

24 October 2017

Events Round-Up

NZ: Net migration ('000), Sep: 5190 vs. 5420 prev.

CA: CPI (y/y%), Sep: 1.6 vs. 1.7 exp.

CA: Retail sales (m/m%), Aug: -0.3 vs. 0.5 exp.

US: Existing home sales (mn), Sep: 5.39 vs. 5.30 exp.

EC: Consumer Confidence, Oct: -1.0 vs. -1.1 exp.

Good Morning

The week has begun on a quiet note. The NZD is showing signs of forming a base after its initial swoon following the formation of a new government. Coming back from a long weekend, locals will note that the NZD is little changed on a TWI basis since leaving the office on Friday. It is slightly weaker against the USD and GBP and slightly higher against the other key developed currencies.

The USD has managed to hold onto gains seen since Friday, with sentiment for the dollar helped by the Senate passing a Budget resolution that allows for \$1.5tn of additional budget deficits over next 10 years and adds to the hope that tax reform can be agreed. To add to that, Trump opened the possibility of both Powell and Taylor in the Chair/Vice Chair roles when he concludes his Fed appointments, with Taylor in the mix seeing to be supportive of higher rates and a USD. Trump noted this morning that he is "very, very close" to making his decision. NZD/USD fell through Friday and into yesterday afternoon to a low of 0.6932, from which it showed a small gain to the current level around 0.6960.

NZD/GBP is down to 0.5270. GBP has been supported over the past couple of trading sessions as the language from the EU on Brexit appears more conciliatory, perhaps aware of PM May's political fragility and having her knocked out wouldn't be in best interests of the EU. European Council President Tusk confirmed that the EU and UK hope to move onto trade talks in December.

JPY was softer after PM Abe won his snap election decisively, paving the way for the continuation of the massive economic stimulus plan, including easier fiscal policy and Governor Kuroda likely being reappointed, helping extend the BoJ's asset purchase programme. This helped the Nikkei 225 index complete a 15-day winning streak, adding just over 1% to close at its highest level since 1996. USD/JPY hit some resistance at 114.10 and has fallen to 113.70. NZD/JPY is up a touch to 79.2.

EUR has been soft since Spain's PM Rajoy said that he will dismiss Catalan President Puigdemont and his government and take control of the regional police force, public television and radio channels. Elections will be held within six months. EUR is down to 1.1740 and NZD/EUR is up to 0.5930.

AUD has been out of the spotlight ahead of important CPI inflation data tomorrow. NZD/AUD got down to as low as 0.8883 early yesterday afternoon but has recovered to 0.8925. NZD/CAD is up to 0.8805, with much of the damage to CAD done after very weak retail sales data and slightly softer CPI data on Friday night saw a reduced chance of the BoC tightening again this year.

So the message on the NZD is one of base forming after falling around 2-2½% on most crosses on the sticker shock of a Labour-led government, which is vowing to make a significant change in economic direction. We await the details of the coalition agreement, due soon, before jumping to conclusions.

The NZ rates market reaction to the new government has been interesting, with lower short term interest rates alongside a pushing out of rate hike expectations, despite higher inflation expectations. On Friday, the 2-year swap rate fell by 4bps to 2.17% and pricing for the first full rate hike was pushed out a few months to February 2019. There was a steepening of the yield curve, with the 10-year swap rate up 1bp to 3.21%, taking the 2s10s spread from 99bps out to 104bps.

At the same time, rates on the long-dated inflation-indexed bonds fell, while nominal government bond yields were higher, implying higher break-even inflation rates. Using the 2025 bonds, inflation expectations rose by 6bps to 1.23%, taking the two-day gain to 12bps (with the Thursday's session getting a whiff of the Labour-led government before the official announcement).

So overall the market's interpretation of the new government is lower real rates consistent with a softer economy, but higher inflation and more tolerance for higher inflation, with an implied delay to any RBNZ rate hikes. All of this is highly debatable, of course. The market has reacted in a very high-level way, but the devil will be in the detail – who will be the next RBNZ Governor, when and how will the RBNZ Act be changed, and will any re-write actually change much the RBNZ's reaction function? All of those details matter.

On Friday, NZ equities opened on a soft note and were down 1.2% early on before staging a strong recovery and ending the day 0.1% higher. Export stocks and those with large offshore revenues outperformed, while property stocks, including the retirement sector, and domestic-focused stocks underperformed.

