

30 October 2018



Events Round-Up

US: Personal income (m/m%), Sep: 0.2 vs. 0.4 exp.

US: Personal spending (m/m%), Sep: 0.4 vs. 0.4 exp.

US: Core PCE deflator (y/y%), Sep: 2 vs. 2 exp.

Good Morning

US equities have staged something of a recovery overnight, although the tech sector has again lagged. The more positive tone to risk assets has helped Treasury yields push a little higher and the JPY underperform. The NZD is little changed against the USD from Friday night's close, although it has made gains on all the crosses.

After what has been a tumultuous month for equity markets, US equity indices have bounced modestly overnight, helping to support broader risk appetite. Equities were initially boosted by reports that China was planning to halve its tax on new car purchases to 5% (with automakers predictably outperforming), which would be the latest in a series of targeted stimulus measures by the Chinese authorities. The S&P500 opened 1.8% higher, following the lead of European bourses, although it has since pared those gains to around 0.2%. The NASDAQ has again underperformed, and now down around 0.6% on the day. The S&P500 is down around 8.5% this month with the NASDAQ 11% lower. Historically, bear markets in US equities (defined as a 20% fall from the peak) have tended to occur in the lead-up to US recessions, so provided the US economy can maintain its poise, equities should be able to find some stability ahead. Earnings reports will be in focus this week, including from Facebook, Apple and Exxon Mobil.

Treasury yields and US equities have continued to trade in lock-step with one another. The 10 year Treasury yield rose 2bps on the day to 3.10%, having earlier fallen as low as 3.06%. The only economic data of note was the release of the core PCE deflator, which rose 2% from a year ago (as foreshadowed by Friday's GDP release), matching economists' expectations. There is plenty of potentially market-moving economic data later in the week, with the employment cost index released Wednesday night, the ISM manufacturing survey on Thursday night, and non-farm payrolls on Friday.

On a more technical note, last week saw the Fed funds effective rate, which the Fed targets, trade at 2.2%, the same level as the interest rate the Fed pays on reserve

balances held by banks. The convergence of the two rates, for the first time since 2009, largely reflects the shrinking in the Fed's balance sheet as it runs down its portfolio of QE holdings. This, in turn, has led to speculation that the Fed might increase the interest rate on excess reserves by less than 25bps in December (it raised it by only 20bps in June) to ensure the market rate remains within its target range. The market prices 17bps of tightening for the Fed's December meeting, which equates to an 85% chance of a 20bp hike, signalling the market still thinks a December rate rise is very likely, despite the recent turbulence in equities.

The USD is broadly stronger on the day, with the DXY dollar index up 0.3% to near its recent highs. The broader Bloomberg DXY, which includes emerging market currencies, is up 0.5% to its highest level since mid-2017. The more risk-on tone to markets has seen the Japanese yen and Swiss franc underperform, with both currencies down around 0.5%.

German Chancellor Angela Merkel's announcement that she would stand down as party leader of the CDU caused an initial 50pip fall in the EUR to 1.1360. The EUR has subsequently bounced to 1.1390, a 0.15% fall on the day, after Merkel later said she would stay on as Chancellor until the next election (this is currently scheduled for 2021 but could sooner if her coalition collapses – Merkel said she will not seek re-election). Elsewhere in Europe, the 10 year Italian bond yield fell 11bps as the market reacted to S&P's decision on Friday night not to downgrade Italy's credit rating.

The NZD initially rose to as high as 0.6556 during the London morning amidst the more positive risk sentiment in markets, but it has since eased back to 0.6530 – slightly higher than Friday night's close. The NZD is the only G10 currency that has appreciated (marginally) against the USD on the day, possibly due to some squaring of speculative short positions. The ANZ business survey on Wednesday is the data highlight locally this week.

Local rates markets took their lead from offshore markets yesterday, with swap rates 1.5 to 2.25bps lower across the curve. The 2 year swap rate fell to 1.99% while the 10 year swap rate fell to 2.78%, its lowest level since late 2016. The market doesn't price the first hike for the RBNZ until early 2021, with a very gradual pace of hikes built-in thereafter. We expect upward pressure on NZ rates to come through over the next twelve months.

