Morning report

Wednesday, 4 August 2021

Equities (close & % change)			Sydney Futures Exchange (close & change)					Interest rates (close & change)		
S&P/ASX 200	7,474	-0.2%		Last		Overnight Chg		**Australia**		
US Dow Jones	35,116	0.8%	10 yr bond	98.85		0.00		90 day BBSW	0.02	0.00
Japan Nikkei	27,642	-0.5%	3 yr bond	99.71		0.00		2 year bond	0.04	0.01
China Shanghai	3,614	-0.5%	3 mth bill rate	99.97		-0.01		3 year bond	0.25	0.01
German DAX	15,555	-0.1%	SPI 200	7,381.0		9		3 year swap	0.37	0.00
UK FTSE100	7,106	0.3%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	1.16	-0.03
Commodities (close & change)*			TWI	61.6	-	-	61.8	**United States**		
CRB Index	215.3	-0.5	AUD/USD	0.7364	0.7408	0.7358	0.7394	3-month T Bill	0.04	-0.01
Gold	1,810.44	-3.0	AUD/JPY	80.51	80.92	80.16	80.63	2 year bond	0.17	0.00
Copper	9,520.00	-160.2	AUD/GBP	0.5303	0.5331	0.5298	0.5314	10 year bond	1.17	-0.01
Oil (WTI)	70.56	-0.7	AUD/NZD	1.0560	1.0565	1.0526	1.0534	**Other (10 year yields)**		
Coal (thermal)	146.40	-1.1	AUD/EUR	0.6203	0.6236	0.6199	0.6233	Germany	-0.48	0.01
Coal (coking)	212.63	-3.9	AUD/CNH	4.7598	4.7882	4.7578	4.7818	Japan	0.01	-0.01
Iron Ore	175.90	-3.3	USD Index	92.1	92.2	91.9	92.1	UK	0.52	0.00

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

Main Themes: Worries about the spread of the Delta variant continue to be a dominant theme in financial markets. However, a batch of encouraging earnings results in the US overwhelmed these worries overnight. And the S&P 500 index hit a new record high. The appetite for risk helped the AUD move higher after jumping in the wake of the Reserve Bank's decision to continue with its plan to taper its bond-buying program in September.

Share Markets: US share markets posted strong gains overnight. The S&P 500 jumped 36 points (or +0.8%) to hit a new all-time high and the Dow rose 278 points (or +0.8%) to be within a whisker of its recent all-time high. The Nasdaq increased 80 points (or +0.6%). Mostly positive earnings results offset investor concerns about the impact on demand from the delta variant and China's possible clampdown on online games.

Interest Rates: US bond yields were little changed overnight with the 2-year yield closing unchanged at 0.04% and the 10-year yield easing 1 basis point to end the session at 1.17%.

The Australian 3-year government bond yield (futures), which earlier rose from 0.27% to 0.30% in response to the Reserve Bank (RBA) decision, fell to 0.29%. Meanwhile, the Australian 10-year yield fell from 1.17% to 1.13% before steadying at 1.15% - roughly unchanged from pre-RBA levels.

Foreign Exchange: The Australian dollar was sidelined yesterday, as it waited for the RBA Board statement. The statement surprised the market. The RBA unexpectedly announced it would not be delaying the start date for the tapering of its bong-buying program. The AUD jumped in the wake of this statement, rising nearly half of one US cent, from 0.7365 to a high of 0.7408. This gain was fully unwound by the New York trading session overnight, before a late recovery to now trade at just under 74 US cents.

Since July 22, the AUD/USD pair has kept to a trading range of 0.7290 to 0.7413. Despite yesterday's movements, the pair has remained within the range. The high of 0.7408 over the past 24 hours is within pips of resistance at around the 0.7415 handle, which proved challenging for the AUD/USD. A lockdown in Australia and no convincing signs that daily infections have peaked in New South Wales are likely capping the AUD/USD as the near-term outlook remains clouded over.

Commodities: Most commodity prices fell overnight over fears about the Delta variant and China renewing restrictions (including cancelling flights) due to a resurgence of COVID-19.

COVID-19: NSW recorded 199 new COVID-19 cases yesterday, 70 of which were confirmed to be in isolation throughout their entire infectious period. Queensland recorded 16 new cases yesterday and

Victoria recorded 4 new cases.

According to the Infectious Diseases Society of America, the spread of the delta variant has pushed the threshold for herd immunity to well over 80% and potentially closer to 90%.

Australia: The RBA stuck to its game plan. It intends to still commence tapering of its bond-buying program in September, as announced last month. This surprised the market, including us. The RBA was widely expected to defer tapering given a contraction in economic activity is likely for the current September quarter.

