

5 November 2018



Events Round-Up

NZ: ANZ consumer confidence, Oct: 115.4 vs. 117.6 prev.

AU: Retail sales (m/m%) Sep: 0.2 vs. 0.3 exp.

UK: Construction PMI, Oct: 53.2 vs. 52 exp.

US: Trade balance (\$b), Sep: -54 vs. -53.6 exp.

US: Change in non-farm payrolls, Oct: 250k vs. 200k exp.

US: Unemployment rate, Oct: 3.7 vs. 3.7 exp.

US: Average hourly earnings (m/m%), Oct: 0.2 vs. 0.2 exp.

US: Average hourly earnings (y/y%), Oct: 3.1 vs. 3.1 exp.

CA: Unemployment rate, Oct: 5.8 vs. 5.9 exp.

Good Morning

A stronger than expected US non-farm payrolls report led to a sharp rise in US Treasury yields and an appreciation in the USD against G10 currencies. Emerging market currencies and equities performed strongly on reports that President Trump had instructed his staff to draft an outline for a possible trade deal with China, although White House advisor Kudlow later tried to cool expectations. Higher US bond yields weighed on US equities, which had initially risen on optimism for a US-China trade deal.

US Treasury yields jumped sharply on Friday night after the non-farm payroll report showed a larger than expected 250k monthly jobs gain, cementing expectations for a Fed rate hike in December. Other aspects of the payrolls report were also strong, although broadly in line with expectations. Average hourly earnings increased to 3.1%, the fastest annual wage growth since 2009, while the unemployment rate was unchanged at 3.7%, the lowest level since 1969. 3 month average payrolls growth is running at 218k, well in excess of the "breakeven" level required to keep the unemployment rate stable; the reason the unemployment rate didn't fall in October was due to a surprise jump in the participation rate. The payrolls report, alongside other US macro indicators, point to a US economy currently growing well above trend.

The 10 year US Treasury yield rose 8bps to 3.21%, closing in on the multi-year highs reached last month of 3.26%. The market prices 18bps into the Fed's December meeting, which equates to a 90% chance of a tightening (assuming the Fed raises the interest rate on excess reserves by only 20bps, as we expect). The market prices a further two full hikes for calendar year 2019, although that remains below the FOMC median projection for three hikes next year.

There has been conflicting news on the possibility of a US-China trade deal. Late Friday afternoon, Bloomberg reported that Trump had directed officials to draft terms for a potential deal, and that he was interested in reaching an agreement at his G20 meeting with Chinese President Xi. The report led to an immediate 0.5% jump in the NZD and AUD and extended gains in Chinese equities and emerging market currencies. The Chinese CSI300 equity index ended the day 3.6% higher while the Hang Seng was even stronger, up 4.2%. The CNY was 0.5% stronger on the day at 6.89, creating a slightly greater buffer from the psychologically important 7.0 level.

Later in the session, White House economic advisor Larry Kudlow tried to cool expectations for a Trump-Xi agreement, telling CNBC "*we're not on the cusp of a deal*". But optimism was renewed when Trump later claimed "*we'll make a deal with China...a lot of progress has been made.*" It remains unclear whether Trump is planning to soften his stance on some of the key US demands (including IP protection) to facilitate a deal. Some of the more cynical analysts suggest Trump's comments are an attempt to temporarily boost the equity market before the mid-term elections tomorrow.

While the initial Bloomberg story on Trump's China plans led to a fall in the USD, the payrolls report sparked an immediate turn-around. The DXY index ended the day 0.2% higher at 96.5, having initially been 0.3% lower on the day. The NZD mirrored these movements. After earlier rising as high as 0.6690 on optimism for a possible US-China deal, the post-payrolls strengthening in the USD saw the NZD drift lower to 0.6650, unchanged on the day.

Against a firmer USD backdrop after payrolls, the EUR was given an additional push lower after MNI reported that the ECB might discuss a possible new round of TLTRO loans to European banks as soon as December. The original €722b of long-term loans start rolling off in 2020, and MNI claimed a new round of TLTROs (probably with less generous terms) could be used as a 'first line of defence' if the European economic slow-down gathered pace. Reuters later reported that December was too soon for the ECB to come to a decision. The EUR ended the day down 0.2% at 1.1380.

US equity markets were initially buoyed by optimism of a US-China trade agreement (S&P futures were +1.2% at one stage), but they turned down shortly after the US payrolls report, probably in response to the sharp rise in bond yields. Trump's "*we'll make a deal with China*" comments late in the session saw US equities pare their losses, but the S&P500 ended down 0.6% and the

NASDAQ down 1.2%. Apple's share price was 6.6% lower after releasing disappointing revenue forecasts and informing the market that it would no longer be publishing iPhone sales figures (some analysts see this as an attempt to move attention away from a slow-down in iPhone sales). Despite Friday's falls, the major US equity indices were up around 2.5% on the week.

