Amplifying Global FX Capital

9 August 2017

View Update - AUD surveys not impressive, RBNZ two-way risk, NZ politics still a NZD negative, corrective equity markets weight on USD/JPY

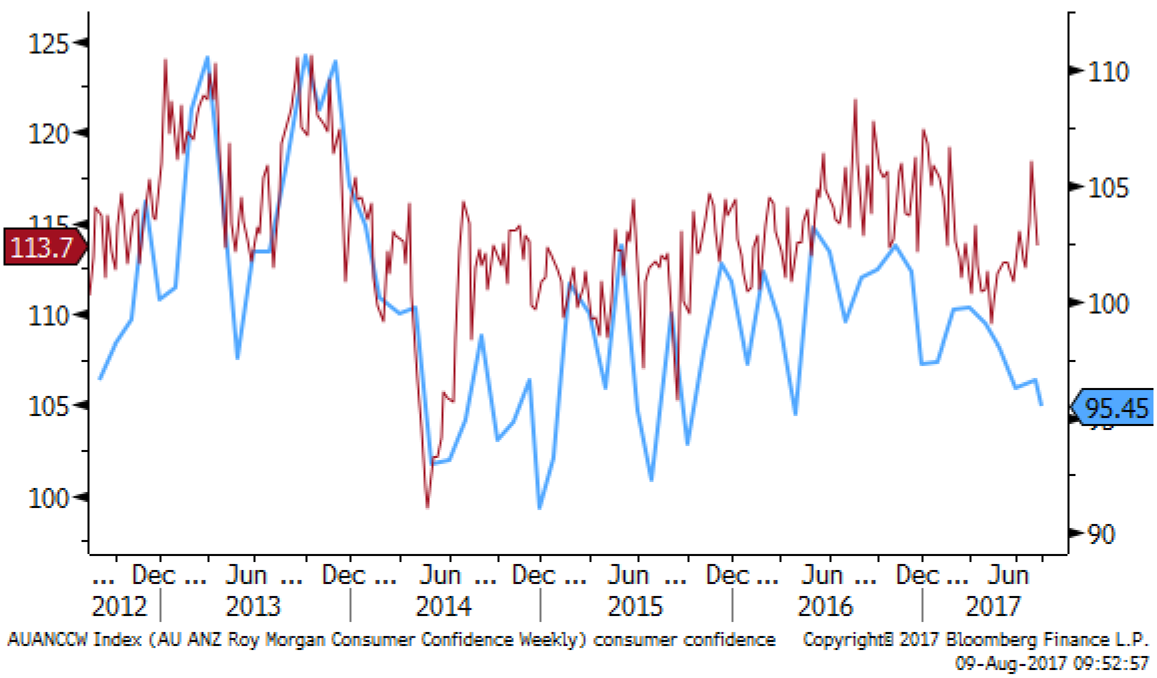
Positions

Long 1.5 units AUD/NZD at 1.0724; s/l 1.0713; t/p 1.1223

Long 0.5 unit USD/JPY at 110.42; s/l 109.33; 114.22

Note: 1 unit of long AUD/NZD was closed on stop (in profit) on Wednesday

Monthly consumer confidence in Australia remained subdued



The Westpac/MI monthly reading was quite soft, and does not support my long AUD/NZD position.

The survey showed a fall in current family finances vs. a year ago to low since 2014, but a rise in expected finances over the year ahead.

Westpac Economics (Bill Evans) said, “The Index components point to clear pressure on family finances. The sub-index tracking views on ‘finances vs. a year ago’ fell 5.1% to 78.1, the lowest level since June 2014.”

“The sub-index tracking expectations for ‘finances over the next 12 months’ firmed 2.1% to 100.4 in August.”

“The survey detail suggests increased pressures on family finances; concerns around interest rates; and housing affordability in NSW and Victoria are more than outweighing increased confidence around jobs.”

“Much of the weakness is likely to reflect a mix of weak growth in wages; increases in key costs such as electricity and emerging concerns about rising interest rates.”

