

18 June 2018



Events Round-Up

NZ: Manufacturing PMI, May: 54.5 vs. 58.9 prev.

JN: BoJ 10-yr yield target, Jun: 0.0 vs. 0.0 exp.

US: Industrial production (m/m%), May: -0.1 vs. 0.2 exp.

US: U. of Mich. cons. sent., Jun: 99.3 vs. 98.5 exp.

US: Empire manufacturing, Jun: 25 vs. 18.8 exp.

Good Morning

After much anticipation, the US administration announced tariffs on \$50b of Chinese imports on Friday with the Chinese government responding in-kind later that day. Commodities, commodity currencies and emerging markets reacted negatively to the threat of a "trade war", although there has been little impact (yet) on US equities or bonds. Against this backdrop, the NZD has fallen to 0.6950, a three-week low.

The big news on Friday was the US administration's decision to impose 25% tariffs on \$50b of Chinese imports, as had been foreshadowed by various media reports earlier in the week. Tariffs that affect 818 products worth \$34bn in annual trade are due to come into effect on 6 July with the US administration saying it would consult on tariffs on the other \$16bn of products, and would apply these later. It didn't take long for China to respond, with the Ministry of Finance announcing on Saturday morning that it would impose 25% tariffs on \$50b of imported US goods (heavily tilted towards agricultural products). The Chinese ministry also said that the previous agreements reached in the bilateral US-China trade negotiations were now off the table.

With President Trump having said he would respond to Chinese retaliation with yet more tariffs, the stage is potentially set for more escalation in the trade conflict. On Friday, Reuters reported that US officials were close to finalizing a second list of tariffs worth \$100b (requested by Trump back in April) while US Trade Representative Lighthizer said that the US would announce investment restrictions on China in the next two weeks.

While an all-out trade war would be unambiguously bad for global growth and risk assets, the US equity and bond market reaction was fairly muted. The S&P500 fell around 0.75% intraday in response to the trade news but rebounded to end the day only 0.1% lower (and flat for the week). Meanwhile, the 10 year Treasury yield was down a

modest 2bps on the day, to 2.92%. It's possible the market sees Trump's decision to impose Chinese tariffs as part of a negotiating strategy that will ultimately lead to compromise (he has after all made numerous policy U-turns during his term in office), although the verdict is still out. The IMF warned last week that retaliatory tariffs would have "serious" macroeconomic implications.

Commodities bore the brunt of the tariff-related news on Friday, with Brent crude oil down over 3%, copper down over 2% and soybeans (which China has targeted with tariffs) down 2%. Last week's weak Chinese data (retail sales, fixed asset investment and industrial production) had already raised concerns about a slowdown in the Chinese economy, and the risk is that trade tariffs will further harm demand for commodities. The CRB commodity index fell 1.4% to a two-month low. OPEC and Russia meet later this week in Vienna amidst the prospect of an increase in oil supply (although Iran over the weekend said that it, along with Iraq and Venezuela, planned to veto any supply increase).

There was also weakness in Asian EM currencies on Friday, with the South Korean Won down 1.3% and the Thai Baht down almost a percent. The JP Morgan emerging market currency index is near its lowest level since November 2016.

Against a backdrop of commodity weakness and some growing trade war fears, the NZD fell around 0.4% on Friday, with similar moves seen in the AUD and CAD. Most of the move lower in the NZD occurred during the Asian session, with the currency fairly range-bound after the NZ close. There was little impact in FX from stronger US consumer confidence and Empire manufacturing surveys, with the data very much overshadowed by news on trade.

The EUR recovered slightly from the large falls seen in the aftermath of the ECB meeting on Thursday night. The EUR was up 0.3% on the day to just above 1.16, although it remains near year-to-date lows. The ECB's Sintra conference starts this week and the market will closely watch the speech given by ECB President Draghi, although we would be surprised if his message materially deviated from that given at the ECB meeting last week. Several other central bankers will be speaking at Sintra including Fed Chair Powell.

