Morning Report

Wednesday, 11 October 2023

Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	7,041	1.0%			**Last**		**Overnight Chg**	**Australia**		
US Dow Jones	33,739	0.4%	10 yr bond		4.44		-0.03	90 day BBSW	4.14	0.00
Japan Nikkei	31,747	2.4%	3 yr bond		3.92		-0.01	2 year bond	3.95	-0.03
China Shanghai	3,224	-0.7%	3 mth bill rate		4.22		0.02	3 year bond	3.92	-0.03
German DAX	15,424	2.0%	SPI 200		7,102.0		30	3 year swap	4.14	0.02
UK FTSE100	7,628	1.8%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	4.46	-0.06
Commodities (close & change)			TWI	60.1	-	-	60.1	**United States**		
CRB Index	279.9	-0.2	AUD/USD	0.6411	0.6433	0.6390	0.6432	3-month T Bill	5.31	-0.04
Gold	1,860.53	-0.9	AUD/JPY	95.21	95.66	95.14	95.65	2 year bond	4.97	-0.11
Copper	8,050.75	65.5	AUD/GBP	0.5238	0.5250	0.5220	0.5235	10 year bond	4.65	-0.15
Oil (WTI futures)	85.88	-0.5	AUD/NZD	1.0645	1.0669	1.0633	1.0638	**Other (10 year yields)**		
Coal (thermal)	148.35	2.5	AUD/EUR	0.6069	0.6081	0.6040	0.6065	Germany	2.78	0.00
Coal (coking)	344.50	-7.5	AUD/CNH	4.6757	4.6868	4.6645	4.6862	Japan	0.78	-0.02
Iron Ore	111.50	0.7	USD Index	106.07	106.25	105.66	105.77	UK	4.43	-0.05

Data as at 8:00am AEST. Change is from the previous trading day (excluding the SFE, which is the change during the night session). Source: Bloomberg.

Main Themes: Market movements were more muted and risk sentiment improved in a session with little in the way of major economic data to drive direction. Additional dovish Fed speak added to expectations that the Federal Reserve may be done in its hiking cycle, supporting sentiment.

US bond yields plunged as the physical market resumed trading after a public holiday. The US dollar pulled back against a basket of major currencies, and equity markets ended higher.

Share Markets: Equity markets ended in the green across the board as comments from numerous Fed members added to expectations that the Fed may be done hiking. Interest rates also declined. This helped to support equity valuations and risk sentiment. The S&P 500 closed 0.5% higher, the Nasdaq gained 0.6%, and the Dow Jones was up 0.4%.

The ASX 200 jumped 1.0% yesterday. All 11 sectors ended higher, led by utilities, IT, and communication services – which surged by over 2% each on the day. Futures are pointing to a positive open today, taking the lead from overseas markets.

Interest Rates: Physical US bonds resumed trading after the Columbus Day public holiday. Yields plunged, reflecting the risk-averse tone in markets due to the conflict between Israel and Hamas and taking the lead from futures prices. The 2-year treasury yield fell 11 basis points, to 4.97%, while the 10-year yield dropped 15 basis points, to 4.65%. Markets have pared back the chance of a further hike from the Fed following global developments and dovish Fed speak from members. Markets are currently attaching around a 30% chance of another hike in this cycle. Almost four cuts are priced out to January 2025.

Movements in Australian bond yields were more muted. The 3-year government bond yield (futures) slipped 1 basis point, to 3.92%. The 10-year government bond yield (futures) fell 3 basis points, to 4.44%. Interest-rate markets are currently attaching around a 50% probability of another hike from the RBA by the end of the year. A 30% chance of a cut is priced by the end of 2024.

Foreign Exchange: The US dollar pulled back amid an improvement in risk sentiment and reduction in US interest rates. The USD Index fell from a high of 106.25 to a low of 105.66. It was trading at 105.77 at the time of writing.

This environment helped to provide some support to the Aussie. The AUD/USD pair rose from a low of 0.6390 to a high of 0.6433 and was trading around that level (0.6432) at the time of writing.

Commodities: Oil prices pulled back following their initial surge after the outbreak of the Israel and Hamas conflict. The West Texas Intermediate (WTI) futures contract fell to US$85.88 per barrel. Saudi Arabia reaffirmed its support for OPEC+ members to stabilise prices.

Copper, thermal coal, and iron ore rose, while coking coal and gold slipped.

Australia: The Westpac-Melbourne Institute consumer confidence index rose 2.9% in October to 82.0 – the strongest reading since January. Despite the bounce, confidence remains deeply entrenched in pessimistic territory.

