bankSA

Morning Report

Thursday, 25 May 2023

Equities (close & % change)		
S&P/ASX 200	7,214	-0.6%
US Dow Jones	32,800	-0.8%
Japan Nikkei	30,683	-0.9%
China Shanghai	3,359	-1.3%
German DAX	15,842	-1.9%
UK FTSE100	7,627	-1.7%
Commodities (close & change)*		
CRB Index	262.7	1.5
Gold	1,957.16	-18.1
Copper	8,068.75	-26.8
Oil (WTI futures)	74.34	1.4
Coal (thermal)	147.60	-12.2
Coal (coking)	232.50	-2.5
Iron Ore	96.25	0.8

Sydney Futures Exchange (last & change)				
	Last		**Overnight Chg**	
10 yr bond	3.68		0.02	
3 yr bond	3.37		0.04	
3 mth bill rate	3.97		0.02	
SPI 200	7,196.0		-31	
FX Last 24 hrs	Open	High	Low	Current
TWI	60.9	-	-	60.9
AUD/USD	0.6611	0.6615	0.6530	0.6544
AUD/JPY	91.59	91.68	90.77	91.18
AUD/GBP	0.5325	0.5327	0.5281	0.5292
AUD/NZD	1.0582	1.0730	1.0568	1.0710
AUD/EUR	0.6137	0.6141	0.6072	0.6086
AUD/CNH	4.6697	4.6787	4.6167	4.6227
USD Index	103.54	103.91	103.35	103.88

Interest rates (close & change)		
Australia		
90 day BBSW	3.92	0.01
2 year bond	3.50	-0.04
3 year bond	3.34	-0.04
3 year swap	3.76	0.02
10 year bond	3.65	0.00
United States		
3-month T Bill	5.19	0.06
2 year bond	4.38	0.06
10 year bond	3.74	0.05
Other (10 year yields)		
Germany	2.47	0.00
Japan	0.41	0.01
UK	4.21	0.06

Data as at 7:45am AEST. Change is from the previous trading day (excluding the SFE, which is the change during the night session). Source: Bloomberg.

Main Themes: Risk sentiment took a hit overnight as limited progress was made on landing a deal to increase the US government debt ceiling. House Speaker McCarthy expressed some optimism on a deal stating, “I still think we have time to get an agreement, and get it done.” US Treasury Secretary Yellen noted that she isn't involved in contingency planning for a potential US default.

US equities are showing increasing signs of concern over the standoff. Investors are demanding higher premiums on bonds that are due to mature given the risk of default. The US dollar edged higher.

In other news, weakness in global equities and commodities prices, coupled with hawkish signals from Fed communications, saw sharp declines in risk sensitive commodity currencies, including the Aussie. The core inflation rate in the UK accelerated, which led to yields on UK gilts increasing sharply to the highs we saw last year when Liz Truss was Prime Minister. The Reserve Bank of New Zealand hiked as expected but signalled the end of the tightening cycle, which saw a sharp fall in the NZ currency.

Share Markets: US share markets closed lower, as investors are showing increasing signs of concern over the US debt ceiling standoff. The S&P 500 dropped 0.7%, the Dow was down 0.8% and the Nasdaq was 0.6% lower.

European markets also closed lower. The FTSE 100 closed 1.8% lower on the back of the higher-than-expected UK inflation read, which saw a sharp jump in UK gilt yields. The German DAX closed 1.9% lower, in part driven by the fall in German business confidence.

The ASX 200 fell for the third consecutive day, closing 0.6% lower. BHP Group contributed the most to the decline, falling by 2.2%. Seven out of eleven sectors that closed lower, led by materials stocks.

Interest Rates: The US 2-year yield lifted 6 basis points to 4.38%. The US 10-year yield also increased by 6 basis points to 3.74%.

Markets are currently attaching a probability of 36% to another rate hike from the US Federal Reserve when they next meet in June.

The 3-year Australian government bond yield (futures) rose 4 basis points, to 3.37%. The 10-year government bond yield (futures) was 2 basis points higher, at 3.68%.

Markets are currently attaching a very low probability of the Reserve Bank (RBA) hiking in June with just a 1% chance of a hike. However, the probability of the RBA hiking by August is sitting at around 50%.

The 2-year UK gilt yield increased to almost 4.40% before settling at 4.35%. This was an increase of almost 30 basis points. Markets have prices in almost 100 basis points of additional hikes by November this year.

Foreign Exchange: Risk-sensitive commodity currencies slid amid weakness in equities and commodities prices.

