

All eyes on Winston and Thursday

- The special votes saw Greens and Labour win a seat each at the expense of National, but the final coalition remains unclear.
- Market participants (and the rest of NZ) are eagerly awaiting Winston's decision, which is expected on Thursday.
- ASB Economics has revamped its commodity index to highlight the growing importance of NZ's fruit exports.

The special votes have been tallied and the vote is finalised. Ultimately, however, not much has changed as we still do not know what shape the next NZ Government will take (and Winston Peters remains firmly in the driver's seat). With the largest number of special votes cast this year than ever before (in fact there were 446,287 special votes compared to initial estimates of around 380,000), the chances that we would see a reshuffle in the distribution of seats were high.

Special votes have historically favoured the left as the proportion of young votes is higher (university students who are still enrolled at Mum and Dad's or twenty-something's on their OE's). And indeed, this was the case again this year. This year's special votes **saw both the Green Party and Labour gain an extra seat, while National lost two seats.** Although this does reduce the gap between a National-led and a Labour-led coalition, **both coalition options remain viable as each coalition has more than the 61 seats required for a majority in parliament.**

So far, **NZ is operating on the assumption that Winston Peters will make his decision on the 12th of October.** This date also represents the Return of Writ and when the list of MPs is finalised. It could be a **rocky road for NZ financial markets as we head towards Thursday, with a particular risk of volatility if coalition talks end up being extended.** We also see more risk of financial market volatility if a Labour/Greens/NZ First coalition was successful, simply because there is more uncertainty associated with a Labour-led government (including markets being less familiar with the people and policies).

Thursday is shaping up to be the big day this week, as we also have the US Federal Reserve's meeting minutes released on Thursday morning. This follows Friday's shock Non-farm Payrolls release for September for which the number of persons employed plummeted by 33,000, the first fall since 2010. However, there were some bright spots, including an acceleration in wage pressures. The lift in wages has added to expectations that the Fed will raise interest rates in December (market pricing is now around 80%) and market participants will be looking to the Fed minutes to reinforce this view. The minutes that will also be closely analysed for any further comments referencing the Fed's decision to begin unwinding the balance sheet in October.

Last week, we released a revamp of the [ASB New Zealand Commodities Index](#). Notably we have added the growing presence of fruit exports to the Index, which have a 6% weight in the new index. Dairy's weight has also increased to 43%. With this refresh and the weekly reporting basis, we believe that the updated Index provides New Zealand's most timely and relevant commodity price measure.

Foreign Exchange

- NZD a tad lower than last week versus all major bilaterals, except for the Pound.

Interest Rates

- NZ interest rates have been broadly steady over the past week.

Week Ahead

- Electronic cards, food price index and consumer confidence.

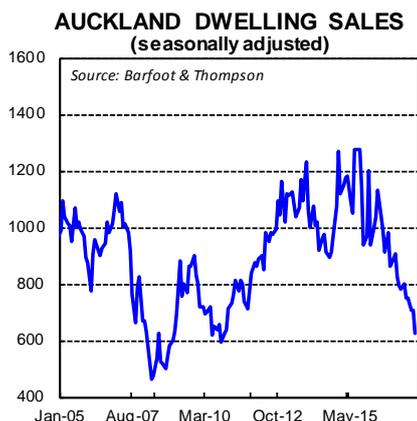
Week in Review

- Business confidence fell over Q3 and dairy prices eased at the GlobalDairyTrade auction last week.

Global Calendars

- RBA financial stability review, US CPI and US Fed meeting minutes are due out this week.

Chart of the Week: Election-related uncertainty widespread



September data so far suggest that, as we thought, there has been a dip in activity as people delay investment decisions until they know who will be in government. Last week's Barfoot & Thompson house sales data showed the housing market was the latest example.

