ANZ RESEARCH

NEW ZEALAND ECONOMICS
MARKET FOCUS

7 June 2016

INSIDE

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THE PENDULUM

ECONOMIC OVERVIEW

We expect the RBNZ to retain the OCR at 2.25%; the economy doesn't need additional stimulus right now. In fact, a scenario where no further easing is delivered at all is actually becoming more credible. However, that looks a step too far for the RBNZ at present, and a clear easing bias will be retained on fear of turbo-charging the NZD to ever-greater heights. Admittedly, we still expect further easing too, in part because we expect to see pressures in the deposit market ramp up later in the year, which, in the absence of lower wholesale rates, will mean higher retail rates. Also this week, manufacturing data is likely to be mixed, while our Monthly Inflation Gauge will give an early steer on Q2 CPI. Housing data will no doubt be strong.

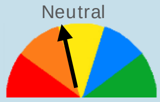
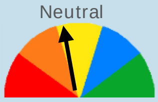
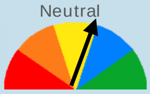
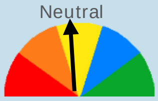
INTEREST RATE STRATEGY

Confirmation of no change to the OCR at the RBNZ *MPS* on Thursday has scope to drive short-end rates mildly higher and flatten the curve, especially given Friday's US data disappointment. In short, we're experiencing the kind of setback that often follows soft US non-farm payrolls data. New Zealand long-end rates generally go wherever US rates go, and the huge miss on US payrolls has gotten the market second guessing when the Fed will deliver its next rate hike. Spread convergence remains a key theme, and we look to episodes of relative New Zealand underperformance (as we have seen today) to re-enter strategic NZ/US spread narrowing trades.

CURRENCY STRATEGY

NZD/USD has quickly reversed from attempts to test lower, but we would try to avoid reading too much into the recent USD weakness. Despite the softer US data, we do not expect the USD to weaken too far, as the overall US economy still looks healthy. We would see a test of recent resistance (0.70-0.7050) as an opportunity to increase hedging for those with currency to sell. NZD/AUD remains strong, with room to test higher still, although we view levels over 0.95 as opportunity to build hedging for importers.

THE ANZ HEATMAP

Variable	View	Comment	Risk profile (change to view)
GDP	2.4% y/y for 2017 Q1	While growth momentum looks reasonable now, tighter financial conditions suggest a more moderate backdrop over 2H 2016.	Neutral Negative  Positive
Unemployment rate	5.3% for 2017 Q1	The unemployment rate should continue to trend lower. Wage inflation is contained, but a turn may be in sight.	Neutral Negative  Positive
OCR	1.75% by Mar 2017	A further 50bps of cuts out to early 2017, despite housing, with the global scene and NZD strength key drivers.	Neutral Down  Up
CPI	1.4% y/y for 2017 Q1	Lower petrol prices and further ACC levy cuts from July expected to keep headline inflation low this year. Core inflation measures to remain historically low.	Neutral Negative  Positive

ECONOMIC OVERVIEW

SUMMARY

We expect the RBNZ to retain the OCR at 2.25%; the economy doesn't need additional stimulus right now. In fact, a scenario where no further easing is delivered at all is actually becoming more credible. However, that looks a step too far for the RBNZ at present, and a clear easing bias will be retained on fear of turbo-charging the NZD to ever-greater heights. Admittedly, we still expect further easing too, in part because we expect to see pressures in the deposit market ramp up later in the year, which, in the absence of lower wholesale rates, will mean higher retail rates. Also this week, manufacturing data is likely to be mixed, while our Monthly Inflation Gauge will give an early steer on Q2 CPI. Housing data will no doubt be strong.

FORTHCOMING EVENTS

Economic Survey of Manufacturing – Q1 (10:45am, Wednesday, 8 June). We are expecting a mixed picture. Weaker livestock slaughtering could weigh on primary good volumes, but "core" manufacturing activity is likely to have held up well.

RBNZ *Monetary Policy Statement* (9:00am, Thursday, 9 June). We don't think the economy needs further interest rate support right now and expect the RBNZ to maintain the OCR at 2.25%. However, a clear easing bias will be retained.

Electronic Card Transactions – May (10:45am, Friday, 10 June). We have pencilled in a 0.5% m/m increase. Higher petrol prices will likely lift fuel spending.

Monthly Inflation Gauge – May (Friday, 1:00pm, 10 June).

REINZ Housing Market Statistics – May (possibly Monday, 13 June). Strength in the regions is being joined by a sharp recovery in Auckland activity. National house price growth is rising again.

WHAT'S THE VIEW?

It certainly doesn't feel like the economy is crying out for further interest rate support right now. House prices are booming. Household credit is growing at its fastest pace since 2008, and is actually starting to look rather problematic! Population growth is the strongest since 1990 and GDP growth is running around 3%. Business and consumer confidence are holding at reasonable levels. Non-dairy exports are rising nicely; the NZD is not an issue for the majority. The construction sector just experienced its best quarterly growth in two years (off already-elevated levels). Anecdotes suggest capacity constraints are becoming an increasing issue on the ground and this links in with the RBNZ's sectoral factor model of inflation (a slow-moving beast that is intuitively appealing – and slowly rising).

A strict interpretation of inflation targeting would imply another rate cut. Inflation is low, and so are inflation expectations. The NZD is trading a long way above where the RBNZ assumed it would be.

The problem is: a) trying to get inflation back up amidst secular inflation-suppressing forces (global forces, technology, shifts in wage-bargaining dynamics) is not easy; and b) the last two OCR cuts didn't get the currency down so it's whistling Dixie trying with a third! Meanwhile, more interest rate fuel obviously turns the heat up further on asset prices. **We're not believers in strict interpretations of inflation targeting; some pragmatism is required, and especially in the current instance.**

All up, we expect the RBNZ to maintain the OCR at 2.25% this week. **In fact, we think there is a credible scenario emerging of the RBNZ actually not delivering any further stimulus at all!**

We don't think the RBNZ will be prepared to take that view this week. There might be some subtle hints within the statement or projections, or even in the various scenarios presented. And it already looks to be a view that the market is slowing coming around to, as it has scaled back the extent of easing priced in. But we have little doubt that the RBNZ will still maintain a clear easing bias, leaving it clear about the likely direction of any future interest rate moves. Fear of turbo-charging the NZD to ever-greater heights will be motivation enough for the RBNZ to retain a relatively dovish stance.

Our base case is still that the RBNZ will be dragged back to the rate-cutting table once again. We may only place the odds of a cut in August at around 60% (i.e. it is far from a strong view), but we still see further easing over the next 12 or so months as more likely than not. The global scene and currency pressures leave the risks skewed in that direction. When currencies don't play ball and diverge from fundamentals, rates will be pressured to converge over time. The market is just taking a tactical hiatus within that strategic endgame.