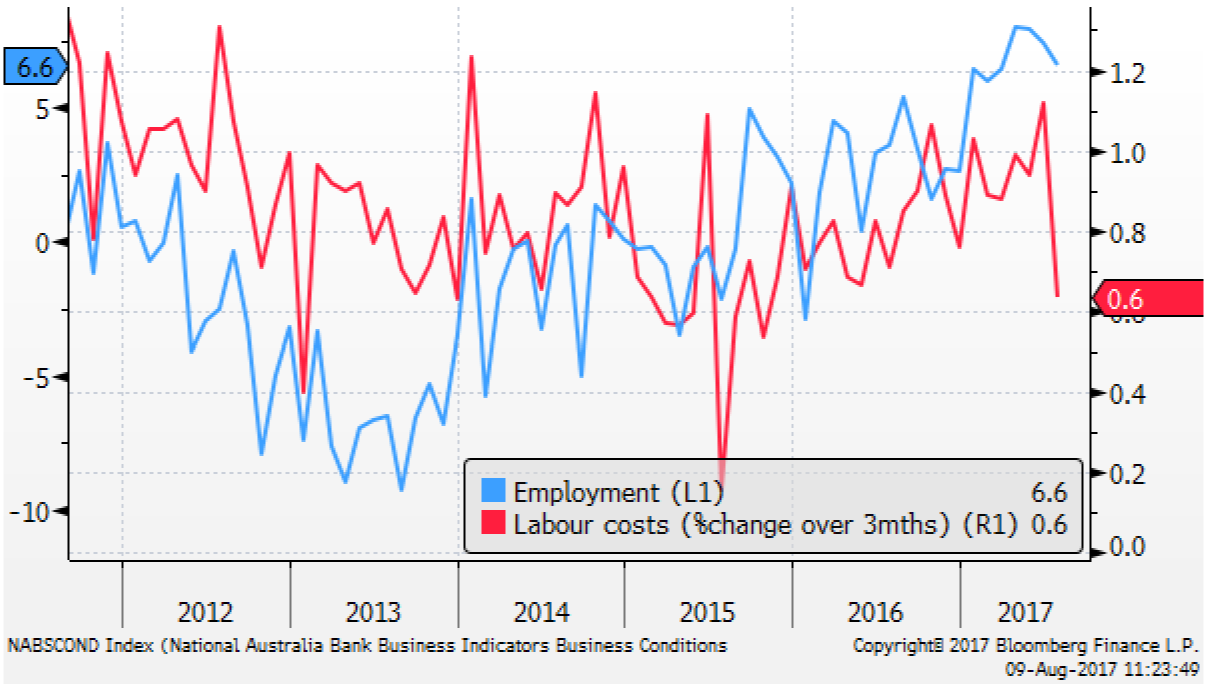
The survey results suggest that there is some concern over rising mortgage rates; three-quarters of respondents said they expect higher rates over the year. And some delayed response to the rise in mortgage rates on interest-only loans.

[Consumer sentiment deteriorates further - melbourneinstitute.unimelb.edu.au]

NAB survey components not so impressive

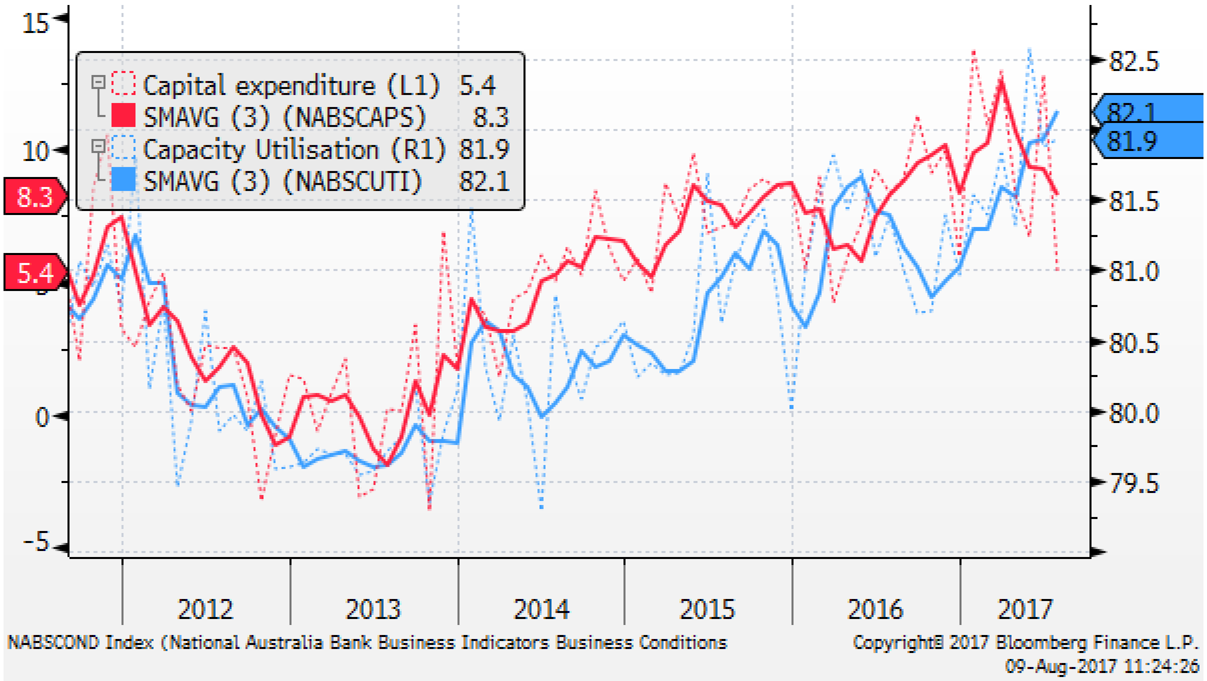
The NAB business survey showed strong headline conditions and confidence, but the underlying components were not impressive. Profitability was the only sub-component of the survey to increase. The report equally does not provide additional support for our long AUD/NZD position.

