Morning report

Bank of Melbourne

Friday, 5 May 2023

Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	7,193	-0.1%		Last		Overnight Chg		**Australia**		
US Dow Jones	33,128	-0.9%	10 yr bond	3.31		0.00		90 day BBSW	3.87	0.00
Japan Nikkei	29,158	0.1%	3 yr bond	2.92		-0.04		2 year bond	3.10	-0.13
China Shanghai	3,512	0.8%	3 mth bill rate	3.86		0.00		3 year bond	2.98	-0.15
German DAX	15,734	-0.5%	SPI 200	7,162.0		-29		3 year swap	3.37	0.10
UK FTSE100	7,703	-1.1%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	3.30	-0.11
Commodities (close & change)*			TWI	60.3	-	-	60.3	**United States**		
CRB Index	256.8	0.2	AUD/USD	0.6672	0.6706	0.6641	0.6693	3-month T Bill	5.06	-0.01
Gold	2,050.27	0.0	AUD/JPY	89.82	90.12	89.17	89.86	2 year bond	3.79	-0.01
Copper	8,456.25	-48.0	AUD/GBP	0.5310	0.5329	0.5284	0.5324	10 year bond	3.38	0.04
Oil (WTI futures)	68.56	0.0	AUD/NZD	1.0712	1.0718	1.0623	1.0660	**Other (10 year yields)**		
Coal (thermal)	178.80	-12.4	AUD/EUR	0.6031	0.6085	0.6000	0.6078	Germany	2.19	-0.06
Coal (coking)	243.50	3.5	AUD/CNH	4.6160	4.6368	4.5959	4.6304	Japan	0.42	0.00
Iron Ore	96.60	-2.8	USD Index	101.20	101.64	101.03	101.42	UK	3.65	-0.04

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: Growing contagion concerns around the health of US regional banks weighed on risk sentiment. These concerns led to large falls in equity prices. Bond yields also fell sharply but retraced their moves later in the day.

The European Central Bank (ECB) delivered a 25-basis-point hike and comments from ECB President Lagarde indicated that they were far from done, suggesting that further hikes are likely to come. The US dollar was mixed against a basket of major currencies but closed higher.

Share Markets: Regional bank shares continued their plunge overnight, led by large falls in Western Alliance, PacWest and First Horizon. The falls were sparked by continued concerns over the health of regional banks following the recent failure of First Republic Bank. This drove the KBW regional banking index down 2.9% on the day. This extended the KBW index's rout to 33% since the beginning of March – prior to the collapse of Silicon Valley Bank.

The S&P 500 ended down 0.7%. The Nasdaq was 0.5% weaker and the Dow Jones lost 0.9%.

The ASX 200 finished 0.1% lower yesterday. Real estate (2.0%) was the best performing sector, followed by materials, IT, and utilities (all up 1.2%). However, the index was dragged down by a 2.5% fall in financials, as banking concerns and weaker-than-expected results weighed on the sector. Futures are pointing to a weaker open today.

Interest Rates: Bond yields gyrated sharply on the day as banking sector concerns weighed on investor sentiment. However, yields recovered much of their sharp movements and ended the session with relatively minor movements from the open. The US 2-year bond yield initially plunged from a high of 3.89% to a low of 3.65%, before retracing much of the loss to finish 1 basis point down on the day, at 3.79%. The 10-year yield also moved sharply from a high of 3.41% to a low of 3.29%, before closing 4 basis points higher, at 3.38%.

Interest-rate markets expect that the Fed is done hiking and are pricing in over 100 basis points of cuts by the end of 2023.

The 3-year Australian government bond yield (futures) closed 4 basis points lower, at 3.92%. The 10-year government bond yield (futures) closed unchanged, at 3.31%. Interest-rate markets are pricing in little chance of further hikes from the RBA and have almost a full 25-basis-point cut priced by the end of 2023.

Foreign Exchange: The US dollar was mixed against a basket of major currencies by ended higher on the day. The USD Index rose from a low of 101.03 to a high of 101.64, before retracing some of that gain to close at 101.42.

The AUD/USD pair was stronger on the day, rising from a low of 0.6641 to a high of 0.6706. It was trading at 0.6693 at the time of writing.

Commodities: Oil and gold ended the session largely unchanged, while copper, iron ore and thermal coal were all weaker.

Australia: The trade surplus widened to $15.3 billion in March. This was the second largest trade surplus on record. The outcome was above consensus expectations of $13.0 billion and followed an upwardly revised surplus of $14.2 billion in February. The outcome reflected a rebound in both exports and imports. The value of exports rose 4% in the month, driven by metal ores and minerals. This followed a 3% fall in February. Stronger exports were partly offset by stronger imports, which rose 2% in the month. This followed a 10% drop in imports in February.

