Morning report

Bank of Melbourne

Friday, 17 November 2023

Equities (close & % change)		
S&P/ASX 200	7,058	-0.7%
US Dow Jones	34,946	-0.1%
Japan Nikkei	33,424	-0.3%
China Shanghai	3,199	-0.7%
German DAX	15,787	0.2%
UK FTSE100	7,411	-1.0%

Commodities (close & change)		
CRB Index	271.3	-5.5
Gold	1,981.15	21.3
Copper	8,218.00	27.0
Oil (WTI futures)	72.92	-3.7
Coal (thermal)	128.15	-1.8
Coal (coking)	323.67	13.7
Iron Ore	130.90	-0.1

Sydney Futures Exchange (last & change)	Last	Overnight Chg
10 yr bond	4.51	-0.06
3 yr bond	4.12	-0.06
3 mth bill rate	4.38	-0.02
SPI 200	7,085.0	-1

FX Last 24 hrs	Open	High	Low	Current
TWI	60.9	-	-	60.9
AUD/USD	0.6507	0.6520	0.6461	0.6466
AUD/JPY	98.52	98.62	97.25	97.47
AUD/GBP	0.5243	0.5252	0.5202	0.5211
AUD/NZD	1.0805	1.0846	1.0798	1.0838
AUD/EUR	0.6001	0.6011	0.5952	0.5962
AUD/CNH	4.7234	4.7327	4.6831	4.6861
USD Index	104.43	104.56	104.01	104.43

Interest rates (close & change)		
Australia		
90 day BBSW	4.39	-0.01
2 year bond	4.23	0.00
3 year bond	4.17	0.00
3 year swap	4.31	-0.10
10 year bond	4.55	0.02
United States		
3-month T Bill	5.24	-0.02
2 year bond	4.85	-0.07
10 year bond	4.45	-0.08
Other (10 year yields)		
Germany	2.59	-0.05
Japan	0.79	-0.01
UK	4.15	-0.08

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: Bond yields resumed their downward trend overnight as a range of second tier US data suggested increased risks of a slowing economy and continued positive signs on inflationary pressures. This was despite Fed members noting that the outcome of the December meeting was still uncertain. Equity markets were mixed as the recent rally appeared to run out of steam. The US dollar ended unchanged despite the falling yields, while the Aussie lost some ground.

Share Markets: Equity markets traded between gains and losses and ended mixed as the recent sharp rally higher appeared to run out of steam. The rally had caused equity prices to venture to around 'overbought' technical levels, likely contributing to weaker demand. The S&P 500 and the Nasdaq both ended the session 0.1% higher, while the Dow Jones was 0.1% lower.

The ASX 200 fell 0.7% yesterday as eight of 11 industries declined. Energy, IT and health care were the worst performers – each falling by 1% or more. Utilities, consumer stables and communication services bucked the trend and rose. Futures are pointing to a weaker open this morning.

Interest Rates: Bond yields continued their declines as economic data re-affirmed the market's view that the Fed was likely done hiking in this cycle. The policy-sensitive 2-year treasury yield fell 7 basis points, to 4.85%. The 10-year yield dropped by a larger 8 basis points, to 4.45%.

Interest-rate markets continue to price no chance of another hike from the Fed in this cycle and have increased their pricing of cuts in 2024. Markets now expect 3.9 cuts by the end of 2024 and 4.5 cuts by January 2025. This compares to around 3.6 and 4.1 cuts, respectively, a day ago.

Australian bond yields mimicked moves in the US. The 3-year and 10-year (futures) yields both fell 6 basis points, to 4.12% and 4.51%, respectively. Interest rate markets have also pared back their expectations of additional hikes from the RBA. Markets are now pricing around a 20% chance of another hike by May next year. This is down from almost 40% a day earlier.

Foreign Exchange: The US dollar ended unchanged against a basket of major currencies. The USD Index ranged between a high of 104.56 and a low of 104.01, before closing at 104.43.

The Aussie lost ground against the US dollar, paring back some of the sharp move higher earlier in the week following weaker-than-expected US inflation data. The Aussie began losing ground after the release of the Australian October labour force data, despite the release showing employment grew by more than expected in the month. The AUD/USD pair slipped from a high of 0.6520 – before the labour force data – to a low of 0.6461 in the wake of the release. It tested this low again during the overlap of the London and New York sessions, before recovering slightly to close at 0.6466.