The labour cost component retreated significantly from +1.1% to +0.6% quarterly change in July. The employment component edged down for a second month to from a recent peak in April/May at 8.0 to 6.6 in July.



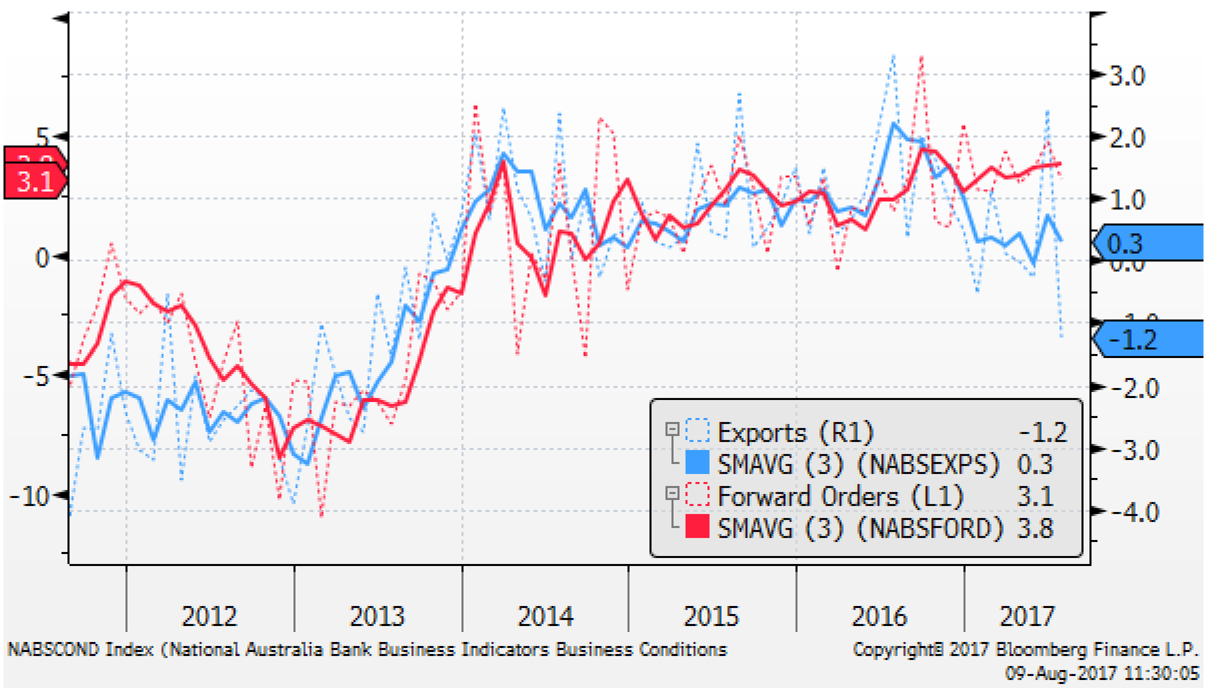
Capital expenditure intentions fell from 12.9 to 5.4 in July. It's volatile, but the three-month average fell from a peak of 12.6 in March to 8.3 in July.