Seasonally-adjusted house sales fell by 11.5% mom in September with just 627 house sales over the month. This is the lowest number of monthly house sales in Auckland since October 2010. But it wasn't only housing data reflecting the impact of uncertainty on the economy last week. **NZIER's Quarterly Survey of Business Opinion showed business confidence tumbled in Q3 as election anxiety increased.**

With heightened uncertainty weighing on activity, the **outlook for Q3 GDP growth is somewhat subdued.** But in saying this, these soft readings **do not reflect any fundamental weakness in the economy and we expect activity will be quick to recover once a government has been formed.**

Foreign Exchange Market

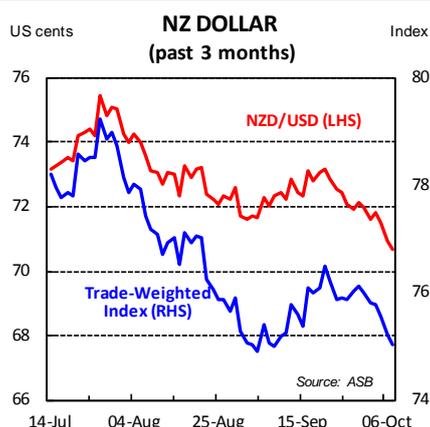
FX Rates	Current*	Week ago	Month ago	6 mths ago	Year ago	ST Bias	Support^	Resistance^
NZD/USD	0.7069	0.7198	0.7232	0.6936	0.7130	FLAT/DOWN	0.695	0.715
NZD/AUD	0.9093	0.9198	0.8986	0.9265	0.9409	FLAT/DOWN	0.9000	0.9200
NZD/JPY	79.59	81.20	78.36	77.27	74.00	FLAT/DOWN	79.0	81.0
NZD/EUR	0.6067	0.6111	0.6016	0.6552	0.6414	FLAT/DOWN	0.5950	0.6100
NZD/GBP	0.5399	0.5383	0.5521	0.5599	0.5736	FLAT	0.5300	0.5500
TWI	75.0	76.0	75.0	75.9	76.3	FLAT/DOWN	74.25	76.25

^Weekly support and resistance levels * Current is as at 9.30 am Monday; week ago as at Monday 5pm.

The NZD TWI starts the week about 1½% lower than at the end of last week, and is lower against most major NZD bilaterals, with the exception of the GBP. **Politics, rather than the tone of data look to be the key driver**, with Brexit-related concerns weighing on the GBP and with currency markets largely shrugging off the weak September US payrolls headline number and focusing on the solid underlying details in the US labour market figures, including falls to the unemployment rate and strengthening labour earnings growth. The NZD has fallen roughly 2% to just over 76.5 US cents since early last week and dipped following the release of the final NZ vote count on Saturday, which saw odds of a more left-leaning government increase as Labour (46 seats) and the Greens (8) both picked up a seat at the expense of the National Party (56).

With little in the way of key data this week aside from the US CPI (Sat) and the Fed Minutes (Thu), **Thursday's scheduled announcement of the shape of the new government by the NZ First party (9 seats) is looming as a binary event for the kiwi**, given that either a left or right-leaning government is feasible. As of last week market positioning had been long euro, marginally long NZD, and short USD, suggesting the risk of larger NZD moves (falls) if a left-leaning government is announced.

Short-term outlook:



Key data

Key data	Date	Time (NZT)	Market
NZ ECT, Sep, %m/m	10/10	10:45am	+0.7%
US FOMC Minutes	12/10	07:00am	-
NZ Return of writ	12/10	-	-
US CPI, Sep – y/y	14/10	1:30am	+2.3%

NZD: Sep ECT (Tue), Sep REINZ house prices (Tue), Sep food prices (Thu), Sep ANZ consumer confidence (Thu), return of writ (Thu), Sep manufacturing PMI (Fri). **USD:** FOMC Minutes (Thu), Sep CPI (Sat), Sep retail sales (Sat), **EUR:** Aug industrial production (Thu). **GBP:** Aug industrial production (Tue), Aug trade balance (Tue). **CAD:** Sep manufacturing PMI (Tue). **JP:** Aug current account (Tue), Aug machinery orders (Wed). **AUD:** Sep NAB business confidence (Wed), RBA FSR (Fri).

