

24 July 2018



Events Round-Up

EC: Consumer confidence, Jun: -0.6 vs -0.7 exp.

US: Existing home sales, Jun: 5.38m vs 5.44m exp.

Good Morning

Global yields moved higher again overnight, as speculation continued to mount ahead of the Bank of Japan monetary policy meeting next week. The PBOC injected liquidity via its MLF facility, and the depreciation in the CNY contributed to a lower AUD and NZD.

The Bank of Japan has been in focus the past two sessions after reports on Friday that BoJ officials were debating tweaks to their monetary policy framework ahead of their meeting next week. Following the reports, the 10 year government bond yield opened 6bps higher yesterday, at 0.09%, prompting the BoJ to intervene in the market – offering to buy unlimited quantities of 10 year JGBs at 11bps (the BoJ has a 10 year yield target of 0% and has intervened in the past when the rate has risen above 0.1%). While the BoJ's intervention stemmed the rise in the 10 year JGB – it closed yesterday at 0.085% - the longer-end of the Japanese curve continued to move higher, with the 30 year yield up almost 9bps – an extremely large move for Japan.

The BoJ is reportedly considering changes to its yield curve control framework to make its policy more sustainable. With the BoJ set to lower its inflation forecasts yet again, the implication is that it will be buying JGBs for even longer than it previously expected; it already owns more than 40% of the market. One way to make its programme more sustainable would be to cut JGB purchases altogether, unless the 10 year yield traded above its intervention threshold. But reports also suggest that one of the concerns among BoJ officials is that the flat yield curve is hurting bank profitability. The difficulty for the BoJ is that any changes to its programme, say for instance targeting the 5 year JGB at 0% and letting the 10 year yield rise, will likely strengthen the Japanese yen, pushing inflation even further away from its target. The yen was flat against the USD overnight, the best performing currency in the G10, while the Nikkei fell 1.3%.

The Asahi newspaper reported that BoJ policymakers wouldn't make a decision at this meeting, but would announce a review of its framework. Nevertheless, speculation continued to mount and the move in Japanese yields reverberated around other global bond markets. The 10 year Treasury yield, which was in an

exceptionally tight 8bp trading range for almost a month, broke higher – it is up 7bps to 2.96%. The 2s10s US yield curve steepened 3bps to 33bps. Japanese institutions are major investors in global fixed income markets (searching out higher returns than those available in Japan), and so the market is very sensitive to any potential changes that might incentivize them to switch back to JGBs. NZ rates went higher yesterday following the global moves, with the 10 year swap rate 3.5bps higher. We can expect a further rise in NZ rates and a steepening of the curve today.

Elsewhere, the PBOC injected \$74b of liquidity via its Medium-Term Lending Facility (MLF), its largest ever operation via this facility. Amidst further policy easing from China, the CNY weakened 0.4%, with USD/CNY approaching its highs for this year of 6.8. The CNY has fallen over 6% against the USD in little more than a month. The weakness in the CNY added some downward pressure to the AUD and the NZD, with both currencies falling around 0.5% overnight (the weakest performing currencies on the day).

The GBP had a brief dip after BoE Deputy Governor Broadbent said he didn't know whether he'd vote for an August rate rise. The fall wasn't sustained though (he was hardly going to say what he intended to do), and the GBP sits just above 1.31, down 0.3% on the day. Conservative cabinet minister Jeremy Hunt was the latest to sound a warning about UK-EU negotiations, saying that there was "a very real risk of a Brexit no deal by accident".

US equities are slightly higher on the day (S&P500 +0.2%, NASDAQ +0.3%), with financials leading the way higher on the back of higher bond yields and a steeper curve. Amazon shares fell initially after President Trump took aim at the company again on Twitter, although they have recovered to be down less than 1%. Earnings continue to provide support for the equity market, with 87% of companies this quarter having beaten earnings estimates (17% of companies have reported so far). Alphabet (Google's parent) reports earnings after the bell today.

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Coming Up

		Period	Cons.	Prev.	NZT
EC	Eurozone Manufacturing PMI	Jul P	54.7	54.9	20:00
EC	Eurozone Services PMI	Jul P	55.1	55.2	20:00
US	Markit US Manufacturing PMI	Jul P	55.1	55.4	01:45
US	Markit US Services PMI	Jul P	56.5	56.5	01:45

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	0.6781	-0.4	0.6777	0.6823	CHF	0.9931	+0.1			S&P 500	2,808	+0.2	13.6	Oil (Brent)	72.85	-0.3
AUD	0.7377	-0.5	0.7372	0.7429	SEK	8.867	+0.2			Dow	25,060	-0.0	16.1	Oil (WTI)	67.66	-0.9
EUR	1.1689	-0.3	1.1684	1.1743	NOK	8.199	+0.3			Nasdaq	7,840	+0.2	22.7	Gold	1224.2	-0.6
GBP	1.3099	-0.3	1.3083	1.3158	HKD	7.849	-0.0			Stoxx 50	3,454	-0.2	0.1	HRC steel	913.0	-0.7
JPY	111.48	+0.1	110.90	111.54	CNY	6.799	+0.4			FTSE	7,656	-0.3	2.7	CRB	192.5	-0.1
CAD	1.3175	+0.2			SGD	1.366	+0.2			DAX	12,549	-0.1	2.5	Wheat Chic.	532.3	-0.4
NZD/AUD	0.9192	+0.1			IDR	14,482	-0.1			CAC 40	5,378	-0.3	5.1	Sugar	11.08	-0.4
NZD/EUR	0.5801	-0.1			THB	33.44	+0.3			Nikkei	22,397	-1.3	12.1	Cotton	86.81	-0.3
NZD/GBP	0.5177	-0.2			KRW	1,131	-0.2			Shanghai	2,860	+1.1	-12.0	Coffee	111.7	+1.1
NZD/JPY	75.59	-0.4			TWD	30.64	-0.2			ASX 200	6,228	-0.9	9.5	WMI powder	2950.0	-0.2
NZD/CAD	0.8934	-0.2			PHP	53.49	+0.1			NZX 50	8,873	-0.9	15.5	Australian Futures		
NZ TWI	73.26	-0.2											3 year bond	97.835	-0.04	
													10 year bond	97.29	-0.05	
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	2.00	2.34	2.86	3.02	USD	2.96	0.07	NZGB 6 05/15/21	1.93	0.01	1 year	2.02	0.00			
AUD	1.50	1.99	2.16	2.90	AUD	2.67	0.05	NZGB 5 1/2 04/15/23	2.15	0.01	2 year	2.15	0.00			
NZD	1.75	1.92	2.15	3.03	NZD	2.63	0.02	NZGB 2 3/4 04/15/25	2.46	0.02	5 year	2.55	0.02			
EUR	0.00	0.06	-0.16	0.92	GER	0.41	0.04	NZGB 4 1/2 04/15/27	2.63	0.02	7 year	2.78	0.03			
GBP	0.50	0.76	1.06	1.53	GBP	1.27	0.04	NZGB 3 04/20/29	2.80	0.02	10 year	3.03	0.03			
JPY	-0.08	-0.04	0.05	0.30	JPY	0.09	0.05	NZGB 3 1/2 04/14/33	2.97	0.01	15 year	3.29	0.04			
CAD	1.50	1.17	2.32	2.63	CAD	2.23	0.06	NZGB 2 3/4 04/15/37	3.11	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: NZT 07:10

Source: Bloomberg

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