A key reason we retain our easing expectation is that pressures in the domestic deposit market are set to intensify later in the year and that means pressure on retail rates to rise if wholesale rates do not fall. The current pace of credit growth relative to deposit growth is simply not sustainable – the former needs to slow and the latter to lift. In a market such as New Zealand where there is a limited saving pool, banks must look offshore to close the gap, and offshore credit spreads have widened. They may not be as wide as they were in February, but they are still above the average of the past three years. Wider issue costs overseas will inevitably turn

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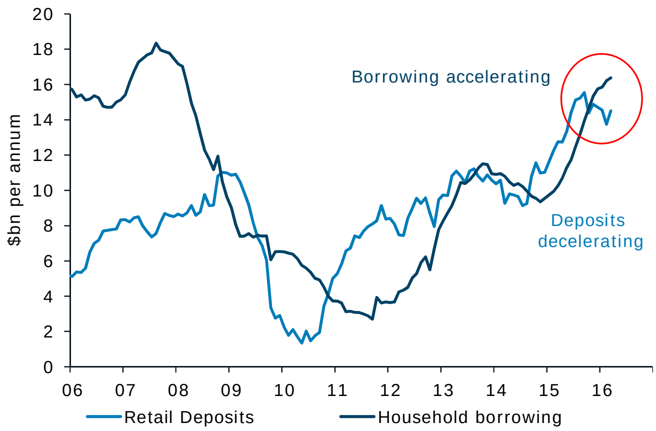
attention back towards the (currently) cheaper local market. It's simple arbitrage.

Relative prices (deposit vs. lending rates) are now manifesting in slowing deposit growth and rising credit growth. That's what happens when interest rates fall but also signals that the relative price has pushed too far in favour of borrowers.

FIGURE 1: BANK FUNDING AND CLAIMS GROWTH



Source: ANZ, RBNZ

A ramping up of competition in the deposit market is likely towards the back half of the year, which all else equal will see pressure on both lending and deposit retail rates to rise, not fall. As older, cheaper funding is replaced by newer, more expensive funding, banks' average costs of funds will lift.

It's incongruous to imagine credit growth can continue to run at the current rate – especially in the housing market. That risks destabilising the economy through a) the accumulation of too much debt (household debt levels relative to income are already higher than prior to the GFC); b) manifesting in an asset bubble (arguably already occurring); and c) making New Zealand more dependent on offshore funding (there has been a huge effort since the GFC to reduce that dependence).

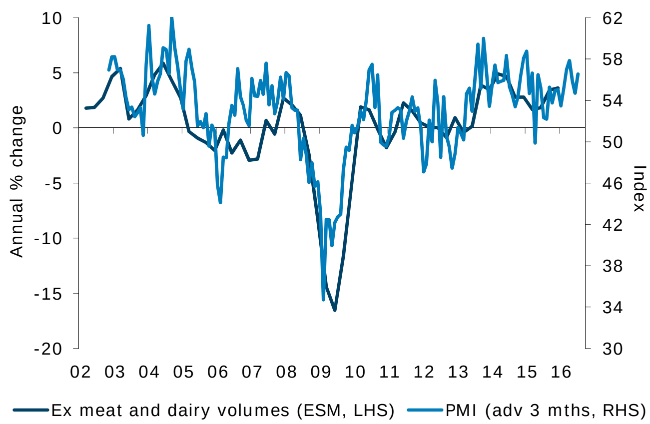
Deposit and credit growth need to converge, which means either one moving fairly sharply, or the two nudging closer together from either side. Logically, deposit growth will need to be at least maintained and credit growth needs to slow.

There will be other consequences. If credit growth needs to slow then that will impact housing supply. Section and apartment lending is more risky than owner-occupied dwellings and will face more scrutiny if credit is being more actively rationed. And these are areas the supply-side needs to step up. That's one big pickle. How do you slow credit growth to a more sustainable level without it negatively impacting available housing supply? It's a tough balancing act.

The above pressures should eventually help result in a better mix of monetary conditions. Housing needs higher retail interest rates but we also need lower wholesale rates to get the currency down to ease dairy pressures. That needs a "wedge" between retail borrowing rates and wholesale rates, and increased competition for domestic deposits along with prudential policy tweaks would help drive that. It would allow the OCR and wholesale rates to fall, but should see retail deposit and borrowing rates not fall by as much, or even rise. Despite our expectation of further OCR cuts, we still see the pendulum swinging away from borrowers and back towards depositors again, and that is a good thing.

Turning to other events this week, the Q1 Economic Survey of Manufacturing is likely to be mixed. With our seasonally adjusted estimates showing livestock slaughtering falling 13% over the quarter, and milk production dipping a touch as well, the figures are expected to show weaker primary good manufacturing activity over the quarter. This is in part due to the hang-over from earlier slaughtering on El Nino fears, and also the cost recalibration occurring in the dairy sector. However, from the perspective of drawing implications for upcoming GDP figures, it is actually "core" (non-dairy and meat) activity that we are more interested in. While movements in sales and inventories need to be adjusted for, PMI data has been providing a signal of pretty decent activity in the sector, and we expect core volumes to have posted a further positive gain over the quarter.

FIGURE 2: MANUFACTURING VOLUMES AND SENTIMENT



Source: ANZ, RBNZ

With regards to how our expectations for Q1 GDP are shaping at present, reasonable growth looks as though it has been recorded. Certainly, the signal from the likes of last week's OTI and Regional Trends figures highlighted some downside risk to our earlier estimates. However, this was mitigated to a large extent by building work data showing that sector surging strongly in Q1. So while the risk is still perhaps

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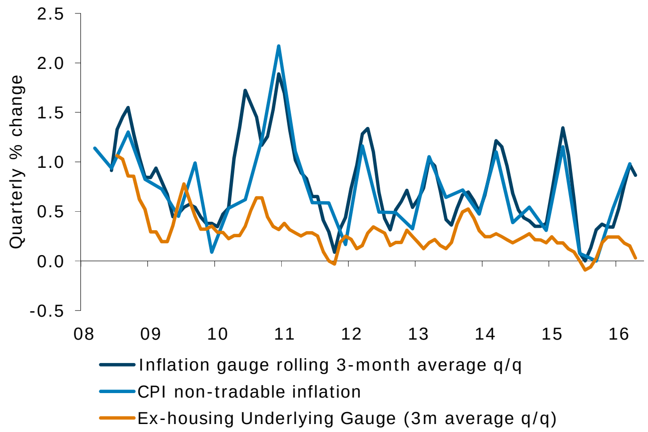
modestly skewed towards a softer GDP outcome (particularly when considering some pay-back from the strong growth over the second half of last year), **our bottom-up estimate sits around 0.7% q/q,** a number which we will look to finalise after the manufacturing figures.

Volatility aside, Electronic Card Transactions data for May should still show a reasonable underlying trend. We have pencilled in a 0.5% m/m gain in total retail spending, with higher fuel prices lifting fuel retailing. While higher petrol prices do reduce households' discretionary cash flow, and the strain in the dairy sector will no doubt be an issue for retailers in many rural areas, we believe that there are enough factors to support the consumer spending environment overall. The labour market continues to improve, net wealth gains from housing are clear, credit growth is accelerating (although this creates medium-term risks), population growth is strong and the tourism sector continues to boom.

