moved up to about 88% according to Fed Fund futures. The 2-year Treasury rate broke up through the 2% mark for the first time since 2008 and finished the day up 2bps at 2.00%. The 10-year rate shot up 5bps to a peak of 2.59% before

buyers returned and sent the yield all the way back down, closing up by less than 1bp at 2.55%. This behaviour suggests that the 2.6% mark is an area of technical resistance and might be hard to crack over the short term.

One might have expected a stronger USD to prevail after the stronger than expected data, but support for the USD was fleeting and it ended lower for the day against all the majors apart from the NZD. The DXY nudged down through the low of last September although broader USD indices still remain above that nadir. Nevertheless, if stronger than expected data and rising expectations for Fed tightening can't support the USD then it raises some serious questions about what could support the USD this year. One economic theory is that the rising dual fiscal and current account deficit will act as a headwind for the USD this year, despite higher interest rates.

The NZD's underperformance likely represents some fatigue after its storming performance at the end of last year and early this year. It peaked at 0.7276 during local trading hours and failed to make any headway after the local close, hovering around the 0.7250 mark where it closed the week. CFTC positioning data showed that the extent of short speculative positioning moderated in the week ending 9 January from the extreme short positioning reached at the end of last year. While this provides a low hurdle for further upside potential on any positive news, we suspect that the strong recovery for the NZD will soon run out of steam.

NZD/EUR and NZD/GBP fell a chunky 1.5% for the day to around 0.5940 and 0.5280 respectively. Our projections show EUR and GBP as our two favoured major currencies for 2018, suggesting plenty more downside for these two NZD crosses through the year.

The day ahead will be quiet with the US public holiday and the global economic calendar is fairly light for the week ahead. Key releases for Australia and China are towards the end of the week, as is another expected rate hike from the Bank of Canada.

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Coming Up

	Period	Cons.	Prev.	NZT
NZ Food Prices (m/m%)	Dec		-0.4	10:45

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	0.7252	-0.3	0.7220	0.7264	CHF	0.9673	-0.9		S&P 500	2,786	+0.7	22.5	Oil (Brent)	69.87	+0.9
AUD	0.7917	+0.3	0.7848	0.7895	SEK	8.050	-1.0		Dow	25,803	+0.9	29.8	Oil (WTI)	64.30	+0.8
EUR	1.2202	+1.4	1.2040	1.2156	NOK	7.920	-1.2		Nasdaq	7,261	+0.7	30.3	Gold	1334.9	+0.9
GBP	1.3728	+1.4	1.3538	1.3700	HKD	7.822	-0.0		Stoxx 50	3,613	+0.5	8.7	HRC steel	669.0	+0.5
JPY	111.06	-0.2	110.97	111.69	CNY	6.469	-0.6		FTSE	7,779	+0.2	6.0	CRB	196.1	+0.5
CAD	1.2459	-0.5			SGD	1.324	-0.4		DAX	13,245	+0.3	13.9	Wheat Chic.	434.3	-2.8
NZD/AUD	0.9160	-0.5			IDR	13,353	-0.4		CAC 40	5,517	+0.5	12.1	Sugar	14.18	+0.0
NZD/EUR	0.5943	-1.5			THB	31.95	-0.2		Nikkei	23,654	-0.2	22.6	Cotton	81.68	-1.2
NZD/GBP	0.5283	-1.5			KRW	1,065	-0.7		Shanghai	3,429	+0.1	10.2	Coffee	122.3	-0.4
NZD/JPY	80.54	-0.4			TWD	29.62	+0.0		ASX 200	6,070	+0.0	6.1	WMI powder	3035.0	+0.0
NZD/CAD	0.9035	-0.6			PHP	50.36	-0.0		NZX 50	8,242	-0.1	17.0	Australian Futures		
NZ TWI	75.11	-0.7											3 year bond	97.825	0.01
													10 year bond	97.23	-0.01
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		Last				
USD	1.50	1.72	2.19	2.54	USD	2.55	0.01	NZGB 3 04/15/20	1.95	-0.03	1 year	1.99	-0.01		
AUD	1.50	1.80	2.03	2.90	AUD	2.75	0.02	NZGB 6 05/15/21	2.13	-0.02	2 year	2.21	-0.01		
NZD	1.75	1.87	2.21	3.20	NZD	2.85	-0.02	NZGB 5 1/2 04/15/23	2.39	-0.02	5 year	2.71	-0.01		
EUR	0.00	0.06	-0.13	0.96	GER	0.58	0.00	NZGB 2 3/4 04/15/25	2.66	-0.02	7 year	2.95	-0.01		
GBP	0.50	0.52	0.87	1.40	GBP	1.34	0.03	NZGB 4 1/2 04/15/27	2.85	-0.02	10 year	3.20	-0.01		
JPY	-0.03	-0.03	0.05	0.27	JPY	0.08	0.01	NZGB 3 1/2 04/14/33	3.17	-0.02	15 year	3.45	-0.01		
CAD	1.00	1.17	2.12	2.49	CAD	2.17	0.01	NZGB 2 3/4 04/15/37	3.32	-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: NY close Sat morning

Source: Bloomberg

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