Sentiment has been bumpy month-to-month since finding a floor in November last year. October's result was no different, meaning the monthly pickup is unlikely to reflect a sustained turnaround in household spirits.

Looking at the detail, a stabilisation in households' assessments of their current and future finances helped underpin the aggregate improvement. However, both measures remain notably weak.

The labour market continues to be a bedrock for households, offsetting weakness elsewhere. This leaves confidence susceptible to retesting cycle lows if the labour market deteriorates more quickly than expected.

While we have probably seen a bottom, it's unlikely that the mood among households will improve materially anytime soon. A successful return to the Reserve Bank's inflation target and relief on interest rates are likely necessary for a sustained rise in sentiment.

The pessimistic mood and prolonged squeeze on household budgets points to further weakness in consumption over the coming quarters. The ongoing rollover of fixed rate mortgages onto much higher variable rates is likely to compound this pressure.

Business conditions fell 3 points to +11 index points in September. Despite the fall, conditions remain around average levels. Business confidence was unchanged and has now been at +1 index point for three consecutive months.

All three sub-indices eased over September – trading (down 3 points to +16), profitability (down 6 points to +8) and employment (down 2 points to +8). Profitability recorded the largest decline and is now below its 10-year average.

Despite the resilience in conditions, we continue to see cost pressures ease with quarterly growth in both labour and input costs moderating by around 1 percentage point.

Growth in labour costs eased to 2.0% over the quarter to September following the sharp spike in July, which resulted from the 2023-24 minimum and award wage increase. In fact, growth in labour costs is well below the 3.3% rate recorded over the quarter to September 2022, suggesting that underlying momentum in wages growth is moderating.

Leading indicators point to resilience with forward orders ticking up back into positive territory and capacity utilisation remaining well above average despite a slight decline over September. This should continue to support business investment and credit growth.

Looking ahead, the stabilisation in leading indicators over recent months suggests that while growth is slowing, the softening in demand is likely to remain orderly. The resilience in conditions is reflective of this and suggests we are one step closer to achieving a soft landing.

Japan: The current account surplus narrowed to ¥2.3 trillion in August, down from ¥2.8 trillion in July. This was below consensus expectations, which centred on a widening of the surplus to ¥3.0 trillion. Despite the weaker-than-expected outcome, the result represents the seventh consecutive month of current account surpluses. The outcome was driven by a fall in exports to ¥7.9 trillion, from ¥8.6 trillion in July. Adding to this was an increase in imports, which rose from ¥8.5 trillion to ¥8.6 trillion in August.

United States: Several Federal Reserve members spoke overnight. Their comments were broadly in line with recent messaging that has helped to bolster the case that the Fed may remain on pause. This has been reflected in reduced market pricing of additional monetary policy tightening.

Raphael Bostic added to calls that the Fed is done hiking, noting that he thinks the "policy rate is at a sufficiently restrictive position to get inflation down to 2%" and that he doesn't "think we need to increase rates anymore".

Neel Kashkari added to recent sentiments from other Fed speakers in noting that "it's certainly possible that higher long-term yields may do some of the work for us in terms of bringing inflation back down". However, he cautioned around the interpretation of what the higher rates mean, stating that "if those higher long-term yields are higher because their expectations about what we're going to do has changed, then we might actually need to follow through in their expectations in order to maintain those yields."

Christopher Waller was somewhat more hawkish and noted that the Fed will stay “on the job to achieve our objective”. He echoed Fed Chair Powell in reiterating that "price stability is a primary responsibility of the Federal Reserve”.

World: The International Monetary Fund (IMF) released its October World Economic Outlook (WEO) overnight. The IMF expects global growth to slow from 3.5% in 2022 to 3.0% in 2023 and 2.9% in 2024. This is well below the historical average of 3.8%. The Fund cut its forecasts for growth in China and the eurozone, while noting the “remarkable strength” in the US economy.

Global inflation is expected to decline, but only gradually. The IMF forecasts global headline inflation to slow from 8.7% in 2022 to 6.9% in 2023 and 5.8% in 2024. Core inflation is expected to decline more slowly and not get back to target until around 2025. Tighter monetary policy and falls in commodity prices are supporting a slowing in inflation.

These forecasts represent upward revisions for inflation and slight downward revisions to growth relative to the previous report. Notably, inflation is expected to be 5.8% in 2024, compared with 5.2% in its July WEO.

Today’s key data and events:

NZ Net Migration Aug prev 5.8k (8:45am)

AU RBA's Kent Speech (11:30am)

EU Ger. CPI Sep Final exp 0.3% prev 0.3% (5pm)

US PPI Final Sep y/y prev 1.6% exp 1.6% (11:30pm)

US FOMC Meeting Minutes (5am)

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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