Our Monthly Inflation Gauge for May will provide an early indication of how risks around Q2 CPI are shaping up. The Gauge rose 0.1% in April, which was consistent with seasonal norms. While we can certainly detect demand-pull inflation pressures in the likes of construction and housing, the overall inflation picture remains benign. Plugging in average results for May and June over the past three years would imply a 0.3% q/q lift in non-tradable CPI over the quarter.

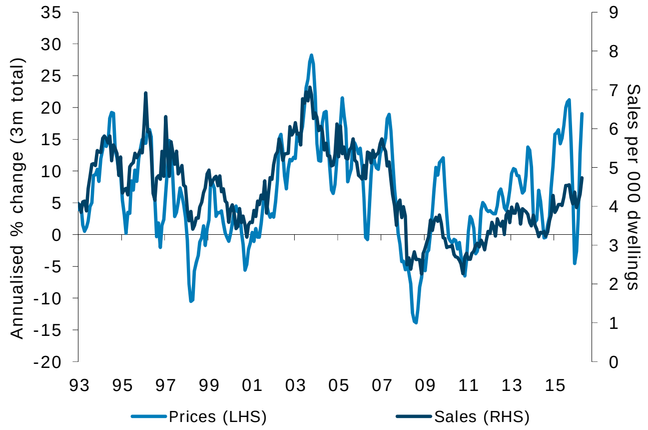
FIGURE 3: MONTHLY INFLATION GAUGE VS NON-TRADABLE CPI



Source: ANZ, Statistics NZ

It is also possible that REINZ housing markets figures for May will be released early next week. These will no doubt be strong. To be fair, a fall in turnover is possible after April's 10% m/m gain, with the level of nationwide turnover sitting at its highest level in nine years. But it's clear from anecdotes of strong open home attendance, multiple offers for vendors and high auction clearance rates that any dip in sales activity wouldn't be indicative of the market overall. Tight inventory levels (falling days to sell), low interest rates and strong investor demand are certainly some powerful tailwinds, and we expect to see a further acceleration in house price growth. This will be led by the regions, although rising Auckland house prices are likely to have continued too.

FIGURE 4: NATIONWIDE HOUSE PRICES AND SALES GROWTH



Source: ANZ, REINZ

LOCAL DATA

Building Consents Issued – April. The number of dwelling consents bounced 6.6% m/m, while non-residential consents were valued at $500m (sa).

ANZ Business Outlook – May. Headline confidence rose 5 points to +11. While firms' own activity expectations fell (-2 points to +30), they remain above historical averages.

RBNZ Credit Aggregates – April. Total private sector credit grew +0.7% m/m (+7.4% y/y) – the strongest annual growth since January 2009.

Overseas Trade Indexes – Q1. The terms of trade rose 4.4% q/q. Export volumes fell 2.7% q/q, while import volumes fell 0.7% q/q.

QV House Prices – May. Nationwide house price growth accelerated to 12.4% y/y.

ANZ Regional Trends – Q1. The nationwide composite measure of economic activity was unchanged. North Island activity was unchanged, while South Island activity rose 0.1% q/q.

GlobalDairyTrade Auction. The GDT TWI rose 3.4%, while whole milk powder prices fell 1.7%.

Building Work Put in Place – Q1. Total building work volumes surged 5.3% q/q (10.7% y/y).

ANZ Commodity Price Index – May. The world price index lifted 1.0% m/m, with NZD prices increasing 2.5% m/m.

ANZ Truckometer – May. The Heavy Traffic Index fell 1.7% m/m, while the Light Traffic Index fell 1.3% m/m.

INTEREST RATE STRATEGY

SUMMARY

Confirmation of no change to the OCR at the RBNZ *MPS* on Thursday has scope to drive short-end rates mildly higher and flatten the curve, especially given Friday's US data disappointment. In short, we're experiencing the kind of setback that often follows soft US non-farm payrolls data. New Zealand long-end rates generally go wherever US rates go, and the huge miss on US payrolls has gotten the market second guessing when the Fed will deliver its next rate hike. Spread convergence remains a key theme, and we look to episodes of relative New Zealand underperformance (as we have seen today) to re-enter strategic NZ/US spread narrowing trades.

THEMES

- Markets are in for a shake-up whatever the RBNZ decision, with 8bps of cuts priced in, and either zero or 25bps on the table. But with an easing bias intact, there is a limit to how high short-end rates can go (and we're almost there).
- Lower US interest rates and the surge in the NZD TWI (to around 74 this morning) highlight the concerns facing the RBNZ. But we don't think it will be enough to tip it over the edge and see it cut the OCR on this occasion.
- Fed Chair Yellen dropped the term "coming months" from her last pre-FOMC speech, but maintained her view that gradual rises remain on the cards.
- We take a breather on our strategic tilt towards curve steepening as the US market re-litigates the timing of the Fed's next move in the wake of the huge non-farm payrolls miss.
- Our higher US bond yield forecasts are predicated on Fed rate hikes. We remain of the view that the Fed will deliver two hikes this year, but markets are pricing in just "0.6" of a hike by December. US bond yields will range trade until we see the market firm up its view on the timing of hikes.

PREFERRED STRATEGIES – INVESTORS

KEY VIEWS – FOR INVESTORS		
GAUGE	DIRECTION	COMMENT
Duration	Neutral	Yields set to drifty mildly higher this week. NZ cheap on global relative basis, and we prefer duration in NZ than in the US.
2s10s Curve	Neutral	Needs US bonds to rise (and thus the Fed to hike) before it can steepen in earnest.
Geographic 10yr spread	Narrower	Divergent policy biases argue for further gradual narrowing, especially off current levels.
Swap spreads	Neutral/wider	Reduced NZGS supply and increased hedge paying.

RBNZ *MPS*: MARKET SHAKE-UP EITHER WAY

We expect the Reserve Bank to leave the OCR on hold at Thursday's *Monetary Policy Statement*. As we discuss in more depth on page 2, the economy simply doesn't need a cut at the moment. Under the hood, the economy is pretty strong, with tourism, the non-dairy agricultural sectors, the housing market and construction all performing well. And while Friday's miss on US non-farm payrolls has put the proverbial cat amongst the pigeons for the Fed as it weighs up its decision for June, the global scene is far less tumultuous than it was in March (even if it is still somewhat fragile).

Nonetheless, we still expect the Bank to retain an easing bias, mindful of ongoing global fragilities, prospects for increased competition for deposits (which will force up borrowing rates if the OCR does not fall), and the resurgent NZD. The latter deserves attention, particularly with the NZD TWI hovering around January highs (Figure 1). Importantly, the NZD is higher than it was in March, when the RBNZ cited it as a factor in its decision to cut the OCR. In our view, this (and the sharp decline in US bond yields since Friday) will be of concern to the Reserve Bank as it deliberates, but we don't think it will be enough to tip it back over the line into the rate-cut camp. However, it does underline another key point that we have been stressing all along: **the low inflation backdrop demands an easing bias,** even if the bulk of the disinflation is global, rather than domestic, in nature.