Finally, NZ swap rates rose by between 1 to 2.5bps on Friday, led by the front-end of the curve. The 2 year swap rate closed at 2.05%, the top of the narrow trading range that has been in place since the August MPS. There are some tentative signs of funding pressures emerging in the NZ market, with the 90 day bank bill rate rising 2bps on Friday (and 5bps over the course of the week), and some modest upward pressure on repo rates. Local swap rates will follow offshore rates higher today.

It's a big week ahead. The US mid-term elections are tomorrow (Nate Silver's FiveThirtyEight site has an 85% chance the Democrats take the House and the same probability the Republicans retain the Senate). The ISM non-manufacturing survey is released tonight (recall this triggered the sharp US bond sell-off last month) and the FOMC meeting is Friday morning (no change expected). The RBA releases its Statement of Monetary Policy on Friday also.

Locally, the RBNZ MPS is on Thursday, where we expect the Bank to retain a similar message to the last Statement (the OCR likely on hold until 2020 and the next move could be up or down), and the NZ labour market report is released on Wednesday.

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Coming Up

		Period	Cons.	Prev.	NZT
CH	Caixin China PMI Services	Oct	52.8	53.1	14:45
UK	Markit/CIPS UK Services PMI	Oct	53.3	53.9	22:30
CA	Bank of Canada's Poloz Gives Speech in London				02:25
US	Markit US Services PMI	Oct F	54.6	54.7	03:45
US	ISM Non-Manufacturing Index	Oct	59.1	61.6	04:00

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	0.6647	-0.0	0.6634	0.6690	CHF	1.0035	+0.1		S&P 500	2,723	-0.6	5.2	Oil (Brent)	72.83	-0.1
AUD	0.7193	-0.2	0.7182	0.7259	SEK	9.061	+0.2		Dow	25,271	-0.4	7.4	Oil (WTI)	63.14	-0.9
EUR	1.1388	-0.2	1.1372	1.1456	NOK	8.368	+0.2		Nasdaq	7,357	-1.0	8.8	Gold	1233.3	-0.4
GBP	1.2970	-0.3	1.2952	1.3041	HKD	7.817	-0.2		Stoxx 50	3,214	+0.3	-12.9	HRC steel	823.0	+0.2
JPY	113.20	+0.4	112.67	113.29	CNY	6.891	-0.5		FTSE	7,094	-0.3	-6.2	CRB	192.3	+0.3
CAD	1.3110	+0.2			SGD	1.376	-0.1		DAX	11,519	+0.4	-14.5	Wheat Chic.	524.0	+0.2
NZD/AUD	0.9241	+0.0			IDR	14,955	-1.1		CAC 40	5,102	+1.1	-7.5	Sugar	13.44	+1.9
NZD/EUR	0.5837	+0.1			THB	32.84	-0.1		Nikkei	22,244	+2.6	-1.3	Cotton	78.79	-0.3
NZD/GBP	0.5125	+0.2			KRW	1,122	-1.4		Shanghai	2,676	+2.7	-20.6	Coffee	120.1	+1.9
NZD/JPY	75.24	+0.5			TWD	30.66	-0.8		ASX 200	5,849	+0.1	-1.9	WM powder	2715.0	+0.4
NZD/CAD	0.8714	+0.1			PHP	53.07	-0.3		NZX 50	8,836	-0.1	9.6	Australian Futures		
NZ TWI	72.74	-0.0											3 year bond	97.86	-0.06
													10 year bond	97.27	-0.09
Interest Rates					Benchmark 10 Yr Bonds				NZ Government Bonds			NZ Swap Yields			
	Rates		Swap Yields			Last	Net Day		Last		Last		Last		
	Cash	3Mth	2 Yr	10 Yr	USD	3.21	0.08	NZGB 6 05/15/21	1.82	0.02	1 year	1.99	0.03		
USD	2.25	2.58	3.11	3.28	AUD	2.69	0.05	NZGB 5 1/2 04/15/23	2.00	0.03	2 year	2.05	0.02		
AUD	1.50	1.93	2.08	2.90	NZD	2.43	0.02	NZGB 2 3/4 04/15/25	2.23	0.02	5 year	2.38	0.02		
NZD	1.75	1.94	2.06	2.88	GER	0.43	0.03	NZGB 4 1/2 04/15/27	2.43	0.02	7 year	2.61	0.01		
EUR	0.00	0.06	-0.11	0.98	GBP	1.49	0.04	NZGB 3 04/20/29	2.58	0.02	10 year	2.87	0.01		
GBP	0.75	0.83	1.19	1.65	JPY	0.13	0.01	NZGB 3 1/2 04/14/33	2.76	0.02	15 year	3.13	0.01		
JPY	-0.07	-0.09	0.04	0.32	CAD	2.53	0.05	NZGB 2 3/4 04/15/37	2.90	0.02					
CAD	1.75	1.17	2.70	2.94											

* 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

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