

17 September 2018



## Events Round-Up

NZ: Manufacturing PMI, Aug: 52 vs. 51.2 prev.

CH: Retail sales (y/y%), Aug: 9 vs. 8.8 exp.

CH: Industrial production (y/y%), Aug: 6.1 vs. 6.1 exp.

CH: Fixed asset investment (y/y%), Aug: 5.3 vs. 5.6 exp.

US: Retail sales ex auto and gas (m/m%), Aug: 0.2 vs. 0.5 exp.

US: Retail sales control group (m/m%), Aug: 0.1 vs. 0.4 exp.

US: University of Michigan sentiment, Sep: 100.8 vs. 96.6 exp.

## Good Morning

On Friday, the US 10 year Treasury yield hit 3% for the first time since the start of August after another round of robust US economic data. The USD was stronger on the day, but remains contained within a broader range. Over the weekend the WSJ reported that President Trump would announce tariffs of 10%, lower than the originally planned 25%, on \$200b of Chinese imports, likely either today or tomorrow. It's possible that risk assets could bounce on the news of a lower tariff rate.

There have been several media reports on Trump's thinking around Chinese tariffs since Friday. On Friday, Bloomberg reported that Trump had instructed officials to press ahead with the planned \$200b of tariffs on Chinese imports, and that he wasn't concerned about implementing these before talks with China, led by US Treasury Secretary Steve Mnuchin, potentially restart over the next few weeks. That account was backed up by a report from the WSJ over the weekend, that said Trump would go ahead with the tariffs, probably over the next few days, but at a lower 10% tariff rate (rather than the 25% originally proposed). As a consequence, China is considering declining the invitation from Mnuchin to resume talks. It's possible that risk assets and the NZD and AUD might bounce somewhat over the coming few sessions if the lower 10% tariff rate is formally adopted, as most market participants were resigned to the fact that Trump would go ahead with the tariffs in any case.

As far as US equities were concerned, there was little impact from the Bloomberg report on Friday that Trump would go ahead with tariffs. The S&P500 fell 0.4% intraday after the headlines hit the screens, but the reaction was fleeting and US equity markets closed unchanged on Friday. The muted market reaction

suggests that the \$200b tariff threat is probably 'priced-in' to a large extent and the burden of proof is on US economic data and corporate earnings to show that the trade war is having a meaningful impact on the US economy. The VIX declined to just 12, which also suggests the market is taking a fairly sanguine (although sceptics might say complacent) view of the trade stand-off with China.

US Treasury yields were higher across the curve on Friday, with the 10 year rate closing just below 3%, 3bps higher on the day. The 10 year yield has increased 15bps over the past two weeks. US retail sales came in below expectations for August, but prior months were revised higher, and both the USD and US yields received a boost from its release. The Atlanta Fed's GDPNow estimate for Q3 was revised from 3.8% to 4.4% after the retail sales release, suggesting the revisions to prior months dominated the downside surprise in August. Later, the University of Michigan consumer confidence index rose sharply, to near its highest levels of the current expansion. Like US equities, there was little impact on US Treasury yields from the tariff reports.

The overall picture from recent US data is that the US economy continues to perform strongly and wage and price inflation appears to be heading gradually higher. There remains little evidence of trade war fears affecting US economic activity at this stage. Chicago Fed President Evans, who historically has been seen as one of the more dovish voices on the committee, noted that the economy was "*firing on all cylinders*" and said it would be "*quite normal and consistent*" if the Fed took its cash rate above neutral over the next few years. The market prices just less than two hikes for 2019, although that remains below the Fed's median projection from the last FOMC meeting of three. We continue to think there are upside risks to US Treasury yields from here.

The USD was stronger on Friday, helped by the increase in rates on the back of the stronger US data and also, to a lesser extent, the later Bloomberg report on Trump's planned tariffs. The DXY rose 0.4%, but it was still down for the week and remains well contained within the range that has been in place since June.

Tariff threats and trade war news continue to have a more pronounced impact on Chinese equities, the CNH and the AUD. The CSI300 was up a meagre 0.2% on Friday, despite strong gains across most other Asian markets. The CSI300 has fallen almost 20% this year versus the 9%

gain in the S&P500.

The CNH was around 0.6% weaker on Friday, although most of that move had occurred in advance of the reports that Trump would press ahead with tariffs on Chinese imports. The CNH has now completely reversed the gains made mid-week after the WSJ first reported that Treasury Secretary Mnuchin had reached out to the Chinese to resume talks. Chinese activity data on Friday was a mixed bag, with retail sales stronger but fixed asset investment continuing to decline (the combination of which is not particularly surprising in light of the Chinese authorities' desire to reorient the economy towards services and away from heavy industry).