FIGURE 1: NZD TWI – BACK AT THE YEAR'S HIGHS

Source: ANZ, Bloomberg

Whatever decision the Bank makes on Thursday, markets are in for a shake-up. With around 30% odds of a cut priced in, the very front end will go one way or the other on the OCR announcement itself. **However, the real focus will be the tone of the document, the Bank's projections, and forward guidance. It is our view that the Bank will maintain an easing bias that underlies our expectation that we are approaching the limit of**

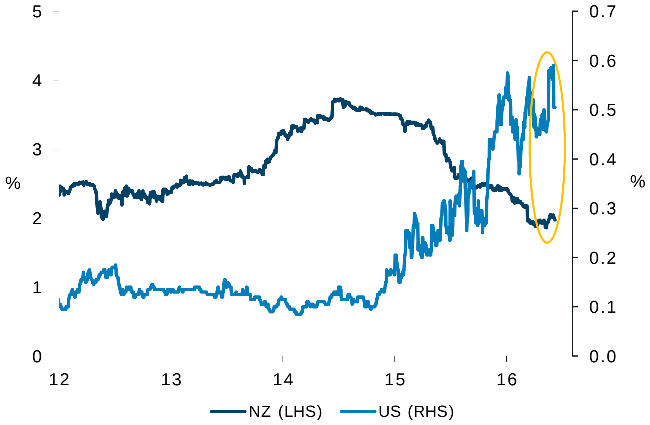
INTEREST RATE STRATEGY

how high bellwethers like the 2 year swap can go. In early trade today, short-end rates are actually a couple of points lower than they were on Friday, with the market taking a lead from the rally in US rates. However, we do expect a mild correction on Thursday – assuming we don't see an OCR cut.

BACK TO THE DRAWING BOARD

Friday's US non-farm payrolls disappointment sent rate-cut expectations (Figure 2) and bond yields nose-diving again. This is familiar territory – and if we're honest we have lost count how many times the market has had to re-hash its Fed view, or had soft data disappoint what had been such an intuitive or obvious course of action. On this occasion, **the US market has all but abandoned any possibility of a June or July rate hike**, with Bloomberg analytics ascribing just 22% odds of a hike by July. That's down from 54% last Monday.

FIGURE 2: 6 MONTH AHEAD CASH RATE EXPECTATIONS

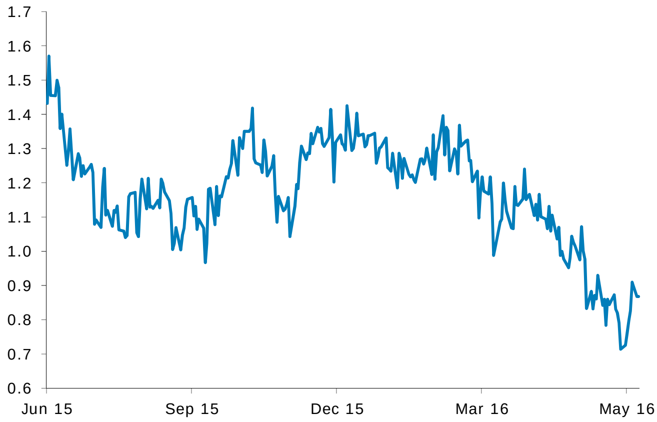


Source: ANZ, Bloomberg

While US market moves since Friday feel like a massive over-reaction to one (volatile) data release, Fed chair Yellen has seemingly endorsed the market's new-found bearishness. Indeed, in her last speech before next week's FOMC meeting, Yellen omitted the term "in coming months", but maintained her view that "the Fed funds rate will probably need to rise gradually over time". Plenty of wriggle room there – no wonder the market is only pricing "0.6" of a hike by December.

For local markets, the combination of less Fed easing than was otherwise envisaged and the maintenance of an easing bias by the RBNZ spells lower outright long-end yields. However, the tendency for spreads to widen as bond yields fall (which is itself a by-product of New Zealand's low-beta status) means that we have seen the NZ/US bond spread snap higher. This type of volatility is typical, but given the divergent direction of NZ and US monetary policy, we continue to favour adding to NZGS on a spread to the US on back-ups like the one we have seen today.

FIGURE 3: NZ/US 10 YEAR BOND SPREAD



Source: ANZ, Bloomberg

PREFERRED STRATEGIES – BORROWERS

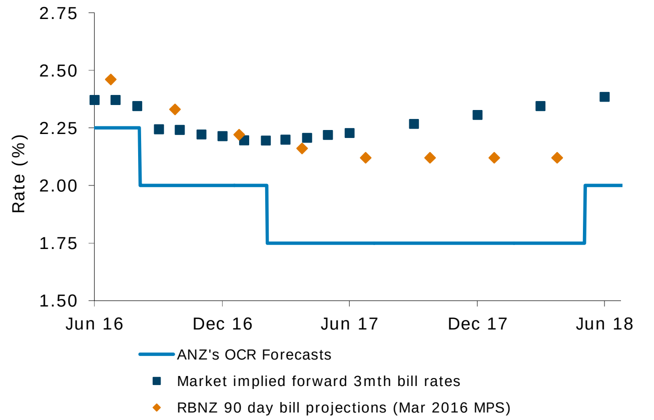
Our expectation of higher US interest rates points to higher term rates here, albeit with some offset provided by spreads. **However, OCR stability/cuts will keep BKBM lower for longer, making for a quandary best solved via optionality**.

KEY VIEWS – FOR BORROWERS		
GAUGE	**VIEW**	**COMMENT**
Hedge ratio	Majority hedged	Options preferred for upside protection AND exposure to lower floating interest rates.
Value	Cheap	More upside risk emerging.
Uncertainty	Elevated	Watch credit spreads.

MARKET EXPECTATIONS

Market pricing has swung back to around 30% odds of a cut on Thursday. **Confirmation of no change is likely to lead to further upward re-pricing of the very short end, but the easing bias will limit how far bellwethers like the 2-year can go**. We think 2.25%/2.30% represents the upper limit of the 2-year.

FIGURE 3: ANZ OCR FORECAST VS MARKET-IMPLIED FWD 3MTH BILL RATES AND RBNZ 90-DAY PROJECTION



Source: ANZ, Bloomberg

CURRENCY STRATEGY

SUMMARY

NZD/USD has quickly reversed from attempts to test lower, but we would try to avoid reading too much into the recent USD weakness. Despite the softer US data, we do not expect the USD to weaken too far, as the overall US economy still looks healthy. We would see a test of recent resistance (0.70-0.7050) as an opportunity to increase hedging for those with currency to sell. NZD/AUD remains strong, with room to test higher still, although we view levels over 0.95 as opportunity to build hedging for importers.