The RBA highlights that this program is “flexible”, leaving the door open for a change of mind. With the number of daily infections yet to peak in New South Wales, leaving the door open is sensible.

The RBA is also sticking to its game plan of not expecting to lift the cash rate before 2024. We are not convinced and still anticipate the first rate hike to arrive in the first half of 2023.

Ahead of this Friday’s quarterly Statement on Monetary Policy, the RBA has also revised its key forecasts. Growth has been revised up a smidgen next year to above 4 per cent - a solid pace. The unemployment rate has been revised down to 4¼ per cent by end next year.

Forecasts have been extended to 2023. Growth in 2023 is expected to be slightly below trend and the unemployment rate forecast to breach what the RBA Governor has previously outlined as full employment.

A notable change to this month’s statement is the RBA expects the pickup in wages growth and underlying inflation to be “only gradual”, no longer “gradual and modest”. Perhaps this is a subtle concession to the possibility of stronger inflationary pressures and a slight hint that a rate hike before 2024 is not inconceivable for the RBA.

What is clear is that the RBA views the disruption from the current outbreak as temporary and a resumption in robust growth is anticipated.

Whether the RBA is able to keep to its plan depends critically on the containment the virus, a high share of the population being vaccinated by the end of the year and international borders gradually reopening from the middle of 2022.

Separately, data released yesterday showed lending for housing fell in June following rapid growth in the second half of 2020 and earlier this year. The value of new loans, excluding refinancing, dropped 1.6% in June from the record high in May.

The decline was led by fall in lending to owner occupiers, especially for construction, and first-home buyers. Investors continued to return to the housing market. Lending to investors lifted 0.7% in June. Regulators will be eyeing the return of investors carefully.

Like housing finance, building approvals pulled back in June. Approvals have wound back further after the pull forward effect of the HomeBuilder scheme, after applications closed in April. Building approvals fell 6.7% in June after falling in the previous two months. Approvals have declined 18.1% from the three-year monthly peak struck in March.

The decline in building approvals has been led by a fall in private sector housing. This category shrunk 11.8% in June – the sharpest monthly decline in almost 21 years. Building approvals for private sector ‘other’ (i.e. multi-density developments) bucked the trend and rose 0.8% in June.

The Roy Morgan weekly consumer confidence index rose 1.1 points to 101.8 in the week ending August 1. During this week, lockdowns came to an end in Victoria and South Australia, and Australians were advised of vaccine targets for reopening the economy.

United States: Factory orders in June rose 1.5%, stronger than the 1.0% expected by consensus. Also, May’s 2.1% gain was revised higher to 2.3%. Factory data this year has been strong, but capacity constraints and supply problems remain a headwind.

Durable goods orders for June were finalised. The final result showed a slightly firmer gain of 0.9% for the month, from a rise of 0.8% previously.

St. Louis Federal Reserve President James Bullard said that a new economic regime may have arrived, and the Fed will have to cope with faster change and more frequent shocks. Bullard added that Covid-19 may have pushed the US into a volatile era of stronger growth and better productivity, but with higher interest rates and faster inflation. Bullard is in favour of tapering starting sooner rather than later.

Federal Reserve President of San Francisco, Mary Daly, said she does not expect labour shortages to persist. She added that there’s "no reason" to think the almost 10 million Americans out of work won't eventually seek jobs.

Meanwhile, Federal Reserve Governor Waller said the Fed could favour tapering quantitative easing (QE) as early as September if the next two jobs reports are as strong as the last one. Alternatively, if the reports are weaker, then tapering will probably be delayed by a couple of months.

Today's key data and events:

NZ Private Wages Q2 exp 0.7% prev 0.4% (8:45am)
NZ Employment Q2 exp 0.7% prev 0.6% (8:45am)
NZ Unemployment Rate Q2 exp 4.4% prev 4.7% (8:45am)
AU Retail Sales (11:30am)
  Nominal or Value Final exp -1.8% prev - 1.8%
  Volumes Q2 exp 0.7% prev -0.5%
CH Caixin Serv. PMI Jul exp 50.5 prev 50.3 (11:45am)
EZ Markit Serv. PMI Jul Final exp 60.4 per 60.4 (6pm)
UK Markit Serv. PMI Jul Final exp 57.8 prev 57.8 (6:30pm)
EZ Retail Sales Jun exp 1.7% prev 4.6% (7pm)
US ADP Employment Jul exp 690k prev 692k (10:15pm)
US Markit Serv. PMI Jul F exp 59.8 prev 59.8 (11:45pm)
US ISM Non-Mfg Jul exp 60.5 prev 60.1 (12am)

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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