

8 October 2018



## Events Round-Up

AU: Retail sales (m/m%), Aug: 0.3 vs. 0.2 exp.  
GE: Factory orders (m/m%), Aug: 2.0 vs. 0.8 exp.  
US: Trade balance (\$b), Aug: -53.2 vs. -53.6 exp.  
US: Change in non-farm payrolls (k), Sep: 134 vs. 185 exp.  
US: Unemployment rate (%), Sep: 3.7 vs. 3.8 exp.  
US: Average hourly earnings (m/m%), Sep: 0.3 vs. 0.3 exp.  
US: Average hourly earnings (y/y%), Sep: 2.8 vs. 2.8 exp.  
CA: Unemployment rate, Sep: 5.9 vs. 5.9% exp

## Good Morning

The NZD and AUD continued to probe fresh multi-year lows, following the US employment report which showed a tightening labour market. The report also saw the US 10-year Treasury rate rise to a fresh 7-year high.

Friday's trading session was typically quiet ahead of the US employment report and we saw plenty of price action after that. The report was a bit of a dog's breakfast, but consistent with the theme that the US labour market continues to tighten and supporting the Fed's gradual policy tightening stance. Non-farm payrolls came in much weaker than expected for September, but this "miss" was negated by upward revisions to prior months. More importantly, the unemployment rate fell to 3.7%, the lowest level since 1969. Wage data were in line with expectations, with annual wage inflation slipping a touch due to favourable base effects (which won't apply next month).

NY Fed President Williams was interviewed by Bloomberg after the employment report and he was still comfortable with the Fed tightening at a gradual pace, despite the fresh low in the unemployment rate, "it doesn't scare me at all...we are not seeing any inflation pressures now so I think this is a bit of a Goldilocks economy". He echoed Chair Powell's comments earlier in the week, that there was still "a ways to go" before getting to a neutral policy rate, with neutral seen to be about 3% compared to the current Fed Funds rate a little above 2%.

US rates rose after the employment report, with the 10-year rate rising to a fresh 7-year high just shy of 3.25%, before ending the day up 5bps at 3.23%. Like we saw earlier in the week after the strong non-manufacturing ISM report, the yield curve steepened, with the 2-year rate

rising by less than 2bps to 2.885%.

Looking at the weekly changes in US Treasury yields is interesting, as they show the 2-year rate up 7bps, the 10-year rate up 17bps, while breaking the nominal 10-year rate into its inflation expectations and real yield components shows the break-even inflation component +3bps and the real yield component +14bps. This tells us that the ramp up in yields for the week was driven by higher growth expectations, rather than concern about inflation (even in the face of higher oil prices for the week, with WTI crude up 1.5%).

Despite the higher growth outlook, the US equity market didn't take the rise in yields very well – likely owing to the impact of higher rates on valuations. The S&P-500 fell by 0.6% on the day and 1.0% for the week. More interesting, the Nasdaq composite was down 3.2% for the week while the Russell 2000 index, a barometer for smaller cap stocks, was down 3.8% for the week.

In other economic data news, Canada's employment report showed strong gains in payrolls, taking market conviction in a rate hike later this month to 100%. The US monthly trade deficit was in line with the advanced estimate. Notably, the US trade deficit with China widened to a record \$38.6b, while China didn't import any US crude oil in August – zero, reflecting the escalation in trade tensions.

In currency markets, the USD turned lower after the US employment report, perhaps reflecting some profit taking after a good run, with Bloomberg's DXY index down 0.2%. But even a weaker USD didn't prevent further falls in the NZD and AUD, as the market took the risk-off tone (lower equities, higher VIX) as an excuse to sell them down further. The NZD reached a fresh multi-year low of 0.6432, before closing the week closer to 0.6440. After its poor run (down 2.7% for the week), the next level of technical support is at 0.6350. That's about the most positive thing you can say about the NZD at present with fundamental support non-existent (risk appetite overdue to correct lower, lower NZ rates versus US, downward pressure on all Asia-Pacific currencies, falling terms of trade, low business confidence, falling consumer confidence). The AUD closed the week at 0.7050, while NZD/AUD nudged down to 0.9130.

Movements in other majors were fairly insignificant for the day apart from GBP, which outperformed as the market took a more optimistic view on Brexit negotiations. There were plenty of Brexit headlines to digest. Reuters

reported that EU Brexit negotiators see a divorce deal as "very close". Bloomberg reported that the EU is set to offer the UK a free-trade deal deeper than any agreement that's gone before, but will reject PM May's demand for "frictionless trade," according to EU diplomats. This could make the deal harder to get through the UK Parliament. The FT reported that the EU is drafting tough contingency plans for a no-deal Brexit, and these will be revealed later this week. Notably, the EU is not planning special arrangements for customs or road transport that would cause long queues and operational difficulties at ports and airports. GBP ended the week at 1.3120, making it the strongest of the majors for the day and the week. NZD/GBP fell to 0.4910, its lowest close since the day of the Brexit vote.