TABLE 1: KEY VIEWS

CROSS	WEEK	MONTH	YEAR
NZD/USD	↔/↑	Fed delayed?	Profile still lower
NZD/AUD	↔/↑	Room to test higher	Remain above long-run averages
NZD/EUR	↔	Still in range	Political risks for EUR
NZD/GBP	↔/↑	Brexit re-emerges	GBP resurgence
NZD/JPY	↔/↑	Oversold?	JPY returning to averages

THEMES AND RISKS

- With minimal US data and the Fed on “blackout”, we don’t see much to alter the perception created by weak US data; thus a soft USD is expected.
- We expect “no change” decisions from both the RBNZ and RBA this week. However, both have ample ability to drive currency direction with commentary, with rates market pricing suggesting risks are biased lower in both cases.
- Chinese data this week is expected to continue to recover, supporting risk, commodities and commodity-based currencies.

TABLE 2: KEY UPCOMING EVENT RISK

EVENT		WHEN (NZST)	IMPACT RISK
AUD	RBA	Tue 16:30	NZD/AUD ↑
EUR	German Industrial prod.	Tue 18:00	NZD/EUR ↑
EUR	Q1 GDP (f)	Tue 21:00	NZD/EUR ↔/↑
GBP	BoE Governor Carney	Wed 09:00	NZD/GBP ↑
NZD	Q1 mfg activity	Wed 10:45	NZD ↑
AUD	Home lending	Wed 13:30	NZD/AUD ↑
CNY	Chinese trade balance	Wed PM	NZD/CNY ↑
GBP	Industrial production	Wed 20:30	NZD/GBP ↓
USD	Jolt Jobs report	Thu 02:00	NZD/USD ↓
NZD	RBNZ	Thu 09:00	NZD ↑
CNY	CPI, PPI	Thu 13:30	NZD/CNY ↔/↑
EUR	ECB Draghi	Thu 19:00	NZD/EUR ↑
CAD	BoC FSR	Fr 02:30	NZD/CAD ↓
USD	Q1 Household net worth	Fri 04:00	NZD/USD ↓
NZD	Card spending	Fri 10:45	NZD ↑
EUR	German CPI (f)	Fri 18:00	NZD/EUR ↑
CAD	Employment	Sat 00:30	NZD/CAD ↓
USD	Michigan Conf	Sat 02:00	NZD/USD ↓
CNY	May Data (IP, R/S, FAI)	Sat 17:30	NZD/CNY ↑
AUD	Queen's Birthday	Mon	NZD/AUD ↔

EXPORTERS’ STRATEGY

We don’t favour chasing this move higher, as NZD/USD direction remains dependent on USD direction, which – despite payrolls weakness – remains uncertain. We prefer to target dips.

IMPORTERS’ STRATEGY

We are at NZD/AUD levels where we favour importers adding to cover. Similarly, we favour NZD/USD importers building up hedges above 0.69 – US hikes are coming even if they are delayed this time.

DATA PULSE

NZD is supported by local data, with the Q1 terms of trade lifting, headline GDT prices increasing (although we note WMP weakness), another solid ANZ business confidence result, and the ex-dairy basket of ANZ commodity prices stable.

USD weakness is the driver for NZD/USD. Despite a headline increase in the manufacturing ISM, US data hasn’t supported the USD, with a weak non-manufacturing ISM, modest Beige Book, and very low payrolls report, although wage growth is reasonable.

Local factors have not been driving EUR, with the Markit PMIs expansionary but uninspiring. EU CPI is deflationary and the ECB in watch-and-wait mode.

Chinese activity data continues to support risk with solid, if unspectacular, PMI results.

GBP was driven lower by Brexit polls showing gains for the leave campaign. There were some encouraging signs from resurgent PMI activity indicators, with expansions from all sectors.

AUD also found support with a strong performance from Q1 GDP, backed up by other data.

TABLE 3: NZD VS AUD: MONTHLY GAUGES

GAUGE	GUIDE	COMMENT
Fair value	↔	FV is above long-run averages.
Yield	↔	In-line with shift in yields.
Commodities	↔	We note iron ore strength.
Data	↔/↑	NZD data is resilient.
Techs	↔/↓	Towards the top of the range.
Sentiment	↔	Equal reactions to sentiment.
Other	↔/↓	RBA sentiment the driver.
On balance	↔	**Close to top of range.**

TABLE 4: NZD VS USD: MONTHLY GAUGES

GAUGE	GUIDE	COMMENT
Fair value	↔	Closer to fair value.
Yield	↔/↓	RBA cut applies pressure.
Commodities	↔	Risks reasonably well priced.
Risk aversion	↔/↑	Resilience to risk notable.
Data	↔/↑	US data has turned lower.
Techs	↔	Testing pivotal support
Other	↑	USD hit by Fed uncertainty.
On balance	↔	**Factors still point lower, but near-term catalysts missing.**

CURRENCY STRATEGY

TECHNICAL OUTLOOK

FIGURE 1. NZD/USD DAILY CANDLES WITH RSI & MA

NZD/USD didn't properly test support and payrolls weakness has shot it back to the top of the range. We hope that buyers managed to get filled last week, as the profile has again shifted to a test of the topside. That said, resistance remains formidable above the 0.70 zone and we suspect sellers will be prevalent in that region.

FIGURE 2. NZD/AUD DAILY CANDLES WITH RSI & MA

NZD/AUD is testing pivotal resistance near 0.95. A break of this level would open up a move to the next resistance which stretches from 0.96 almost to 0.97. We would view moves above 0.95 toward this resistance as impulsive given the overbought nature of this cross.

TABLE 5: KEY TECHNICAL ZONES

CROSS	SUPPORT	RESISTANCE
NZD/USD	0.6600 – 0.6650 0.6480 – 0.6520	0.7050 – 0.7080 0.7180 – 0.7220
NZD/AUD	0.9160 – 0.9200 0.9010 – 0.9060	0.9480 – 0.9520 0.9630 – 0.9660
NZD/EUR	0.5800 – 0.5850	0.6200 – 0.6230
NZD/GBP	0.4530 – 0.4560	0.4930 – 0.4980
NZD/JPY	69.80 – 70.20	77.70 – 78.50

POSITIONING

Leverage funds added to net long USD positioning in the week ending 31 May; however, this report predates the Payrolls disappointment. JPY and GBP longs were added to, and there were small additions to NZD and CAD longs, but AUD longs were reduced.

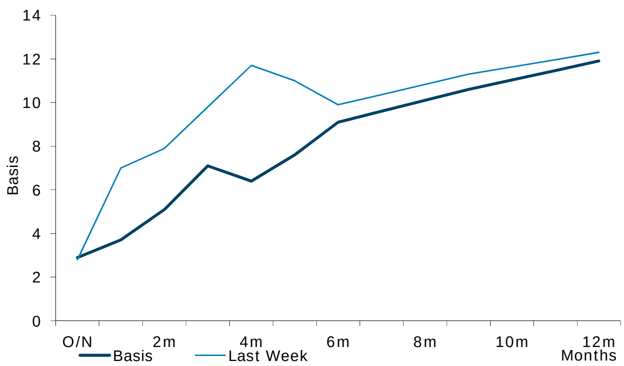
GLOBAL VIEWS

The USD itself continues to be the focus for currency markets, with the question of Fed normalisation the primary driver. The Fed had been signalling that it was close to continuing the normalisation process, but the data has turned softer with markets noting the particularly weak payrolls report and softer details in the ISM surveys.

