

28 June 2017

## Events Round-Up

NZ: Trade balance (\$m), May: 103 vs. 419 exp.

US: Conf. Board cons. confid., Jun: 118.9 vs. 116.0 exp.

## Good Morning

A day that looked quiet on paper has turned out to be newsworthy. In currency markets, European currencies have surged, led by EUR on hawkish comments by ECB President Draghi, while the NZD has underperformed. Bond yields are higher across the board, driven by Draghi's comments and this has helped drag down equity markets.

After a number of low vol sessions, EUR is up a chunky 1.4% to 1.1340, its highest level since August last year, driving up other European currencies in the process like SEK, CHF and NOK. ECB President Draghi offered an upbeat assessment of the euro area economic recovery and signalled an eventual removal of policy accommodation. The key sentence in a speech delivered was "As the economy continues to recover, a constant policy stance will become more accommodative, and the central bank can accompany the recovery by adjusting the parameters of its policy instruments – not in order to tighten the policy stance, but to keep it broadly unchanged." The speech talked of "reflationary" forces in the economy and that factors weighing on the path of inflation at present are "mainly temporary factors that typically the central bank can look through". The market took that as signalling a further step towards policy normalisation, allowing a discussion of the tapering of asset purchases over coming months.

Draghi's more hawkish tone sent German bond yields higher, with the 10-year rate up 13bps to 0.37% and driving global bond rates higher, with UK rates up 8bps and the US 10-year rate up 6bps to 2.20%. The ECB's highly accommodative policy stance has been instrumental in depressing European bond yields and the euro so the market is taking notice of Draghi's signal that the end of that policy setting is nigh. The ECB will need to tread carefully from here in its communications to avoid a taper-tantrum scenario that the US saw back in 2013. Back then the US 10-year rate shot up by 140bps in a space of a few months after then-Fed Chair Bernanke first signalled a possible tapering of asset purchases.

Much stronger European currencies have spilled over into a stronger GBP, which is up 0.6% to breach the 1.28

mark. Following the release of its Financial Stability Review, the Bank of England raised banks' counter-cyclical capital buffer initially to 0.5% by June 2018 and then again to 1% in November 2018 to mitigate against the risks posed by 10% annual gains in consumer credit and to prepare for the uncertain outcome of Brexit talks. This will require banks to raise over £11b in fresh capital. By tightening macro-prudential policy members who voted for a rate increase at the last MPC meeting might now pull back on that view, making an imminent tightening less likely. But the UK OIS curve didn't show much change to near-term policy expectations after the announcement.

In US news, consumer confidence was stronger than expected, with an increasing number of respondents saying that "jobs are plentiful". The IMF reduced its forecast for US growth by 0.2pp to 2.1% for 2017 and by 0.4pp to 2.5% for next year after removing the previously assumed fiscal stimulus. That remains well short of Trump's optimistic budget proposal which assumes a 3% target. Fed's Yellen's speech in London didn't offer much new. She noted that the gradual rate-hike pace is well anticipated in markets and that asset valuations are "somewhat rich by traditional metrics". The S&P500 was already lower before her speech, driven by a weaker tech sector again, and the index made further losses during the speech to be currently down 0.5%.

For the day, only the NZD and yen are currently weaker against the USD. USD/JPY is up 0.2% to 112.10, no doubt driven by wider global rate-JGB spreads. The risk-off tone to markets has seen NZD down to 0.7280 after a short lived spike up to 0.7344 last night. After making a number of breaks above 0.73 over the last couple of weeks, the NZD has yet to close above that mark using New York closes. This suggests the 0.73 mark remains an important area of resistance.

We've already noted the rise in US 10-year rates. The curve steepened, with rates driven higher at the long end. The 2-year rate was up by a more modest 3bps to 1.365%. The overnight move suggests that ECB policy is as much an influence on US rates, or even more important, than Fed policy from here.

The NZ rates curved showed only small moves yesterday, but we'll see a jump higher on the open today. In the calendar ahead, known Fed dove Kashkari speaks this morning during the NZ time zone and there's not much else tonight either. I imagine that markets will be trying to find their feet and wondering how much higher to take

bond yields in the immediate future. If we do see further upward pressure then the overdue equity market correction feared by many investors could be in the makings. This wouldn't be NZD-supportive.