US 10-year rates are higher since leaving the office on Friday, supported by the aforementioned Budget resolution and speculation around the Fed chair/vice chair appointments. The 10-year rate failed to break the important 2.40% level, but is close, at around 2.37%.

Today we'll be on tenterhooks awaiting the possible release of coalition agreements and agreed policy positions. Winston Peters is set to be Deputy Prime

Minister and Foreign Affairs Minister when PM-elect Ardern officially allocates portfolios tomorrow. Tonight sees the release of global PMI data.

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Coming Up

		Period	Cons.	Prev.	NZT
GE	Markit manufacturing PMI	Oct P	60	60.6	20:30
GE	Markit services PMI	Oct P	55.6	55.6	20:30
EC	Markit manufacturing PMI	Oct P	57.7	58.1	21:00
EC	Markit services PMI	Oct P	55.8	55.8	21:00
US	Markit manufacturing PMI	Oct P	53	53.1	02:45
US	Markit services PMI	Oct P	55	55.3	02:45

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	0.6963	+0.0	0.6954	0.6990	CHF	0.9864	+0.2	S&P 500	2,572	-0.1	20.1	Oil (Brent)	57.41	-0.6
AUD	0.7802	-0.2	0.7796	0.7835	SEK	8.209	+0.6	Dow	23,336	+0.0	28.6	Oil (WTI)	51.87	+0.0
EUR	1.1742	-0.4	1.1733	1.1777	NOK	8.005	+0.3	Nasdaq	6,613	-0.2	25.8	Gold	1277.7	+0.0
GBP	1.3204	+0.1	1.3158	1.3227	HKD	7.802	-0.0	Stoxx 50	3,609	+0.1	17.3	HRC steel	595.0	+0.0
JPY	113.72	+0.2	113.61	113.97	CNY	6.640	+0.3	FTSE	7,524	+0.0	7.2	CRB	184.7	+0.3
CAD	1.2651	+0.2			SGD	1.363	+0.1	DAX	13,003	+0.1	21.4	Wheat Chic.	454.5	+2.2
NZD/AUD	0.8925	+0.2			IDR	13,543	+0.2	CAC 40	5,387	-0.3	18.8	Sugar	13.88	-0.7
NZD/EUR	0.5930	+0.4			THB	33.19	+0.0	Nikkei	21,697	+1.1	25.9	Cotton	69.56	+4.0
NZD/GBP	0.5273	-0.1			KRW	1,130	-0.1	Shanghai	3,381	+0.1	8.1	Coffee	124.4	-0.7
NZD/JPY	79.18	+0.2			TWD	30.26	+0.0	ASX 200	5,894	-0.2	9.0	WM powder	2975.0	-0.8
NZD/CAD	0.8809	+0.2			PHP	51.52	+0.1	NZX 50	8,130	+0.1	16.8	Australian Futures		
NZ TWI	73.76	-0.6										3 year bond	97.86	0.02
												10 year bond	97.19	0.03
Interest Rates							NZ Government Bonds				NZ Swap Yields			
Rates		Swap Yields		Benchmark 10 Yr Bonds										
	Cash	3Mth	2 Yr	10 Yr	Last	Net Day	Last		Last					
USD	1.25	1.36	1.81	2.35	USD	2.37	-0.01	NZGB 3 04/15/20	2.04	-0.03	1 year	2.02	-0.01	
AUD	1.50	1.70	2.00	2.92	AUD	2.80	0.02	NZGB 6 05/15/21	2.19	-0.04	2 year	2.17	-0.04	
NZD	1.75	1.94	2.17	3.21	NZD	2.96	0.02	NZGB 5 1/2 04/15/23	2.49	-0.02	5 year	2.68	-0.03	
EUR	0.00	0.06	-0.18	0.89	GER	0.43	-0.02	NZGB 2 3/4 04/15/25	2.78	0.01	7 year	2.94	-0.01	
GBP	0.25	0.39	0.81	1.36	GBP	1.31	-0.02	NZGB 4 1/2 04/15/27	2.96	0.02	10 year	3.21	0.01	
JPY	-0.04	-0.04	0.04	0.26	JPY	0.07	-0.01	NZGB 3 1/2 04/14/33	3.30	0.03	15 year	3.44	0.01	
CAD	1.00	1.17	1.83	2.34	CAD	2.03	-0.00	NZGB 2 3/4 04/15/37	3.50	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 06:49

Source: Bloomberg

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