Also ahead this week is the BoE meeting on Thursday (no change expected) and the European flash PMIs. The latter will garner attention given the slow-down in European

activity indicators this year. Locally, NZ GDP is released on Thursday, and we are looking for a 0.5% increase on the quarter (albeit with downside risks), in line with consensus.

nick.smyth@bnz.co.nz

Coming Up

		Period	Cons.	Prev.	NZT
NZ	Performance of services index	May		55.9	10:30
US	NAHB housing market index	Jun	70	70	02:00
US	Fed's Bostic speaks on monetary policy outlook				05:00
EC	ECB's Draghi gives opening remarks at Sintra conferenc				05:30

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	0.6949	-0.4	0.6928	0.6977	CHF	0.9976	+0.1		S&P 500	2,780	-0.1	14.2	Oil (Brent)	73.44	-3.3
AUD	0.7442	-0.5	0.7440	0.7480	SEK	8.786	+0.5		Dow	25,090	-0.3	17.3	Oil (WTI)	65.06	-2.7
EUR	1.1610	+0.4	1.1543	1.1627	NOK	8.147	+0.1		Nasdaq	7,746	-0.2	25.9	Gold	1278.5	-2.3
GBP	1.3278	+0.1	1.3212	1.3298	HKD	7.849	+0.0		Stoxx 50	3,505	-0.6	-1.5	HRC steel	904.0	+0.0
JPY	110.66	+0.0	110.39	110.90	CNY	6.439	+0.6		FTSE	7,634	-1.7	1.8	CRB	196.2	-1.4
CAD	1.3184	+0.6			SGD	1.351	+0.5		DAX	13,011	-0.7	1.9	Wheat Chic.	534.3	-1.1
NZD/AUD	0.9338	+0.0			IDR	13,932	+0.4		CAC 40	5,502	-0.2	4.6	Sugar	12.35	-1.7
NZD/EUR	0.5985	-0.9			THB	32.67	+1.5		Nikkei	22,852	+0.5	14.6	Cotton	89.85	-3.3
NZD/GBP	0.5233	-0.7			KRW	1,098	+1.4		Shanghai	3,022	-0.7	-3.2	Coffee	117.6	-0.3
NZD/JPY	76.90	-0.4			TWD	30.01	+0.3		ASX 200	6,094	+1.3	5.5	WM powder	3200.0	-0.2
NZD/CAD	0.9162	+0.3			PHP	53.34	+0.4		NZX 50	8,976	-0.0	18.8	Australian Futures		
NZ TWI	73.69	-0.1											3 year bond	97.845	0.00
													10 year bond	97.30	0.00
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	Net Day	Last	Net Day	Last	Net Day	Last	Net Day	
USD	2.00	2.33	2.82	2.98	USD	2.92	-0.01	NZGB 6 05/15/21	2.02	-0.02	1 year	2.09	-0.00		
AUD	1.50	2.06	2.10	2.89	AUD	2.69	-0.03	NZGB 5 1/2 04/15/23	2.29	-0.03	2 year	2.24	0.00		
NZD	1.75	2.01	2.23	3.12	NZD	2.75	-0.04	NZGB 2 3/4 04/15/25	2.56	-0.04	5 year	2.68	-0.02		
EUR	0.00	0.06	-0.17	0.92	GER	0.40	-0.02	NZGB 4 1/2 04/15/27	2.75	-0.04	7 year	2.90	-0.02		
GBP	0.50	0.63	1.00	1.55	GBP	1.33	-0.01	NZGB 3 04/20/29	2.91	-0.05	10 year	3.14	-0.03		
JPY	-0.07	-0.04	0.05	0.26	JPY	0.04	-0.01	NZGB 3 1/2 04/14/33	3.10	-0.05	15 year	3.40	-0.04		
CAD	1.25	1.17	2.24	2.61	CAD	2.22	-0.05	NZGB 2 3/4 04/15/37	3.24	-0.06					

* 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

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

Senior FX Strategist
+61 2 9293 7109

Gavin Friend

Senior Market Strategist
+44 20 7710 1588

Skye Masters

Head of Fixed Income Research
+61 2 9295 1196

Alex Stanley

Senior Interest Rate Strategist
+61 2 9237 8154

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.