The AUD/USD pair reached a low of 0.6530, the lowest since mid-November 2022. The pair traded outside the tight range of 0.6600-0.6800 it had held for the last few months. The pair is now trading around 0.6543. However, downside risks remaining given the pull back in risk sentiment. The Canadian dollar also fell against the greenback, declining to a 4-week low of around 0.6585.

The New Zealand dollar was sold off after the RBNZ signalled an end to the hiking cycle – the AUD/NZD pair increased to a high of 1.0709 – the highest level in four weeks. The NZD/USD pair declined by 1.3% to 0.6166, the lowest since May.

The US dollar ended higher on the day on the back of the higher US yields and hawkish message from Fed officials. The DXY Index rose from a low of 103.35 to a high of 103.91, before settling at 103.88.

Commodities: Commodities were generally softer. The price of copper declined to levels not seen since November last year. Gold and coal were both down. Iron ore was broadly unchanged, while the price of oil was slightly higher. The West Texas Intermediate (WTI) crude future rose to US$74.34 per barrel.

Australia: The Westpac - Melbourne Institute Leading Index declined to negative 0.78% in April, from negative 0.69% in March. The Index has recorded below-trend growth for nine consecutive months, indicating the slowdown that started in the December quarter 2022 is likely to extend through to the end of 2023 and into early 2024. The components that show weakness are shifting from financial conditions to the construction and commodity sectors.

New Zealand: The Reserve Bank of New Zealand (RBNZ) raised interest rates by 25 basis points to 5.5% from 5.25%. While the hike was widely expected, the forward guidance surprised the market.

The RBNZ signalled that no further tightening would be needed to bring inflation back to its target level. The RBNZ forecasts showed that the policy rate has now peaked, with cuts beginning in the September quarter of 2024. This led to a selloff in the New Zealand dollar, which saw the NZD/USD pair decline by as much as 1.8% to its lowest since March this year. The yield on policy-sensitive 2-year bonds dropped by almost 30 basis points to 4.77%.

Retail Sales declined by 1.4% over the March quarter, to be 4.1% lower in annual terms. The outcome was lower than the growth of 0.2% the market was expecting. The December quarter outcome was revised to a fall of 1.0%, compared with the initial estimate of a 0.6% fall. Elevated cost of living pressures, subdued confidence and higher interest rates are likely to continue to weigh on household spending.

United Kingdom: The Consumer Price Index increased by 8.7% in annual terms to the month of April. The outcome was stronger than the 8.2% the market was expecting. The deceleration in inflation from thew 10.1% recorded in March was mainly driven by a sharp slowdown in electricity and gas prices. The core inflation rate, which excludes food and energy, accelerated from 6.2% to increase by 6.8% in annual terms. This was well above the 6.2% the market was expecting. This core inflation read was the highest since March 1992.

Following the release of the inflation read, the Pound rose and the market quickly moved to price in further rate increases.

The Confederation of British Industry Manufacturing orders edged higher to -17 in May from -20 in April. Expected average selling price over the next three months fell to +21 in May from +23 in April, signalling manufacturers expect to raise prices at the smallest rate. The read suggests that demand remains subdued wile inflationary pressures remain elevated, with some signs of easing.

The national house price index declined by 1.2% over the month of March but was 4.1% higher in annual terms. This represents a step down from the growth of 5.8% recorded over the year to February.

United States: Minutes from the Fed Policy Committee's May meeting show that members were divided on whether further rate hikes would be needed to lower inflation. The Minutes note that "several participants noted that if the economy evolved along the lines of their current outlooks, then further policy firming after this meeting may not be necessary." The Minutes show that the Fed will retain its data dependent approach with members commenting "that progress in returning inflation to 2% could continue to be unacceptably slow" as such "additional policy firming would likely be warranted at future meetings."

Christopher Waller, member of the Fed's Board of

Governors, said incoming data would help determine whether to pause or hike next month. He noted that it's premature to declare tightening over stating that he "does not support stopping rate hikes unless we get clear evidence that inflation is moving down towards our 2% objective".

As negotiations to raise the US debt ceiling continue, Janet Yellen, US Treasury Secretary, warned that signs of market stress are emerging as the Government moves closer to running out of cash. Yellen also noted that she isn't involved in contingency planning with banks for a default.

Today's key data and events:

US GDP Annualised Q1 Est. 2 prev 1.1% (10:30pm)

US Chicago Fed Act. Index Apr prev -0.19 (10:30pm)

US Pending Home Sales Apr exp -5.2% (12am)

US Kansas City Fed Index May prev -10 (1am)

Times are AEST. All data forecasts are m/m or q/q and seasonally adjusted unless otherwise specified. Forecasts for Australian data are our forecasts and for other countries they are consensus forecasts.

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