

8 November 2018



Events Round-Up

NZ: Unemployment rate (%), Q3: 3.9 vs. 4.4 exp.
NZ: Employment (q/q%), Q3: 1.1 vs. 0.5 exp.
NZ: LCI pvt wages ex overtime (q/q%), Q3: 0.5 vs. 0.5 exp.
NZ: QES avg hrly earnings (q/q%), Q3: 1.4 vs. 0.8 exp.
NZ: RBNZ 2yr inflation expect., Q4: 2.03 v. 2.04 prev.
CH: Foreign Reserves (\$b), Oct: 3053 vs. 3059 exp.
GE: Industrial production (m/m%), Sep: 0.2 vs. 0.0 exp.
EC: Retail sales (m/m%), Sep: 0.0 vs. 0.1 exp.

Good Morning

The USD is modestly softer across the board after the in-line result of the US mid-term elections, US Treasury yields are down slightly, driven by the long end, and US equities are stronger. The NZD has been the star performer following the surprising strength in labour market data yesterday.

The NZD is 1.8% stronger from this time yesterday, closing in on 0.68 after a much stronger than expected labour market report and generalised USD weakness post the US mid-term elections. Gains have been made on all the crosses, with the TWI some 1.4% higher. In Q3, much stronger than expected employment drove a plunge in the unemployment rate to 3.9%, its lowest level in a decade. The key LCI wage data were in line, consistent with inflation running near the middle of the target range.

The data add to the evidence that the economy is doing just fine, with no sign that weaker business confidence is impacting the real economy. The NZD moved up 70pips to 0.6750 after the result and NZ rates moved higher, driven by expectations of tighter monetary policy. The OIS market has now effectively priced out the chance of any further cut in the OCR, and sees a rising chance of tighter policy from the second half of next year, which now aligns with our own expectation. The 2-year swap rate closed up 9bps to 2.15%, a 4-month high, while the belly of the curve bore the brunt of changing policy expectations, with the 5-year rate up 13bps to 2.55% and the 10-year rate up 11bps to 3.03%.

The much stronger labour market data comes at an awkward time for the RBNZ, which releases its latest forecasts and policy statement today. The forecasts would have already been finalised and will already be out of date,

but there has been time for the Bank to re-write its press release, which forms the opening chapter. With inflation now running close to the middle of the target band and the unemployment rate towards the lower edge of its natural (non-inflationary) level, it would certainly come across as less credible if the Bank continued to run the line that it could cut the OCR. Still, without the smoking gun of higher wage inflation and with core CPI inflation steady at around 1¾% over the last quarter the Bank is unlikely to be in a rush to tighten policy and might well continue to signal an "on-hold" stance for some time yet.

The other market-moving event has been the US mid-term elections which caused some intra-day volatility yesterday as the results began to drift in, but the end result was in line with expectations. Vote counting continues in a number of close races, but the Democrats have won enough seats so far to take the House, while the Republicans have extended their Senate majority. US equities have staged a relief rally, with the S&P500 currently up 1.5%. Stocks have historically performed well after mid-terms, with the average gain in the S&P500 through to the end of the year up more than 10% on average in data since 1950.

The US 10-year rate is down 4bps to 3.19% while the 2-year rate is unchanged. The divided government reduces the chance of further tax cuts and will act as a restraint on any changes to domestic policy, although increased infrastructure spending is one possible area of agreement that could potentially add to the current stimulatory fiscal environment. This morning Trump said that he saw ample opportunities to cut deals with the Democrats, although this looks dependent on the Democrats not investigating Trump's conduct. Republican control of the Senate still gives plenty of leeway for Trump on political appointments and foreign policy, including trade. For the bond market, some key dates ahead are 7 December, when the "continuing resolution" funding the government runs out and raises the spectre of another government shutdown, while ahead of 1 March focus will turn to the debt ceiling.

With the in-line result, the impact on the USD has been modest, with the various dollar indices we monitor down 0.3-0.4%. Much of the move came during NZ trading hours, with only the NZD and AUD adding to gains in overnight trading. We have previously said that the 0.6730 level would need to be convincingly broken to declare the downward trend in the NZD over. The turnaround in NZ monetary policy expectations supports

that technical view and, combined with a more recent positive vibe on US-China trade talk, we have a more constructive view of the NZD heading into year-end.