Commodities: Oil prices plunged overnight and the West Texas Intermediate (WTI) futures contract dropped more than 5% at one point and finished at US$72.92 per barrel. The move extends the recent downtrend following data that showed US inventories are higher and that the demand picture looks weak. Trend-following strategies have also exacerbated the moves as prices breached key technical support levels.

Australia: Employment rose a very solid 55.0k in October. Strong labour demand is continuing to soak up rapid growth in the working age population. However, we are slowly nearing the point where the data takes a more decisive turn.

There has been a significant shift in the composition of employment growth. Since the middle of the year full-time employment has fallen by 29.8k, while part-time employment is up 161.6k. Businesses still want workers, but they don’t need them working as many hours.

A rise in the participation rate to a record equalling 67.0% saw labour supply grow more quickly than employment in October. This pushed the number of unemployed people up by 27.9k and drove a marginal lift in the unemployment rate to 3.7%, from 3.6% previously.

Growth in hours worked continues to slow and is not keeping pace with growth in employment. In fact, since June the number of hours worked has fallen by 0.3% while employment has grown by 0.9%. This is driving a fall in the average hours worked per employed person, a sign that the labour market is beginning to soften via hours rather than headcount.

In an early sign that firms may be becoming more selective in their hiring decisions, the youth unemployment rate jumped up sharply to 9.2% from 8.0% in September. This could also be an early indicator of some emerging fatigue in labour demand.

The path ahead for the labour market looks more challenging than the recent past. However, the jobs market is proving much more resilient than expected. This means that the anticipated adjustment in the labour market is likely to remain gradual.

Consumer inflation expectations rose to 4.9% in November, from 4.8% in October, as reported by the Melbourne Institute. Consumer inflation expectations have risen for two consecutive months, from 4.6% in September. However, expectations remain well down from their peak of 6.7% in June 2022.

Japan: Core machinery orders, which exclude volatile orders such as ships, rose 1.4% in September, above consensus forecasts for a 0.9% gain. The outcome follows a 0.5% drop in August. Core machinery orders provide an indicator of future capital spending in the economy. In annual terms, core orders were 2.2% down from their level a year ago. This outcome was better than expected and followed a 7.7% annual drop in August.

United States: The run of softer price data continued as import and export prices fell by more than expected in October. Import prices were down 0.8% in the month, following an upwardly revised 0.4% gain in the September. The result was weaker than the 0.3% drop expected by markets and was driven by a 6.5% plunge in petroleum prices. Excluding petroleum, import prices were down 0.2% in October.

Export prices fell 1.1% in October, below consensus estimates of a 0.4% drop. The fall follows a downwardly revised 0.5% gain in September. In annual terms, export prices were 4.9% down from a year earlier.

Industrial production fell by 0.6% in October, following a 0.1% gain in September. This ended a run of three consecutive months of growth. Separately, capacity utilisation slipped to 78.9%, from 79.5%. Both measures were weaker than expected by consensus. Factory production was impacted in the month by United Auto Workers strike-related slowdowns in activity at automaking firms, which also impacted related suppliers.

Homebuilder confidence declined as high interest rates and stretched affordability continue to impact homebuyers and flow through to confidence among homebuilders. The NAHB housing market index fell to 34 in November. This was down from the October reading and below consensus expectations, which were both at 40.

The Philadelphia Fed business outlook index rose in November but remained in contractionary territory. The measure rose from -9.0 in October to -5.9 in November, above consensus expectations of -8.0. Delivery times, inventories, and prices received rose in the month. While prices paid, new order, employment, and shipments all fell.

The Kansas City Fed manufacturing index was also higher in the month but remained in contractionary territory. The index rose to -2 in November, from -8 in October and above expectations of a -9 reading. Key subcomponents remained weak, however, reading around the volume of new orders and the number of employees were stronger compared to last month.

A few Fed members spoke overnight. Lisa Cook noted that she is "attuned to the risk of an unnecessarily sharp decline in economic activity and employment". She noted potential risks from tightener financial conditions on certain economic participants, including small businesses, the housing sector, and lower income households.

Loretta Mester noted that it will "take some time" for inflation to return to the Fed's 2% target. She remains open to the possibility of another hike. She noted that monetary policy settings were "more balanced" but that the outcome of the next meeting was still uncertain and that officials had time to assess the evolution of the economy.

Today's key data and events:

NZ PPI Q3 prev 0.2% (8:45am)

UK Retail Sales Oct exp 0.4% prev -0.9% (6:00pm)

US Housing Starts Oct exp -0.6% prev 7.0% (12:30am)

US Building Permits Oct exp -1.4% prev -4.5% (12:30am)

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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