Coming only a day after Turkey's huge 625bp rate hike, the Russian central bank hiked its policy rate by 25bps to 7.5% in a surprise move (only one of 42 economists had expected a hike). The Russian Ruble was up slightly on the day despite a 0.3% fall in the JPM EMFX index. Continued Fed tightening and further strength in the USD against EM currencies is likely to see further monetary tightening from affected EM central banks, as they seek to stem currency weakness and keep inflation under control.

The NZD closed at 0.6545 on Friday, down around 0.4% on the day. The NZD spent most of the local session grinding higher towards 0.6590, before reversing those moves during the New York session amidst the USD strength. The NZ PMI improved marginally to 52 on Friday, but it remains stuck below its long-term average.

New orders and production indices improved but, balanced against that, employment fell back into contractionary territory. Today brings the Services version of the PMI, but all eyes will be on GDP which is released on Thursday. Bloomberg reports the median consensus estimate is for a 0.8% rise on the quarter, which is above both our 0.6% and the RBNZ's 0.5% predictions.

NZ rates again saw little movement on Friday, although there should be some modest upward pressure in long-end rates today. NZ inflation-indexed bonds continued to perform strongly however, with the 10 year breakeven inflation rate rising another 4bps to 1.35%, bringing its rise on the week to 15bps.

It's a relatively quiet week data-wise in the US, and most of the focus will be on the FOMC meeting on the 27<sup>th</sup> September (NZ time). ECB President speaks on Tuesday and Thursday and the European PMIs are released on Friday night. Much focus will again centre on the prospective US tariffs on China.

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### Coming Up

		Period	Cons.	Prev.	NZT
NZ	Performance Services Index	Aug		55.1	10:30
EC	CPI Core YoY	Aug F	1	1	21:00
EC	CPI YoY	Aug F	2	2.1	21:00

Source: Bloomberg, BNZ.

Foreign Exchange							Equities				Commodities**		
Indicative overnight ranges (*)				Other FX			Major Indices				Price		
	Last	% Day	Low	High		Last	% Day			Last	% Day	Net Day	
NZD	0.6545	-0.4	0.6543	0.6596	CHF	0.9684	+0.3			Oil (Brent)	78.09	-0.1	
AUD	0.7153	-0.6	0.7154	0.7216	SEK	9.051	+1.1			Oil (WTI)	68.99	+0.6	
EUR	1.1625	-0.6	1.1624	1.1722	NOK	8.257	+0.5			Gold	1196.2	-0.5	
GBP	1.3068	-0.3	1.3062	1.3143	HKD	7.847	-0.0			HRC steel	837.0	+0.5	
JPY	112.06	+0.1	111.75	112.17	CNY	6.868	+0.3			CRB	190.5	-0.5	
CAD	1.3036	+0.3			SGD	1.374	+0.3			Wheat Chic.	530.3	+2.4	
NZD/AUD	0.9150	+0.1			IDR	14,807	-0.2			Sugar	11.16	-4.5	
NZD/EUR	0.5630	+0.2			THB	32.70	+0.2			Cotton	81.90	+0.3	
NZD/GBP	0.5008	-0.1			KRW	1,117	-0.5			Coffee	99.7	-0.9	
NZD/JPY	73.34	+0.2			TWD	30.74	-0.2			WM powder	2685.0	-1.3	
NZD/CAD	0.8532	+0.0			PHP	53.95	-0.2			<b>Australian Futures</b>			
NZ TWI	71.48	+0.3								3 year bond	97.945	0.01	
										10 year bond	97.37	-0.02	
<b>Interest Rates</b>													
	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	2.00	2.33	2.96	3.06	USD	3.00	0.03	NZGB 6 05/15/21	1.67	0.01	1 year	1.93	-0.01
AUD	1.50	1.92	2.03	2.80	AUD	2.60	-0.00	NZGB 5 1/2 04/15/23	1.89	0.01	2 year	1.98	-0.00
NZD	1.75	1.89	1.98	2.82	NZD	2.37	0.01	NZGB 2 3/4 04/15/25	2.15	0.00	5 year	2.31	0.00
EUR	0.00	0.06	-0.15	0.94	GER	0.45	0.03	NZGB 4 1/2 04/15/27	2.37	0.01	7 year	2.55	0.00
GBP	0.75	0.80	1.13	1.61	GBP	1.53	0.03	NZGB 3 04/20/29	2.55	0.00	10 year	2.82	0.00
JPY	-0.06	-0.04	0.06	0.34	JPY	0.12	0.01	NZGB 3 1/2 04/14/33	2.73	0.00	15 year	3.08	0.00
CAD	1.50	1.17	2.47	2.73	CAD	2.35	0.02	NZGB 2 3/4 04/15/37	2.88	0.00			

\* 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: New York Close

Source: Bloomberg

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