In other news, China's foreign currency reserves fell \$34b in October, close to market expectations. The fall largely reflected valuation changes of the USD and Treasury holdings, with signs of only modest capital outflows. In the UK, Cabinet ministers were invited to read a copy of the draft Brexit Withdrawal Agreement. Sources indicated that an emergency Cabinet meeting to sign it off is set to happen later this week or Monday, although note that it doesn't yet include the final clause on the Irish backstop. GBP made modest gains against a softer USD but made little progress against other currencies.

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Coming Up

		Period	Cons.	Prev.	NZT
NZ	RBNZ official cash rate (%)	Nov	1.75	1.75	09:00
CH	Trade Balance (\$b)	Oct	35.1	31.7	
CH	Imports (\$b, y/y%)	Oct	14.7	14.3	
CH	Exports (\$b, y/y%)	Oct	11.7	14.5	

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	0.6792	+0.8	0.6746	0.6793	CHF	0.9995	-0.3		S&P 500	2,797	+1.5	8.0	Oil (Brent)	72.17	+0.1
AUD	0.7285	+0.5	0.7239	0.7300	SEK	8.999	-0.5		Dow	26,012	+1.5	10.4	Oil (WTI)	61.88	-0.5
EUR	1.1466	+0.3	1.1431	1.1500	NOK	8.324	-0.5		Nasdaq	7,536	+2.2	11.4	Gold	1229.7	+0.3
GBP	1.3154	+0.4	1.3108	1.3175	HKD	7.829	-0.0		Stoxx 50	3,246	+1.2	-11.3	HRC steel	817.0	-0.7
JPY	113.33	-0.1	112.95	113.37	CNY	6.920	+0.0		FTSE	7,117	+1.1	-5.3	CRB	191.4	+0.1
CAD	1.3103	-0.2			SGD	1.370	-0.3		DAX	11,579	+0.8	-13.5	Wheat Chic.	526.0	-0.2
NZD/AUD	0.9323	+0.2			IDR	14,590	-1.4		CAC 40	5,138	+0.9	-6.3	Sugar	13.02	+0.5
NZD/EUR	0.5924	+0.4			THB	32.81	-0.4		Nikkei	22,086	-0.3	-3.6	Cotton	79.27	+2.4
NZD/GBP	0.5163	+0.4			KRW	1,123	-0.0		Shanghai	2,641	-0.7	-22.7	Coffee	115.2	+1.7
NZD/JPY	76.97	+0.7			TWD	30.73	-0.1		ASX 200	5,897	+0.4	-2.0	WM powder	2675.0	-1.7
NZD/CAD	0.8900	+0.6			PHP	52.86	-0.2		NZX 50	8,855	+0.4	10.1	Australian Futures		
NZ TWI	74.08	+0.5											3 year bond	97.83	-0.02
													10 year bond	97.26	0.01
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	2.25	2.59	3.12	3.25	USD	3.19	-0.04	NZGB 6 05/15/21	1.92	0.07	1 year	2.02	0.02		
AUD	1.50	1.94	2.09	2.90	AUD	2.73	0.00	NZGB 5 1/2 04/15/23	2.13	0.09	2 year	2.15	0.09		
NZD	1.75	1.97	2.14	3.02	NZD	2.57	0.09	NZGB 2 3/4 04/15/25	2.37	0.10	5 year	2.55	0.13		
EUR	0.00	0.06	-0.12	0.99	GER	0.45	0.01	NZGB 4 1/2 04/15/27	2.57	0.09	7 year	2.78	0.13		
GBP	0.75	0.85	1.21	1.69	GBP	1.53	-0.01	NZGB 3 04/20/29	2.73	0.09	10 year	3.03	0.11		
JPY	-0.07	-0.09	0.04	0.32	JPY	0.12	-0.01	NZGB 3 1/2 04/14/33	2.92	0.10	15 year	3.29	0.11		
CAD	1.75	1.17	2.69	2.92	CAD	2.52	-0.02	NZGB 2 3/4 04/15/37	3.06	0.10					

* 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 06:54

Source: Bloomberg

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