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Coming Up

	Period	Cons.	Prev.	NZT
GE Unemployment Rate	Oct	5.1	5.1	21:55
EC Economic Confidence	Oct	110	110.9	23:00
EC GDP (q/q%)	3Q A	0.3	0.4	23:00
GE CPI (y/y%)	Oct P	2.4	2.2	02:00
US Conf. Board Consumer Confidence	Oct	135.95	138.4	03:00

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	0.6528	+0.4	0.6522	0.6556	CHF	1.0016	+0.5		S&P 500	2,682	+0.8	3.9	Oil (Brent)	77.60	-0.0
AUD	0.7066	-0.3	0.7062	0.7109	SEK	9.132	-0.0		Dow	24,720	+0.1	5.5	Oil (WTI)	67.30	-0.4
EUR	1.1390	-0.1	1.1361	1.1416	NOK	8.377	+0.3		Nasdaq	7,144	-0.4	6.6	Gold	1228.3	-0.6
GBP	1.2803	-0.2	1.2792	1.2853	HKD	7.843	+0.0		Stoxx 50	3,155	+0.6	-13.6	HRC steel	831.0	-0.4
JPY	112.43	+0.5	111.85	112.56	CNY	6.962	+0.3		FTSE	7,026	+1.3	-6.4	CRB	193.7	-0.9
CAD	1.3120	+0.1			SGD	1.382	+0.2		DAX	11,335	+1.2	-14.2	Wheat Chic.	525.8	+0.2
NZD/AUD	0.9239	+0.4			IDR	15,223	+0.0		CAC 40	4,989	+1.5	-9.2	Sugar	13.50	-2.5
NZD/EUR	0.5731	+0.2			THB	33.23	+0.5		Nikkei	21,150	-0.2	-3.9	Cotton	77.72	-1.0
NZD/GBP	0.5099	+0.3			KRW	1,141	-0.1		Shanghai	2,542	-2.2	-25.0	Coffee	114.3	-4.5
NZD/JPY	73.39	+0.8			TWD	30.99	-0.0		ASX 200	5,728	+1.1	-3.2	WM powder	2660.0	+0.4
NZD/CAD	0.8565	+0.6			PHP	53.62	+0.1		NZX 50	8,616	+0.6	5.8	Australian Futures		
NZ TWI	72.06	+0.3											3 year bond	97.96	-0.01
													10 year bond	97.40	-0.02
Interest Rates						NZ Government Bonds				NZ Swap Yields					
Rates		Swap Yields		Benchmark 10 Yr Bonds		Last		Last		Last					
	Cash	3Mth	2 Yr	10 Yr											
USD	2.25	2.52	3.04	3.17	USD	3.10	0.03	NZGB 6 05/15/21	1.74	-0.01	1 year	1.94	0.00		
AUD	1.50	1.92	2.01	2.78	AUD	2.57	-0.03	NZGB 5 1/2 04/15/23	1.91	-0.02	2 year	1.99	-0.01		
NZD	1.75	1.89	1.99	2.78	NZD	2.35	-0.02	NZGB 2 3/4 04/15/25	2.16	-0.02	5 year	2.30	-0.02		
EUR	0.00	0.06	-0.12	0.95	GER	0.38	0.03	NZGB 4 1/2 04/15/27	2.35	-0.02	7 year	2.53	-0.02		
GBP	0.75	0.81	1.09	1.55	GBP	1.40	0.02	NZGB 3 04/20/29	2.51	-0.02	10 year	2.78	-0.02		
JPY	-0.07	-0.10	0.05	0.31	JPY	0.11	-0.00	NZGB 3 1/2 04/14/33	2.69	-0.02	15 year	3.04	-0.02		
CAD	1.75	1.17	2.64	2.84	CAD	2.41	0.02	NZGB 2 3/4 04/15/37	2.83	-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 07:09

Source: Bloomberg

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