The monthly trade data is in nominal terms and doesn't abstract from the impact of changing prices. However, it is possible to adjust the monthly data by the quarterly trade price indices. This suggests that net exports are likely to drag on real GDP growth in the March quarter. This drag could range between 0.5 and 1.1 percentage points based on the average historical relationship between the monthly and quarterly trade data. The final estimate will be available when the Australian Bureau of Statistics publishes the March quarter balance of payments data, due 6 June.

China: The manufacturing sector slipped into contractionary territory in April as the Caixin manufacturing purchasing managers index (PMI) fell to 49.5 in the month. This was below consensus expectations and down from the March reading, which were both at 50.0. Output slowed from March but remained in expansionary territory. New orders and employment were also down.

The manufacturing sector may face continued challenges going forward as tight monetary policy in advanced economies and slowing global growth reduce demand for Chinese made goods from overseas trading partners.

Eurozone: The European Central Bank (ECB) hiked by 25 basis points. This was widely expected by markets and sees the main refinancing rate rising to 3.75%. The hike is unlikely to be the last in the cycle, as ECB President Lagarde pushed back against the thought of a pause by stressing that they have more work to do to control inflationary pressures. Specifically, she stated that "we have more ground to cover and we are not pausing".

The ECB also sees further upside risks to inflation. The decision was supported by almost all members, with those dissenting members favouring a larger 50-basis-point hike, rather than a pause. In addition to hiking rates, in July, the ECB will stop reinvesting the proceeds from assets it purchased under its quantitative easing asset purchase program (APP). This will act as an additional form of monetary policy tightening.

Separately in Europe, the Norges Bank, Norway's central bank, also hiked by 25 basis points, to 3.25%.

Producer prices continued to decline in March, falling 1.6% in the month. This was slightly weaker than the 1.7% drop expected by consensus and followed a 0.4% fall in February. In annual terms, producer prices have been falling rapidly over recent months from a peak of 43.4% in August 2022 but remain elevated, at 5.9% over the year to March. The March outcome reflected a large drop from the 13.3% annual result in February due to significant base effects washing out of the calculation, including those following Russia's invasion of Ukraine in February 2022.

The services PMI was finalised at 56.2 in April, from a preliminary reading of 56.6.

New Zealand: Building permits for all dwellings rose 7.0% in March. This was the first monthly gain in four months and followed a 9.4% fall in February. House approvals also posted their first gain in four months, rising 0.2% in March.

United Kingdom: The services sector was in expansionary territory for the third consecutive month, as the services PMI was finalised at 55.9 in April. This follows a preliminary reading of 54.9.

United States: The trade deficit narrowed in March to $64.2 billion but was above consensus expectations of a $63.1 billion deficit. This followed a deficit of $70.6 billion in February. The outcome reflected a 2.1% gain in exports and a 0.3% fall in imports.

Non-farm labour productivity declined 2.7% in Q1 as unit labour costs rose 6.3%. The fall in productivity and increase in unit labour costs were both larger than expected. Unit labour costs are an indicator of the average cost of labour per unit of output produced in the economy and provide a measure of labour costs accounting for productivity. This measure can be very volatile in the near term so needs to be considered with caution. However, weaker productivity growth can mean that the level of wage growth consistent with inflation returning to target is lower than otherwise. This may cause additional challenges for the Federal Reserve in its goal of returning inflation to the 2% target. Domestically, concerns around rising unit labour costs have also been raised by the RBA in its recent decision to hike by 25 basis points.

Today's key data and events:

NZ Retail Card Spending Apr prev 0.7% (8:45am)

AU RBA Statement on Monetary Policy (11:30am)

AU Housing Finance Mar (11:30am)

Investor exp 0.0% prev -0.5%

Owner-occupier exp -0.5% prev -1.2%

Total exp -0.3% prev -0.9%

CN Caixin Serv. PMI Apr exp 57.0 prev 57.8 (11:45am)

EZ Ger. Factory Orders Mar exp -2.3% prev 4.8% (4pm)

EZ Retail Sales Mar exp -0.2% prev -0.8% (7pm)

US Non-farm Payrolls Change Apr exp 182k prev 236k (10:30pm)

US Unemployment Rate Apr exp 3.6% prev 3.5% (10:30pm)

US Average Hourly Earnings Apr exp 0.3% prev 0.3% (10:30pm)

US Consumer Credit Mar exp $16.8bn prev $15.3bn (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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