It remains a question of when, not if, the US Fed will continue the normalisation process. But the dynamic for the USD appears to be changing. The Fed and markets are assigning a greater degree of circularity to the idea that normalisation will result in USD strength. This is because USD strength acts as a break on the economy, lessening the requirement to normalise. Thus those looking for USD strength to provide relief for 'overvalued' currencies (an argument common amongst NZD and AUD traders) would do well to note this change.

FORWARDS: CARRY AND BASIS

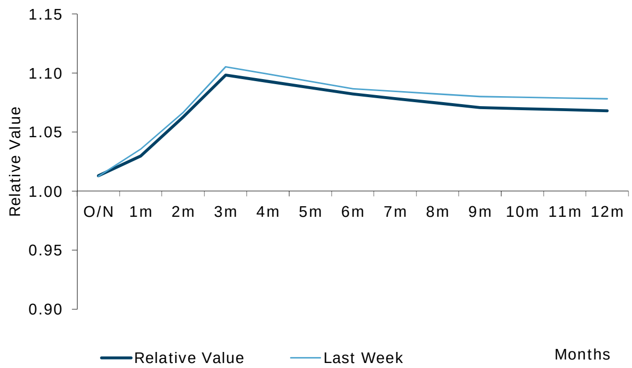
FIGURE 3. NZD/USD SHORT BASIS CURVE



Source: ANZ, Bloomberg, Reuters

Short-end basis remains tight, but 3mth FRA/OIS is very wide at 25.5bpts (has been at 20) so this has tightened the basis point value. Implied yields remain near unchanged from last week and cash has remained stable trading around OCR, implying light positioning in the spot market.

FIGURE 4. RELATIVE ATTRACTION OF THE FWD CURVE



Source: ANZ, Bloomberg, Reuters

DATA EVENT CALENDAR

DATE	COUNTRY	DATA/EVENT	MKT.	LAST	NZ TIME
7-Jun	AU	RBA Cash Rate Target - Jun	1.75%	1.75%	16:30
	GE	Industrial Production SA MoM - Apr	0.7%	-1.3%	18:00
	GE	Industrial Production WDA YoY - Apr	1.0%	0.3%	18:00
	AU	Foreign Reserves - May	--	A$65.7B	18:30
	UK	Halifax House Prices MoM - May	0.3%	-0.8%	19:30
	UK	Halifax House Price 3Mths/Year - May	8.9%	9.2%	19:30
	EC	GDP SA QoQ - Q1 F	0.5%	0.5%	21:00
	EC	GDP SA YoY - Q1 F	1.5%	1.5%	21:00
	CH	Foreign Reserves - May	$3200.0B	$3219.7B	UNSPECIFIED
	CH	Leading Index - Apr	--	99.1	7-9 Jun
8-Jun	US	Nonfarm Productivity - Q1 F	-0.6%	-1.0%	00:30
	US	Unit Labor Costs - Q1 F	4.0%	4.1%	00:30
	US	IBD/TIPP Economic Optimism - Jun	48.2	48.7	02:00
	US	Consumer Credit - Apr	$18.00B	$29.67B	07:00
	NZ	Mfg Activity Volume QoQ - Q1	--	1.3%	10:45
	NZ	Mfg Activity SA QoQ - Q1	--	-1.9%	10:45
	JN	BoP Current Account Balance - Apr	¥2303.0B	¥2980.4B	11:50
	JN	BoP Current Account Adjusted - Apr	¥2013.7B	¥1893.6B	11:50
	JN	Trade Balance BoP Basis - Apr	¥919.0B	¥927.2B	11:50
	JN	GDP SA QoQ - Q1 F	0.5%	0.4%	11:50
	JN	GDP Annualized SA QoQ - Q1 F	1.9%	1.7%	11:50
	JN	GDP Nominal SA QoQ - Q1 F	0.6%	0.5%	11:50
	JN	GDP Deflator YoY - Q1 F	0.9%	0.9%	11:50
	AU	Home Loans MoM - Apr	2.5%	-0.9%	13:30
	AU	Investment Lending - Apr	--	1.5%	13:30
	AU	Owner-Occupier Loan Value MoM - Apr	--	-1.2%	13:30
	UK	Industrial Production MoM - Apr	0.0%	0.3%	20:30
	UK	Industrial Production YoY - Apr	-0.4%	-0.2%	20:30
	UK	Manufacturing Production MoM - Apr	-0.1%	0.1%	20:30
	UK	Manufacturing Production YoY - Apr	-1.5%	-1.9%	20:30
	US	MBA Mortgage Applications - 3-Jun	--	-4.1%	23:00
	CH	Trade Balance - May	$55.85B	$45.56B	UNSPECIFIED
	CH	Exports YoY - May	-4.0%	-1.8%	UNSPECIFIED
	CH	Imports YoY - May	-6.7%	-10.9%	UNSPECIFIED
9-Jun	UK	NIESR GDP Estimate - May	--	0.3%	02:00
	US	JOLTS Job Openings - Apr	5675	5757	02:00
	NZ	RBNZ Official Cash Rate - Jun	2.00%	2.25%	09:00
	UK	RICS House Price Balance - May	35%	41%	11:01
	CH	CPI YoY - May	2.2%	2.3%	13:30
	CH	PPI YoY - May	-3.2%	-3.4%	13:30
	GE	Trade Balance - Apr	€22.8B	€26.2B	18:00
	GE	Current Account Balance - Apr	€21.0B	€30.4B	18:00
	GE	Exports SA MoM - Apr	-0.8%	1.9%	18:00
	GE	Imports SA MoM - Apr	1.3%	-2.3%	18:00
	GE	Labor Costs WDA YoY - Q1	--	2.1%	18:00
	GE	Labor Costs SA QoQ - Q1	--	0.5%	18:00
	UK	Visible Trade Balance GBP/Mn - Apr	-£11100	-£11204	20:30
	UK	Trade Balance Non EU GBP/Mn - Apr	-£3200	-£3114	20:30

