

Wednesday, 5 July 2023

Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	7,279	0.5%			Last	Overnight Chg		Australia		
US Dow Jones	34,418	closed	10 yr bond	4.00		0.00	90 day BBSW	4.33	-0.01	
Japan Nikkei	33,423	-1.0%	3 yr bond	3.98		0.02	2 year bond	4.06	0.02	
China Shanghai	3,402	0.0%	3 mth bill rate	4.47		0.00	3 year bond	3.98	0.02	
German DAX	16,039	-0.3%	SPI 200	7,233.0		-12	3 year swap	4.30	0.00	
UK FTSE100	7,520	-0.1%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	4.01	0.04
Commodities (close & change)*			TWI	61.9	-	-	61.9	United States		
CRB Index	260.9	-1.1	AUD/USD	0.6672	0.6705	0.6642	0.6691	3-month T Bill	5.18	closed
Gold	1,925.48	3.8	AUD/JPY	96.51	96.83	96.08	96.65	2 year bond	4.94	closed
Copper	8,406.00	82.3	AUD/GBP	0.5257	0.5269	0.5236	0.5263	10 year bond	3.85	closed
Oil (WTI futures)	71.00	1.2	AUD/NZD	1.0844	1.0856	1.0781	1.0806	Other (10 year yields)		
Coal (thermal)	151.25	-3.2	AUD/EUR	0.6113	0.6155	0.6095	0.6150	Germany	2.45	0.02
Coal (coking)	227.50	-3.5	AUD/CNH	4.8389	4.8449	4.8111	4.8370	Japan	0.39	-0.02
Iron Ore	108.60	-0.2	USD Index	102.97	103.11	102.88	103.08	UK	4.42	-0.02

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: Trading was thin as US markets were closed for the Independence Day public holiday. Bond yields across the Eurozone generally declined at the short end but rose at the long end. European equity markets were lower. The US dollar was slightly higher against major currencies.

Share Markets: US markets were closed. European markets were down on the day. The Euro Stoxx 50 fell 0.2%, the FTSE 100 was 0.1% down, and the German DAX declined 0.3%.

The ASX 200 rose 0.5% yesterday following a pause decision from the Reserve Bank (RBA). Six of 11 sectors rose and the ASX 200 jumped immediately after the decision. Energy, financials, and real estate were all more than 1% higher on the day. Futures are pointing to a weaker open today.

Interest Rates: US physical bonds were closed for the Independence Day public holiday. In Germany, the 2-year yield fell 3 basis points to 3.20% while the 10-year yield was 2 basis points higher, at 2.45%. In the UK, 2-year and 10-year gilt yields were both down 2 basis points, at 5.29% and 4.42%, respectively.

The 3-year Australian government bond yield (futures) rose 2 basis points to 3.98%. The 10-year futures yield was unchanged, at 4.00%. Interest-rate markets continue to price additional hikes from the RBA despite yesterday's pause. Markets are

currently attaching around a 45% probability of a 25-basis-point hike in August. Looking forward, markets expect the cash rate to rise to around 4.48% by the end of 2023.

Foreign Exchange: The US dollar rose slightly against a basket of major currencies. The DXY Index traded between a low of 102.88 and a high of 103.11, before closing at 103.08.

The AUD/USD pair strengthened overnight, despite a stronger US dollar and a pause from the RBA. The pair initially dropped sharply from around 0.6687 in the minutes before the RBA decision to a low of 0.6642 in the wake of the decision. However, it soon recovered that ground during the crossover of the Asian and London sessions. It then continued to trade higher during the London and New York sessions, reaching a high of 0.6705. It was trading at 0.6691 at the time of writing.

Commodities: Oil traded higher, rising to US\$71 per barrel. In recent days, Saudi Arabia announced that it would extend its previously announced 1 million barrel per day output cut into August. Russia also announced that it would cut its exports by 500k barrels per day in August. Overnight, Asian producers noted that there is plentiful supply from non-OPEC+ producers to help offset some of the impact of these supply cuts in the Asian region.

Copper and gold were also higher. Coal and iron ore

both declined on the day.

Australia: The Reserve Bank (RBA) Board left the cash rate unchanged at 4.10%, following twelve rate increases since May last year. However, the Governor's statement suggests that the pause may be short lived with the statement saying more tightening "may be required," and the pause providing more time to assess the economy.

Changes to the statement provide clues on the outlook for policy. There were plenty of changes. A key change was the recognition that the rapid increase in interest rates is having the intended impact on demand.

The hit to demand is expected to be significant enough that the reference to the economy remaining on an "even keel" was dropped for the very first time this cycle and replaced with the economy is expected "to grow as inflation returns to the target range, but the path to achieving this balance is a narrow one".

One interpretation of this change is that the RBA will do whatever it takes to get inflation down even if it leads to a sharp downturn. This is the approach followed by other central banks in the US and New Zealand and points to further hikes.

Another interpretation is that the RBA believes it is at risk of going too far and if it goes further, it may overshoot and do serious harm to the labour market. This interpretation is supported by the removal of a key paragraph outlining the upside risks to services inflation from wages growth.

Data since the last RBA Board meeting suggests that these risks remain – wages growth in enterprise agreements continue to pick up. The Fair Work Commission's 5.75% increase for award wages and the aged care wage decision, which provides a 15% wage boost, started from 1 July. This makes the RBA's messaging difficult to interpret.

Given the RBA's recent shifts in messaging, we don't yet believe there is enough evidence to materially change our expectation for the peak in the cash rate. We retain the expectation of two further hikes, with the next hike occurring in August. However, we stress that there are risks around the final hike – in terms of materialising and/or timing. The RBA will release an updated set of forecasts before the August Board meeting which should provide more clarity.

Today's key data and events:

CN Caixin Services PMI Jun exp 56.2 prev 57.1 (11:45am)
 EZ Markit Services PMI Jun Final exp 52.4 prev 52.4 (6pm)
 UK Markit Services PMI Jun Final exp 53.7 prev 53.7 (6:30pm)
 EZ PPI May y/y exp -1.3% prev 1.0% (7pm)
 US Factory Orders May exp 0.8% prev 0.4% (12am)
 US Durable Goods Orders May Final exp 1.7% prev 1.7% (12am)
 US FOMC Meeting Minutes (4am)

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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The Detail

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