The economic calendar is light over the next 24 hours and is fairly light for the week as well. The key release this week is US CPI data out Thursday night NZ time. It might

still be an interesting start to the week, after the weekend announcement of the PBoC cutting its reserve requirement ratio for banks by 100bps, the fourth easing this year. The CNY reference rate was unchanged last week during the Golden Week holiday. The chunky falls in NZD and AUD last week seem to have already pre-empted, to some extent, the downward pressure on the CNY that might prevail.

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### Coming Up

		Period	Cons.	Prev.	NZT
CH	Caixin PMI services	Sep	51.4	51.5	14:45
GE	Industrial production (m/m%)	Aug	0.3	-1.1	19:00

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	0.6438	-0.6	0.6432	0.6483	CHF	0.9920	+0.0		S&P 500	2,886	-0.6	13.1	Oil (Brent)	84.05	-0.6
AUD	0.7050	-0.3	0.7043	0.7087	SEK	9.067	+0.1		Dow	26,447	-0.7	16.1	Oil (WTI)	74.29	-0.1
EUR	1.1524	+0.1	1.1484	1.1549	NOK	8.259	+0.1		Nasdaq	7,788	-1.2	18.3	Gold	1202.5	+0.4
GBP	1.3120	+0.8	1.3003	1.3123	HKD	7.835	+0.0		Stoxx 50	3,346	-0.9	-7.4	HRC steel	828.0	-0.2
JPY	113.72	-0.2	113.56	114.08	CNY	6.869	-0.3		FTSE	7,319	-1.3	-2.5	CRB	199.0	+0.1
CAD	1.2939	+0.1			SGD	1.383	+0.1		DAX	12,112	-1.1	-6.6	Wheat Chic.	540.3	+0.7
NZD/AUD	0.9132	-0.2			IDR	15,183	+0.0		CAC 40	5,359	-1.4	-0.4	Sugar	12.63	+2.4
NZD/EUR	0.5587	-0.7			THB	32.83	+0.2		Nikkei	23,784	-0.8	14.9	Cotton	76.49	+0.1
NZD/GBP	0.4907	-1.3			KRW	1,131	+0.1		Shanghai	2,821	+1.1	-15.8	Coffee	109.0	+1.9
NZD/JPY	73.21	-0.7			TWD	30.85	+0.2		ASX 200	6,185	+0.1	8.3	WM powder	2690.0	-0.4
NZD/CAD	0.8330	-0.4			PHP	54.26	-0.1		NZX 50	9,215	-0.5	15.5	<b>Australian Futures</b>		
NZ TWI	70.74	-0.5											3 year bond	97.895	-0.01
													10 year bond	97.23	-0.03
Interest Rates							NZ Government Bonds				NZ Swap Yields				
Rates		Swap Yields			Benchmark 10 Yr Bonds		Last				Last				
	Cash	3Mth	2 Yr	10 Yr		Last	Net Day								
USD	2.25	2.41	3.06	3.27	USD	3.23	0.05	NZGB 6 05/15/21	1.77	-0.00	1 year	1.93	-0.00		
AUD	1.50	1.92	2.02	2.91	AUD	2.71	0.01	NZGB 5 1/2 04/15/23	1.97	-0.01	2 year	2.02	0.00		
NZD	1.75	1.89	2.02	2.90	NZD	2.43	-0.01	NZGB 2 3/4 04/15/25	2.23	-0.00	5 year	2.38	0.00		
EUR	0.00	0.06	-0.09	1.08	GER	0.57	0.04	NZGB 4 1/2 04/15/27	2.43	-0.01	7 year	2.63	0.01		
GBP	0.75	0.80	1.22	1.79	GBP	1.72	0.05	NZGB 3 04/20/29	2.60	-0.01	10 year	2.90	0.01		
JPY	-0.06	-0.07	0.06	0.37	JPY	0.16	-0.00	NZGB 3 1/2 04/14/33	2.78	-0.01	15 year	3.16	0.01		
CAD	1.50	1.17	2.66	2.97	CAD	2.60	0.04	NZGB 2 3/4 04/15/37	2.91	-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: NY close Sat morn

Source: Bloomberg

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