Speakers: **FOMC:** Kaplan (Wed), Evans (Thu), Brainard (Fri), Powell (Fri, Sat). **RBA:** Debelle (Tue). **BoC:** Wilkins (Wed, Fri). **ECB:** Praet (Thu, Fri), Draghi (Fri), Coeure (Fri). **BOJ:** Kuroda (Tue).

Medium-term outlook:

Last Quarterly Economic Forecasts

We updated our FX forecasts in early September. The NZD still remains the recipient of some key supports - including the near record Terms of Trade, relatively high interest rates and a solid domestic outlook – which are expected to support NZD TWI consolidation around current levels over the forecast period. **While there is a temporary and modest political risk to our NZD forecast in the short term, these fundamental factors are expected to keep the NZD elevated over the forecast horizon.**

Our forecasts also incorporate a weaker USD. Further USD falls are expected given the upward bias in non-USD rates, fiscal policy inaction by the Trump Administration (delays to pending tax rate cuts), and with the strengthening synchronised global economy typically bullish for commodity currencies like the NZD and AUD. We have increased our near-term NZD/USD forecasts modestly to reflect a weaker USD. We expect the NZD/USD to end 2017 at 0.74 and 2018 at 0.77. **The narrowing Australian current account deficit, and the strengthening trading partner growth should eventually pressure the NZD/AUD lower** and we expect the NZD/AUD to ease from 0.93 by the end of 2017 to 0.91 by late 2018.

Supportive growth prospects, signals of pending tapering by the ECB before the end of the year and prospective ECB rate hikes next year will support the euro. **We expect NZD/EUR to end 2017 at 0.60 and 2018 at 0.61.** With EU-UK Brexit negotiations weighing on the UK economic outlook, the NZD is expected to remain elevated against the GBP. We expect the NZD/GBP to remain in a 0.56-0.57 range till the end of 2018. **We expect the NZD/JPY to hover around the 79/80 level over the next couple of years.** The large Japanese current account surplus and low US Treasury yields, and no indication of further easing by the BOJ are expected to support the JPY.

Interest Rate Market

Wholesale interest rates	Current	Week ago	Month ago	6 mths ago	Year ago	ST Bias
Cash rate	1.75	1.75	1.75	1.75	2.00	FLAT
90-day bank bill	1.94	1.96	1.95	1.97	2.18	FLAT
2-year swap	2.22	2.22	2.15	2.28	2.09	FLAT
5-year swap	2.76	2.76	2.58	2.84	2.26	UP
5-year benchmark gov't stock	2.54	2.55	2.37	2.42	2.07	UP
NZSX 50	7992	7929	7816	7244	7151	UP

^Weekly support and resistance levels * Current is as at 9.30am Monday; week ago as at Monday 5pm.

NZ interest rates remained broadly steady, moving within a fairly narrow range over the past week. NZ market participants have been in a **holding pattern waiting for a Government to be formed**, which is likely to be by Thursday this week.

NZ longer-term rates drifted slightly lower on Friday, moving in sympathy with Australian interest rates. Australian rates fell in response to an **unexpected decline in retail sales**, with the previous month's results revised from flat to a contraction in spending. With two consecutive months of contraction and falls being broad-based across major components and all Australian States, the result sent a strong message that spending remains soft despite a pick in the labour market. And that message reinforces the Reserve Bank of Australia (RBA) is likely to remain on hold well into 2018.

In contrast, **US interest rates lifted heading into the weekend.** While the headline employment figures were weak due to hurricane disruption, the **underlying detail and wage figures were stronger than expected.** This reinforced the upward trend in the US economy and has seen market participants pricing in a higher probability of a Fed rate hike in December. **However, US longer-term rates remained capped as US-North Korea tensions remain high.**

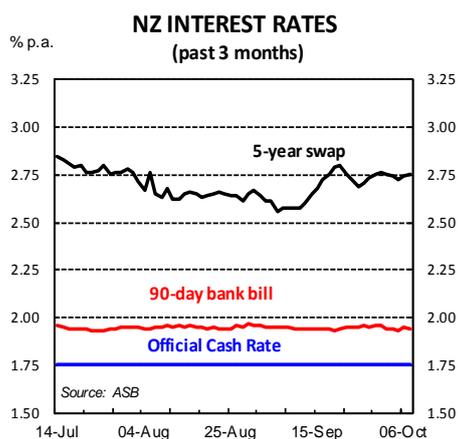
Short-term outlook:

Key data

Date

Time (NZT)

Market



NZ Electronic Card Spending, Sep %mom	10/10	10.45 am	0.7
US FOMC Meeting Minutes	12/10	7.00 am	-
NZ Election Results: Return of writ & Winston Peter's self-imposed coalition deadline	12/10	-	-
US CPI, September, Headline, %yoy	14/10	1:30am	+2.3%

Comment: The key event for local markets is the **expectation that a coalition agreement will be made and a Government formed**, after over 2 weeks of uncertainty since the General Election. Either National or a Labour-Green bloc can form a Government with NZ First, with the power now in Winston Peter's hands.

Offshore, the key event will be the US Federal Reserve meeting minutes which will likely reinforce the likelihood of a US Fed Funds hike in December and provide support to US interest rates. In Australia, there are some minor releases due and also the RBA Financial Stability Review on Friday.

Medium-term outlook:

Last Quarterly Economic Forecasts

The RBNZ continued to hold the OCR at its record-low of 1.75% at September OCR Review. The RBNZ retained its neutral bias and continued to note the numerous uncertainties. However, the key surprise was the **RBNZ downgraded its growth outlook**, commenting it expected growth to "maintain its current pace" whereas at the August Monetary Policy Statement (MPS), the RBNZ's forecasts assumed growth would accelerate. However, the RBNZ will be mindful that **election promises will likely boost growth further once the RBNZ has revised fiscal projections from Treasury.** Furthermore, we have for some time seen upside risks to the RBNZ's growth forecasts due to the RBNZ's relatively modest dairy price assumption.

The NZD had eased since August, when the RBNZ had been very frustrated. Nonetheless, the RBNZ continues to note that a lower NZD would be helpful in delivering more inflation and a more 'balanced' growth outlook.

The RBNZ remains confident in the medium-term inflation outlook, despite anticipated volatility in headline inflation this year. The RBNZ's August MPS forecasts show the RBNZ expects inflation will dip below 1% (due to volatility in fuel and food) before swiftly recovering to reach 2% by 2018. The RBNZ appears to be relying on a very swift pick-up in non-tradable inflation. This is a fairly bold assumption given the RBNZ is wary that price-setting behaviours have become more backward looking. Nonetheless, we expect the RBNZ will start lifting the OCR in Q1 2019, which is slightly earlier than the RBNZ's expectations for a hike in Q3 2019.

Key international data for the week ahead

Data	Date	Time (NZT)	Previous	Market expects	ASB expects
UK Industrial Production, August, %mom	10/10	9.30 pm	0.2	0.2	0.3
Australia WBC/MI Consumer Confidence, October, Index	11/10	12.30 pm	97.9	-	-
US Federal Reserve Meeting Minutes	12/10	7.00 am	-	-	-
Australia Housing Finance, August, Loan Value, %mom	12/10	1.30 pm	2.9	0.5	1.5
Eurozone Industrial Production, August, %mom	12/10	10.00 pm	0.1	0.6	0.3
Reserve Bank of Australia Financial Stability Review	13/10	1.30 pm	-	-	-
US CPI, September, Headline, %yoy	14/10	1.30 am	1.9	2.3	-

Japan's already-released trade balance suggests Japan's **current account surplus** will have stayed large at around JPY 2 trillion in August.

Australia's **consumer confidence** has been below its long-run average for the past year. Soft wages growth and elevated underemployment are weighing on sentiment. This year's run of strong employment growth should help boost confidence.

We expect a small increase in **Australia's dwelling commencements** after the weather-related fall in Q1. Annual commencements are running at 223k. Annual population growth is 389k.