Capacity utilization was up a bit to 81.9, down from its peak in May of 82.6, but its three-month average was at a peak of 82.1.



The Export component fell from +2.4 to -1.2, a low since 2013 (although the 3mth average is relatively stable)

New orders fell from 4.7 to 3.1, although the 3mth average firmed a bit to 3.8

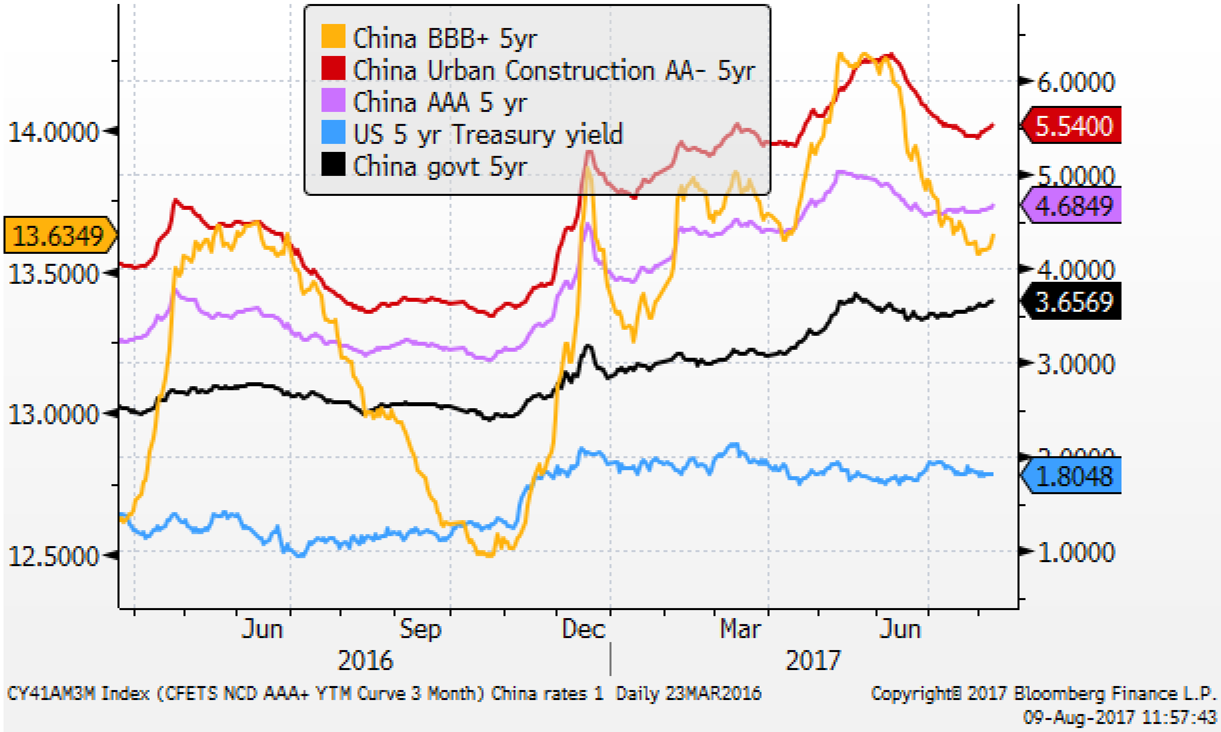


[NAB Monthly Business Survey: July 2017 - business.nab.au]

Chinese rates watch

The most recent Chinese trade data, with a pull-back in Chinese commodity imports and weaker trade growth data overall are also not supportive of our AUD/NZD trade. However, Chinese commodity prices have been relatively stable in around recent highs.

We are seeing some slight evidence of tightening in the Chinese shadow finance sectors. NCD rates (a funding vehicle for small and medium sized banks) have edged up recently (after falling back in the second half of June. Chinese corporate bond yields have clicked up a bit in recent weeks. The moves are modest so far, but need watching as AUD often trades a proxy for financial stress in China.



RBNZ two-way risk

The RBNZ policy statement is a near term factor that may influence the AUD/NZD cross. At the very least it will make the pair volatile around the event.