[jason.k.wong@bnz.co.nz](mailto:jason.k.wong@bnz.co.nz)

Coming Up

	Period	Cons.	Prev.	NZT
US Fed's Kashkari speaks in Michigan				09:30
US Fed's Williams speaks in Canberra				19:30
US Advance goods trade balance (\$b)	May	-66.0	-67.6	00:30
US Pending home sales (m/m%)	May	1.0	-1.3	02:00

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	0.7283	-0.1	0.7266	0.7344	CHF	0.9599	-1.3		S&P 500	2,428	-0.4	21.4	Oil (Brent)	46.65	+1.8
AUD	0.7594	+0.1	0.7581	0.7624	SEK	8.606	-1.3		Dow	21,373	-0.2	24.7	Oil (WTI)	44.25	+2.0
EUR	1.1345	+1.5	1.1182	1.1345	NOK	8.401	-0.9		Nasdaq	6,180	-1.1	34.5	Gold	1246.4	+0.0
GBP	1.2805	+0.6	1.2718	1.2806	HKD	7.801	+0.0		Stoxx 50	3,538	-0.7	31.2	HRC steel	589.0	+0.0
JPY	112.13	+0.2	111.46	112.47	CNY	6.813	-0.4		FTSE	7,434	-0.2	24.3	CRB	170.0	+0.9
CAD	1.3159	-0.6			SGD	1.387	-0.1		DAX	12,671	-0.8	36.7	Wheat Chic.	469.0	+0.8
NZD/AUD	0.9590	-0.2			IDR	13,300	-0.1		CAC 40	5,259	-0.6	32.0	Sugar	12.65	+0.3
NZD/EUR	0.6420	-1.5			THB	33.97	+0.0		Nikkei	20,225	+0.4	32.0	Cotton	74.44	+1.0
NZD/GBP	0.5688	-0.7			KRW	1,137	-0.0		Shanghai	3,191	+0.2	9.6	Coffee	125.3	+0.6
NZD/JPY	81.66	+0.2			TWD	30.33	+0.0		ASX 200	5,714	-0.1	12.0	WM powder	3000.0	-1.6
NZ TWI	78.51	-0.4			PHP	50.26	+0.2		NZX 50	7,626	+0.4	13.5	<b>Australian Futures</b>		
										3 year bond			98.14	-0.05	
										10 year bond			97.52	-0.09	
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	1.29	1.57	2.17	USD	2.20	0.06	NZGB 3 04/15/20	2.11	0.00	1 year	2.03	0.00		
AUD	1.50	1.72	1.86	2.72	AUD	2.35	-0.02	NZGB 6 05/15/21	2.19	-0.00	2 year	2.22	0.00		
NZD	1.75	1.96	2.23	3.13	NZD	2.72	-0.01	NZGB 5 1/2 04/15/23	2.45	-0.00	5 year	2.69	-0.00		
EUR	0.00	0.06	-0.15	0.82	GER	0.37	0.13	NZGB 2 3/4 04/15/25	2.63	-0.00	7 year	2.91	-0.01		
GBP	0.25	0.30	0.61	1.20	GBP	1.09	0.08	NZGB 4 1/2 04/15/27	2.72	-0.01	10 year	3.13	-0.01		
JPY	-0.05	0.00	0.04	0.23	JPY	0.05	-0.01	NZGB 3 1/2 04/14/33	3.05	-0.00	15 year	3.37	-0.01		
CAD	0.50	1.17	1.28	1.90	CAD	1.57	0.11	NZGB 2 3/4 04/15/37	3.26	-0.01					

\* 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 06:56

Source: Bloomberg

## Contact Details

<b>New Zealand</b>	Jason Wong	Senior Market Strategist	+ (64 4) 924 7652
<b>Australia</b>	Ray Attrill	Head of FX Strategy	+ (61 2) 9237 1848
	Rodrigo Catril	Currency Strategist	+ (61 2) 9237 7109
<b>London</b>	Nick Parsons	Head of Research, UK & Europe	+ (44 0) 20 7710 2993
	Gavin Friend	Senior Market Strategist	+ (44 0) 20 7710 0898

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