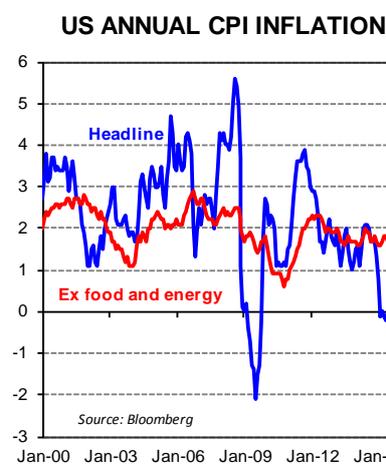
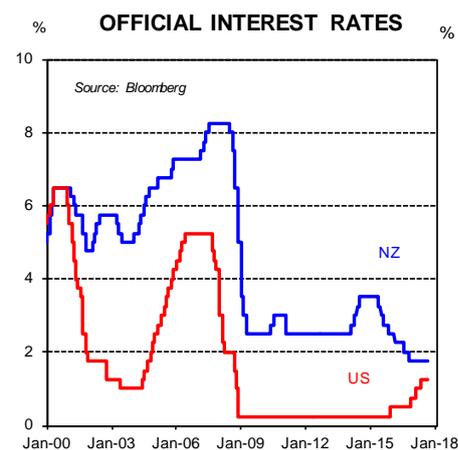
With regards to **Australia's housing finance**, lending to owner-occupiers has trended higher over the past year. However, lending to investors is slowing partly due to recent interest rate increases on investor and interest-only loans.

The **Reserve Bank of Australia's Financial Stability Review** will provide an update on potential risks to financial stability. Developments in the housing market are likely to be the main focus, given higher household debt-to-income ratios. However, the RBA may be a little more comfortable now that the share of interest-only loans is decreasing.

Recently-released manufacturing PMI data point to further decent growth in both the **Eurozone and the UK's industrial production**.

The **Federal Open Market Committee's meeting minutes** will shed light on the US Fed's discussion about the pace of future tightening and balance sheet reduction.

The **US CPI** may temporarily lift in September, reflecting shortages on account of the disruption caused by the hurricanes. After abstracting the volatility out, inflation pressures in the US remain soft.



NZ Data Preview: a look at the week ahead

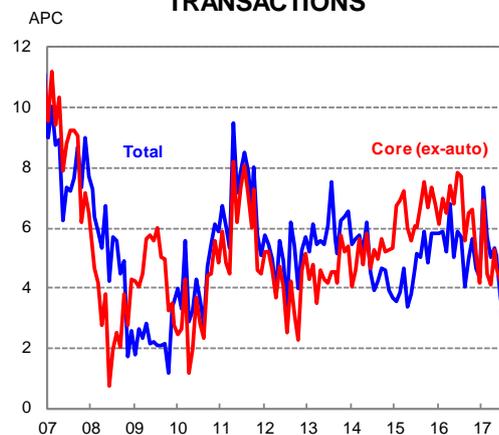
Data	Date	Time (NZT)	Previous	Market expects	ASB expects
Electronic Card Transactions, September, Total, %mom	10/10	10:45am	-0.2	0.7	0.8
Food Price Index, September, Total, %mom	12/10	10:45am	+0.6	-	-1.0
Consumer confidence, October	12/10	1:00pm	129.9	-	-

Electronic Card Spending has been soft over recent months. For September, we expect spending growth to rebound, especially as petrol prices lifted over the month. In addition, we expect core spending growth to lift to a moderate rate following last month's fall. **All up, we expect total card spending to rise 0.8% over the month, while core spending may rise by around 0.3%.**

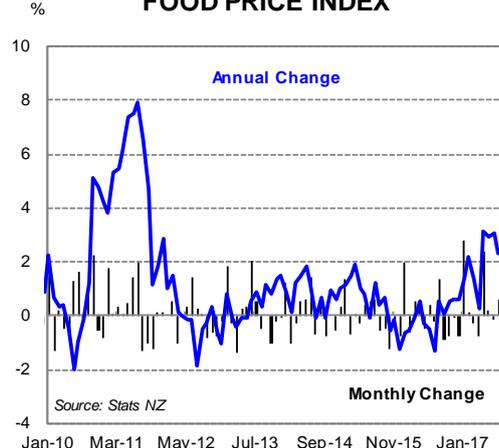
We are expecting food prices to dip by 1.0% mom in September. We expect the price pressures from this year's high levels of rainfall to have eased slightly over Q3. However, sharp increases in milk fat prices will support overall food price inflation. We will finalise our Q3 CPI forecast shortly after the release, but our preliminary forecast is for inflation to lift slightly to 1.8% yoy.