It is hard to predict what the RBNZ will say and do. They don't really need to change their main policy statement or medium term forecasts. But the quarterly MPS gives them the opportunity to shift the tone around their latest forecasts. There is a possibility that they choose to change their statement on the exchange rate to express a firmer desire for a lower rate, even though in fact commodity prices have risen further.

Analysts and commentators have concluded that the recent fall in the NZD reflects some expectation that the RBNZ will lower their rate forecasts. However, the RBNZ doesn't have a hike in the profile until the second half of 2019, near the end of their forecast profile. There isn't much scope to lower this further. Despite some weaker indicators this year, I don't see them discussing a risk of growth falling on a sustained basis below trend. As such, they are unlikely to forecast or express a risk that rates will be cut. As such, there is a risk that the market will see this as a reason for a rebound in NZD.

It is perhaps for this reason that I can see the RBNZ attempting to express a clearer desire for the NZD to remain lower or fall further, as an offset for leaving its rate outlook unchanged.

With inflation readings lower in Q2 than expected, and a weaker than expected housing market, the RBNZ might argue that a lower exchange rate would be more helpful in achieving its inflation goals. The most obvious tactic is to emulate the success the RBA had with the tweak to its exchange rate rhetoric.

NZ politics

NZ political polls show a massive rise in Labour support, fall in Greens and NZ First. Nationals also down a bit. As it stands, NZ First remains a likely kingmaker. The momentum behind Labour raises the odds that it take control of government.

Some may see a strong swing towards Labour leader Adearn after she took the leadership of her party as a positive thing, like Macron in France. However, the difference is that the market knows and likes Nationals. The next government will probably involve NZ First, the policy shift will be towards lower immigration and less foreign investment in the housing market, posing growth risks.

Newshub-Reid Research poll: NZ First overtakes Greens as third biggest party - newshub.co.nz

Heavy equity markets weigh on USD/JPY

USD/JPY has taken a hit since I went long on the back of the hotter rhetoric between President Trump and Supreme Leader Kim Jong-Un.

I didn't rush to exit the trade because I thought the latest war of words would be quickly dismissed as bluff and bluster.

It would seem the most obvious approach would be for the US to persist for the time being with sanctions. I thought the market would see the threat by Trump as exaggerated and hollow, as much of his rhetoric tends to be. The response by Kim probably further unsettled the market by specifically mentioning Guam, seeming to give it more credibility. However, such a response by Kim and/or the NK media is part of a regular pattern.

As such, I thought it best to hang tight. My stop loss is set below what could be a trend line touching the last two bottoms.

The extent of the fall in USD/JPY probably also reflects the fact that the stock market may be over-bought and vulnerable to a correction. That appears to be the view of many commentators quoting high valuations, sentiment surveys, low cash holdings, and thinner holiday markets. Analysts also see the market as now short JPY funding carry trades. As such we have seen a correction in most markets where positions are seen to be significant (short JPY, long EUR, long AUD, long NZD).

The NK/US tensions also contributed to some correction in AUD/NZD, after the recent significant fall in NZD, the AUD was more vulnerable to risk-off type trading.

Equities in the US are not bouncing today, so it does look like they are a bit heavy at the moment. US 10 year yields are off their lows, getting back to flat on the day, so this may be a bit more encouraging for USD/JPY.

The CPI data on Friday will be watched closely, and are a potential key factor for USD/JPY. The market is looking for a more normal 0.2%m/m rise in core and headline, anticipating that the recent weak trend in inflation has run its course.

I have no reason to doubt this expectation.

I bought USD/JPY on the view that some of the US data was looking better, Trump negativity may be getting fully priced in, and US yields looked like they may be turning up, having held above recent lows.

I don’t like the fact that USD/JPY has not been able to relatively quickly regain and hold the 110 level. In the current corrective mood in equities, downside risks remain. My position is small, and I will just leave the trade on with the stop loss that doesn't reflect huge conviction.

Disclosure and Certification

- The report does not contain and is not based on any non-public, material information.
- The information in this report has been obtained from sources we believe to be reputable and accurate, but we have not independently checked or verified that information.
-
- Our Company is incorporated and licensed in Australia to provide only general financial advice. Please see our financial services guide and terms and conditions for use of this report for more information.

Greg Gibbs,
Founder, Analyst and PM
Amplifying Global FX Capital Pty Ltd