Continued on following page

DATA EVENT CALENDAR

DATE	COUNTRY	DATA / EVENT	MKT.	LAST	NZ TIME
9-Jun	UK	Trade Balance - Apr	-£3700	-£3830	20:30
10-Jun	US	Initial Jobless Claims - 4-Jun	270k	267k	00:30
	US	Continuing Claims - 28-May	2171k	2172k	00:30
	US	Wholesale Inventories MoM - Apr	0.1%	0.1%	02:00
	US	Wholesale Trade Sales MoM - Apr	1.1%	0.7%	02:00
	NZ	Card Spending Retail MoM - May	0.5%	0.9%	10:45
	NZ	Card Spending Total MoM - May	--	1.5%	10:45
	NZ	ANZ Inflation Gauge - May	--	0.1%	13:00
	GE	Wholesale Price Index MoM - May	--	0.3%	18:00
	GE	Wholesale Price Index YoY - May	--	-2.7%	18:00
	GE	CPI MoM - May F	0.3%	0.3%	18:00
	GE	CPI YoY - May F	0.1%	0.1%	18:00
	GE	CPI EU Harmonized MoM - May F	0.4%	0.4%	18:00
	GE	CPI EU Harmonized YoY - May F	0.0%	0.0%	18:00
	UK	Construction Output SA MoM - Apr	1.4%	-3.6%	20:30
	UK	Construction Output SA YoY - Apr	-4.8%	-4.5%	20:30
	UK	BoE/TNS Inflation Next 12 Mths - May	--	1.8%	20:30
	NZ	REINZ House Sales YoY - May	--	18.4%	10-14 Jun
	CH	Money Supply M0 YoY - May	6.3%	6.0%	10-15 Jun
	CH	Money Supply M1 YoY - May	21.9%	22.9%	10-15 Jun
	CH	Aggregate Financing CNY - May	1000.0B	751.0B	10-15 Jun
	CH	New Yuan Loans CNY - May	750.0B	555.6B	10-15 Jun
	CH	Money Supply M2 YoY - May	12.5%	12.8%	10-15 Jun
11-Jun	US	U. of Mich. Sentiment - Jun P	94	94.7	02:00
	US	Monthly Budget Statement - May	-$56.0B	--	06:00

Key: AU: Australia, EC: Eurozone, GE: Germany, JN: Japan, NZ: New Zealand, UK: United Kingdom, US: United States, CH: China.
Source: Dow Jones, Reuters, Bloomberg, ANZ Bank New Zealand Limited. All $ values in local currency
Note: All surveys are preliminary and subject to change

LOCAL DATA WATCH

Domestic economic momentum is reasonable at present. However, downside risks exist (mainly from offshore). We believe the RBNZ will cut the OCR twice more, with the next cut pencilled in for August.

DATE	DATA/EVENT	ECONOMIC SIGNAL	COMMENT
Wed 8 Jun (10:45am)	Economic Survey of Manufacturing – Q1	Mixed	Primary volumes may be weaker, but a decent result from core is likely – as signalled by PMI data.
Thu 9 Jun (9:00am)	RBNZ *Monetary Policy Statement*	On hold	We don't think the economy needs further interest rate support right now. However, a clear easing bias will be retained.
Fri 10 Jun (10:45am)	Electronic Card Transactions – May	Respectable	A number of support factors for consumer spending remain, which should keep the underlying pace respectable overall.
Fri 10 Jun (1:00pm)	ANZ Monthly Inflation Gauge – May	--	--
13-17 Jun	REINZ Housing Market statistics – May	Booming	Strength in the regions is being joined by a sharp recovery in Auckland activity. National house price growth is rising again.
Tue 14 Jun (10:45am)	Food Price Index – May	Small lift	A small lift is possible, led by a seasonal gain in fruit and vegetable prices.
Wed 15 Jun (10:45am)	Balance of Payments – Q1	Slightly wider	Courtesy of deterioration in the goods balance, we expect the annual current account deficit to widen slightly.
Thu 16 Jun (early am)	GlobalDairyTrade Auction	Up off lows, but still low	Prices have lifted off lows, but we still do not believe the fundamental backdrop is conducive to a meaningful recovery.
Thu 16 Jun (10:45am)	GDP – Q1	Not bad	We have pencilled in a 0.7% q/q lift. While this is modestly below the pace of growth over H2 2015, it is still decent.
Fri 17 Jun (10:30am)	BNZ-Business NZ PMI – May	Holding up	Despite the pressures on manufacturing globally, the domestic sector continues to perform well.
Fri 17 Jun (1:00pm)	ANZ-Roy Morgan Consumer Confidence – Jun	--	--
Mon 20 Jun (10:30am)	BNZ-Business NZ PSI – May	Still solid	Like a number of other indicators, we expect this to reinforce a reasonable picture for the economy overall.
Wed 22 Jun (10:45am)	International Travel & Migration – May	Steady and strong	Recent data has hinted that a top is in place. However, the net inflow overall looks set to remain large for some time yet.
Thu 23 Jun (10:00am)	ANZ Job Ads – May	--	--
Mon 27 Jun (10:45am)	Overseas Merchandise Trade – May	Small surplus	A small monthly surplus is possible, although rising oil prices are likely to start having an impact.
Thu 30 Jun (10:45am)	Building Consents Issued – May	Still trending higher	We expect issuance to trend higher, although we are wary that capacity issues are capping the upside.
Thu 30 Jun (1:00pm)	ANZ Business Outlook – Jun	--	--
Thu 30 Jun (3:00pm)	RBNZ Credit Aggregates – May	Strong	Household credit growth is running at its fastest pace since 2008. We don't see it rising much further, but it should remain strong.
Tue 5 Jul (10:00am)	NZIER QSBO – Q2	Bouncing back	Following the signals from our Business Outlook, confidence is likely to have lifted. We will be on the lookout for further signs of increased capacity pressures.
Tue 5 Jul (10:00am)	Government Financial Statements – May	In reasonable shape	Timing of tax payments is having some influence, but we suspect the numbers will look decent overall.
Tue 5 Jul (1:00pm)	ANZ Commodity Price Index – Jun	--	--
Thu 7 Jul (10:00am)	ANZ Truckometer – Jun	--	--
On balance		**Data watch**	**Reasonable momentum at present, but with risks. Inflation remains low.**

KEY FORECASTS AND RATES

	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18
GDP (% qoq)	0.9	**0.7**	**0.7**	**0.6**	**0.6**	**0.6**	**0.7**	**0.7**	**0.7**	**0.7**
GDP (% yoy)	2.3	**2.8**	**3.1**	**2.8**	**2.5**	**2.4**	**2.4**	**2.5**	**2.6**	**2.7**
CPI (% qoq)	-0.5	0.2	**0.4**	**0.4**	**0.0**	**0.6**	**0.4**	**0.7**	**0.3**	**0.6**
CPI (% yoy)	0.1	0.4	**0.4**	**0.5**	**1.0**	**1.4**	**1.4**	**1.7**	**1.9**	**1.9**
Employment (% qoq)	1.0	1.2	**0.6**	**0.5**	**0.4**	**0.4**	**0.4**	**0.4**	**0.4**	**0.4**
Employment (% yoy)	1.4	2.0	**2.3**	**3.3**	**2.7**	**1.9**	**1.7**	**1.6**	**1.6**	**1.6**
Unemployment Rate (% sa)	5.4	5.7	**5.5**	**5.4**	**5.4**	**5.3**	**5.2**	**5.2**	**5.1**	**5.0**
Current Account (% GDP)	-3.0	**-3.0**	**-3.0**	**-3.4**	**-3.7**	**-4.3**	**-4.4**	**-4.3**	**-4.1**	**-3.8**
Terms of Trade (% qoq)	-2.0	4.4	**-5.8**	**-2.7**	**-0.3**	**0.8**	**1.7**	**2.8**	**1.7**	**0.8**
Terms of Trade (% yoy)	-3.2	-0.1	**-7.3**	**-6.2**	**-4.6**	**-7.9**	**-0.6**	**5.1**	**7.2**	**7.2**