Headline ANZ/Roy Morgan consumer confidence surprisingly lifted in September, despite the uncertainty around the election. The September reading was the highest since July 2014. The index will likely fall in October, with the election result effectively 'up in the air' until coalition negotiations are completed sometime later in the month. Further out, **with the strengthening labour market and rural incomes improving, consumer sentiment is likely to remain broadly firm.**

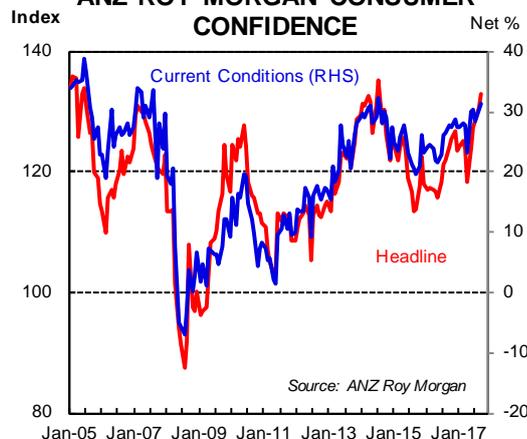
RETAIL ELECTRONIC CARD TRANSACTIONS



FOOD PRICE INDEX



ANZ ROY MORGAN CONSUMER CONFIDENCE

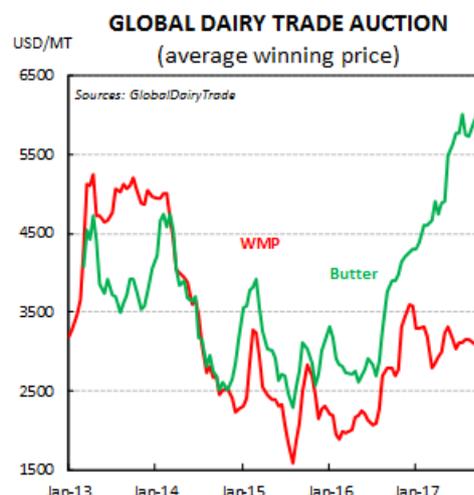
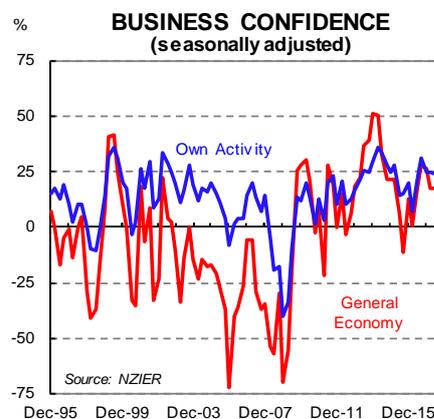


Data Recap: weekly recap

Data	Date	Actual	Market forecast	ASB Forecast
NZIER QSBO, Business Confidence (Q3) s.a.)	03/10	6.7	-	5
GlobalDairyTrade auction, whole milk powder, % change	03/10	-2.7	-	+2 to +4

General business confidence fell in Q3, as expected, due to the increased uncertainty of the 2017 General Election outcome in September. However, expectations for own-activity actually increased, while employment and investment intentions also held up at relatively high levels. The latter measures, rather than general business confidence, tend to correlate better with GDP growth. **Businesses' continued confidence in their own outlook suggests growth is likely to pick up once the election uncertainty has passed.** In saying that, the **QSBO has over-predicted economic growth over the past year**, while the ANZ monthly business outlook survey has been a better guide and is not quite as optimistic as the QSBO.

Overall dairy auction prices eased modestly at last week's auction, with the GDT Price index down 2.4% on the previous event. The result is in contrast to recent futures pricing, which pointed to gains. NZ production was weak over August as the impact of very wet weather has been starting to slow spring production. We are continuing to keep an eye on the wet NZ spring that has been saturating most of the country including the key dairy regions. As long as the wet spring weather continues, it creates the risks that prices spike higher over coming months, if production at this important time of the year is impacted. **Despite the dip in prices overnight, we see potential for overall prices, particularly for WMP, to push higher over coming months.** Firstly, NZ weather has been poor (very wet) and production is reportedly back on last season in key regions at this juncture. Secondly, global milk fat (butter) demand continues to surge, while supply struggles to keep pace.



Global Data Calendars

Calendar - Australasia, Japan and China

Date	Time (NZT)	Eco	Event	Period	Unit	Last	Forecast	
							Market	ASB
Mon 9 Oct	14:45	CH	Caixin China PMI composite	Sep	Index	52.4	~	~
Tue 10 Oct	10:45	NZ	Electronic Card Transactions	Sep	m%ch	-0.2	0.7	0.8
	11:30	AU	ANZ Roy Morgan Weekly Consumer	Oct	Index	113.4	~	~
	12:14	NZ	REINZ house sales	Sep	y%ch	-20.0	~	~
	12:50	JN	BoP current account adjusted	Aug	¥bn	2032.9	~	~
	13:30	AU	NAB business conditions	Sep	~	15.0	~	~
	16:20	AU	RBA's Debelle speaks on FX code of conduct					
Wed 11 Oct	12:30	AU	WBC consumer confidence	Oct	Index	97.9	~	~
	13:30	AU	Dwelling commencements	Q2	q%ch	-11.4		5.0
Thu 12 Oct	10:45	NZ	Food prices	Sep	m%ch	0.6	~	-1.0
	12:50	JN	PPI	Sep	m%ch	0.0	~	~
	13:00	NZ	ANZ consumer confidence	Oct	Index	129.9	~	~
	13:00	AU	Consumer inflation expectation	Oct	%	3.8	~	~
	13:30	AU	Housing finance - No. of owner-occupiers	Aug	m%ch	2.9	~	0.8
	17:30	JN	Tertiary industry index	Aug	m%ch	0.1	~	~
Fri 13 Oct	~	CH	Trade balance	Sep	CNY bn	286.5	261.8	~
	13:30	AU	RBA Financial Stability Review					

Calendar - North America & Europe

Date	Time (UKT)	Eco	Event	Period	Unit	Last	Forecast	
							Market	ASB
Tue 10 Oct	09:30	UK	Industrial production	Aug	m%ch	0.2	~	0.3
	09:30	UK	Trade balance	Aug	£mn	-2,872	~	~
	13:00	UK	NIESR GDP estimate	Sep	%	0.4	~	~
Wed 11 Oct	15:00	US	Fed's Kashkari speaks at Regional Economic Conference					
	01:00	US	Fed's Kaplan speaks at Stanford Institute					
	12:15	US	Fed's Evans speaks on Economy and Monetary Policy					
	19:00	US	FOMC Meeting Minutes	Sep	~	~	~	~
	19:40	US	Fed's Williams gives Community Leaders speech					
	19:50	EC	ECB's Praet speaks in New York					
Thu 12 Oct	10:00	EC	Industrial production	Aug	m%ch	0.1	~	0.3
	13:30	US	PPI final demand	Sep	m%ch	0.2	0.4	~
	15:15	US	ECB's Draghi, Fed's Brainard speak on Monetary Policy Panel					
	15:30	US	Fed's Powell speaks at IIF Conference in Washington					
Fri 13 Oct	13:30	US	CPI	Sep	m%ch	0.4	0.6	~
	13:30	US	Retail sales advance	Sep	m%ch	-0.2	1.2	~
	13:30	US	Real average hourly earning	Sep	y%ch	0.6	~	~
	15:00	US	Uni. of Michigan Sentiment	Oct P	Index	95.1	95	~
	15:00	US	Business Inventories	Aug	%	0.2	0.4	~

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