	Aug-15	Sep-15	Oct-15	Nov-15	Dec-15	Jan-16	Feb-16	Mar-16	Apr-16	May-16
Retail ECT (% mom)	0.5	0.9	0.1	0.7	0.2	0.3	0.7	0.1	0.9	--
Retail ECT (% yoy)	4.2	6.1	5.8	4.6	6.6	5.2	9.2	6.2	7.8	--
Credit Card Billings (% mom)	1.5	-2.0	1.7	0.7	-0.7	1.8	-0.5	-1.4	2.5	--
Credit Card Billings (% yoy)	10.4	7.3	7.8	8.5	7.4	8.2	7.3	4.8	9.1	--
Car Registrations (% mom)	-2.3	0.1	-1.2	-2.0	3.1	-2.8	5.8	-3.7	6.1	-3.1
Car Registrations (% yoy)	7.8	5.0	3.8	1.3	2.4	-1.1	7.4	-0.2	8.7	4.2
Building Consents (% mom)	-7.4	-4.7	5.0	1.7	2.7	-8.4	10.4	-9.7	6.6	--
Building Consents (% yoy)	11.2	17.5	14.7	7.2	17.7	4.9	26.7	0.7	12.7	--
REINZ House Price Index (% yoy)	17.3	20.1	14.1	12.5	12.6	10.7	11.9	13.3	14.5	--
Household Lending Growth (% mom)	0.6	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.8	--
Household Lending Growth (% yoy)	6.3	6.7	6.9	7.2	7.4	7.5	7.6	7.7	7.9	--
ANZ Roy Morgan Consumer Conf.	109.8	110.8	114.9	122.7	118.7	121.4	119.7	118.0	120.0	116.2
ANZ Business Confidence	-29.1	-18.9	10.5	14.6	23.0	..	7.1	3.2	6.2	11.3
ANZ Own Activity Outlook	12.2	16.7	23.7	32.0	34.4	..	25.5	29.4	32.1	30.4
Trade Balance ($m)	-1090	-1140	-905	-795	-42	12	366	189	292	--
Trade Bal ($m ann)	52446	52287	52101	52648	52510	52764	52834	52604	52662	--
ANZ World Commodity Price Index (% mom)	-5.3	5.6	7.1	-5.6	-1.8	-2.3	0.5	-1.3	-0.8	1.0
ANZ World Comm. Price Index (% yoy)	-23.6	-18.2	-11.6	-15.3	-12.9	-14.7	-17.8	-22.4	-16.8	-11.7
Net Migration (sa)	5490	5570	6130	6200	5540	6090	6010	5330	5520	--
Net Migration (ann)	60290	61234	62477	63659	64930	65911	67391	67619	68110	--
ANZ Heavy Traffic Index (% mom)	-0.4	1.8	1.0	0.2	2.9	-4.3	1.7	3.3	-2.6	-1.7
ANZ Light Traffic Index (% mom)	-0.5	2.7	-0.4	0.3	0.9	-1.4	2.7	0.6	-0.1	-1.3

Figures in bold are forecasts. mom: Month-on-Month qoq: Quarter-on-Quarter yoy: Year-on-Year

KEY FORECASTS AND RATES

	ACTUAL			FORECAST (END MONTH)						
FX RATES	Apr-16	May-16	Today	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17
NZD/USD	0.698	0.673	0.691	0.66	0.66	0.63	0.61	0.61	0.63	0.66
NZD/AUD	0.918	0.929	0.937	0.89	0.92	0.94	0.92	0.92	0.93	0.94
NZD/EUR	0.609	0.604	0.608	0.60	0.61	0.58	0.54	0.53	0.53	0.55
NZD/JPY	74.31	74.79	74.26	69.3	69.3	66.2	61.0	61.0	63.0	66.0
NZD/GBP	0.477	0.461	0.478	0.46	0.44	0.41	0.39	0.38	0.39	0.40
NZ$ TWI	72.2	71.3	73.8	69.3	69.8	67.5	64.5	64.0	64.8	67.4
INTEREST RATES	Apr-16	May-16	Today	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17
NZ OCR	2.25	2.25	2.25	2.25	2.00	2.00	1.75	1.75	1.75	1.75
NZ 90 day bill	2.40	2.42	2.37	2.40	2.20	2.10	2.00	2.00	2.00	2.00
NZ 10-yr bond	2.85	2.62	2.60	2.80	2.90	2.90	3.10	3.20	3.40	3.50
US Fed funds	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.25	1.25	1.50
US 3-mth	0.64	0.67	0.68	0.83	0.83	1.08	1.08	1.33	1.33	1.58
AU Cash Rate	2.00	1.75	1.75	1.75	1.50	1.50	1.50	1.50	1.50	1.50
AU 3-mth	2.15	1.99	1.99	2.00	1.80	1.80	1.80	1.80	1.80	1.80

	3 May	30 May	31 May	1 Jun	2 Jun	3 Jun
Official Cash Rate	2.25	2.25	2.25	2.25	2.25	2.25
90 day bank bill	2.38	2.41	2.42	2.43	2.42	2.40
NZGB 12/17	2.15	2.10	2.11	2.12	2.10	2.08
NZGB 03/19	2.24	2.13	2.14	2.16	2.14	2.13
NZGB 04/23	2.73	2.43	2.45	2.50	2.48	2.46
NZGB 04/27	2.88	2.58	2.60	2.65	2.64	2.62
2 year swap	2.30	2.31	2.33	2.33	2.31	2.30
5 year swap	2.47	2.41	2.43	2.42	2.40	2.37
RBNZ TWI	73.7	72.38	72.58	73.19	73.52	73.63
NZD/USD	0.70	0.67	0.67	0.68	0.68	0.68
NZD/AUD	0.91	0.93	0.93	0.93	0.94	0.94
NZD/JPY	74.85	74.34	74.83	75.08	74.41	74.19
NZD/GBP	0.48	0.46	0.46	0.47	0.47	0.47
NZD/EUR	0.61	0.60	0.60	0.61	0.61	0.61
AUD/USD	0.77	0.72	0.72	0.73	0.72	0.72
EUR/USD	1.15	1.11	1.11	1.11	1.12	1.12
USD/JPY	106.20	111.14	111.20	110.66	109.06	108.61
GBP/USD	1.47	1.46	1.47	1.45	1.44	1.44
Oil (US$/bbl)	44.75	49.36	49.36	49.10	49.07	49.14
Gold (US$/oz)	1293.15	1202.50	1213.20	1215.35	1215.07	1211.90
Electricity (Haywards)	6.69	5.91	6.49	6.54	17.46	7.14
Baltic Dry Freight Index	682	--	612	612	606	610
Milk futures (USD)	44	--	50	49	50	49

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