Morning report

Bank of Melbourne

Thursday, 14 May 2020

Equities (close & % change)			Sydney Futures Exchange (close & change)					Interest rates (close & change)		
S&P/ASX 200	5,421.9	0.3%		Last		Overnight Chg		Australia		
US Dow Jones	23,248.0	-2.2%	10 yr bond	99.09		0.04		90 day BBSW	0.09	0.00
Japan Nikkei	20,267.1	-0.5%	3 yr bond	99.76		0.00		2 year bond	0.23	0.01
China Shanghai	3,037.9	0.2%	3 mth bill rate	99.87		0.00		3 year bond	0.24	0.00
German DAX	10,542.7	-2.6%	SPI 200	5,371.0		-53		3 year swap	0.21	-0.02
UK FTSE100	5,904.1	-1.5%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	0.96	0.00
Commodities (close & change)*			TWI	57.3	-	-	57.2	United States		
CRB Index	120.6	-2.0	AUD/USD	0.6477	0.6524	0.6438	0.6455	3-month T Bill	0.11	-0.02
Gold	1,716.3	13.6	AUD/JPY	69.43	69.76	68.89	69.11	2 year bond	0.16	0.00
Copper	5,231.0	2.3	AUD/GBP	0.5279	0.5299	0.5262	0.5276	10 year bond	0.65	-0.01
Oil (WTI)	25.6	-0.2	AUD/NZD	1.0646	1.0781	1.0617	1.0767	Other (10 year yields)		
Coal (thermal)	55.1	1.0	AUD/EUR	0.5970	0.5999	0.5947	0.5966	Germany	-0.53	-0.03
Coal (coking)	112.3	-2.8	AUD/CNH	4.6030	4.6333	4.5808	4.5905	Japan	0.00	0.00
Iron Ore	86.2	0.8	USD Index	100.0	100.3	99.6	100.2	UK	0.21	-0.04

Copper, oil, coal & iron ore prices are based on futures pricing. Source: Bloomberg, Thomson Reuters Eikon.
Data as at 8am AEST. Change from previous trading day (excluding the SFE which is the change during the night session).

Main Themes: Sentiment soured following a warning from Fed Chair Powell about the significant downside economic risks from the coronavirus pandemic. Investors also mulled the recent flare up in tensions with China and the potential for a second wave of infections.

Share Markets: US equities slumped overnight. The Dow Jones fell 2.2% and the S&P 500 was down 1.8% to a 3 week low. Weakness was broad based, with all sectors in the S&P 500 declining. Concerns over a second wave of infections left energy and airline stocks down the most.

European shares traded lower, with the Euro Stoxx 50 down 2.6%. Futures are pointing to a weaker open on the ASX.

Interest Rates: US treasury yields traded in a relatively narrow range, but with pressure to the downside following Fed Chair Powell's sobering comments. The 2-year yield was unchanged at 0.16% while the 10-year yield fell 1 basis point to 0.65%. Fed funds futures had been pricing in a slight chance of a negative Fed funds rate this year, but those bets were pushed out to the middle of next year after Powell reiterated that the Federal Open Market Committee did not favour the policy.

Australian bond yields were mixed yesterday. The 3-year yield was steady at 0.24% and the 10-year yield was unchanged at 0.96%.

Foreign Exchange: The US dollar index rose to 100.2 from 100.0 yesterday as the mood remained risk-off. The Japanese yen was one of the best performing currencies overnight, and is currently at 107.06. Most currency price action occurred around Fed Chair Jerome Powell's speech. Trading was in a relatively narrow range otherwise.

The New Zealand dollar fell sharply following the RBNZ's announcement that it was loosening monetary policy further. The New Zealand dollar fell from around US$0.6080 before the announcement to US$0.6030 shortly after. It continued to weaken overnight and is currently at US$0.5998 this morning.

The Australian dollar is currently at US$0.6455 after trading as high as US$0.6524 overnight.

Commodities: Oil prices fell despite an unexpected decline in US stockpiles last week. OPEC once again slashed its forecasts for the oil market outlook. The cartel cut estimates for the amount of crude it will need to supply over the next three months by about 15%. WTI futures fell by US$0.2 per barrel to US$25.6.

Gold prices rose amid the risk-off sentiment to US$1,716.3 per ounce.

The domestic supply of beef in the US has fallen sharply, prompting fast-food giant Wendy's to issue a warning that some items will be discontinued if the shortage persists. News reports suggest that imports from other countries, particularly Mexico, have increased.

COVID-19: Global cases rose by 65,500 yesterday and deaths rose by 3,576, according to data compiled by Bloomberg. The number of new cases and deaths appear to be stabilising, but concerns remain of a second wave of infections globally.

Australian data show that there were 13 new cases yesterday. There have been 98 deaths due to COVID-19 in Australia, according to the Department of Health.

Australia: The wage price index rose 0.5% for the fourth consecutive quarter in the March quarter, confirming that there was little upward pressure on wages ahead of the widespread movement restrictions introduced in Australia to contain the spread of the coronavirus. On an annual basis, wage price growth slipped to 2.1%, from 2.2% in the December quarter of 2019, the weakest in nearly two years. There have been some early signs of wages growth slowing amid an increase in unemployment and a fall in aggregate demand. With the unemployment rate expected to remain elevated for some time, wage growth is likely to remain subdued.

After a historic decline in April, the Westpac-Melbourne Institute consumer sentiment index rebounded sharply in May, lifting from a 29-year low of 75.6 to 88.1. It was the largest monthly gain in the 47-year history of the survey, and followed the biggest decline on record. The sharp rebound suggests there is optimism over how Australia has dealt with the coronavirus outbreak, given new cases have stabilised at a low level. Moreover, talk of easing social distancing restrictions occurred during the survey period, which likely gave confidence a lift. Despite the rebound, the level of the index remains at low levels, and below 100, suggesting consumers remain pessimistic. It was also the second lowest reading since 2009. Caution among consumers is understandable given the risks of a renewed wave of infections with re-opening the economy and given the fragile economic backdrop.

United Kingdom: The latest round of production and activity data was weak, but not as bleak as consensus expectations. GDP fell 2.0% in Q1 and 5.8% in the month of March alone. Industrial production declined 4.2% in March while manufacturing output was 4.6% lower. The UK began its lockdown in March, and progressively ramped up measures as cases and deaths surged. It has since begun to gradually ease some restrictions.

New Zealand: The Reserve Bank of New Zealand (RBNZ) significantly expanded quantitative easing and nearly doubled its Large Scale Asset purchase (LSAP) programme from $33 billion to $60 billion. The RBNZ views the balance of risks towards the downside, and was particularly concerned about the world economy even if COVID-19 were successfully contained locally. The RBNZ stated that the expansion of the LSAP programme aimed to “reduce to cost of borrowing quickly and sharply”, and suggested it was the path of least regret by taking action now instead of later and possibly requiring more stimulus. The RBNZ also flagged the possibility for further monetary easing and “prepared to use additional monetary policy tools if and when needed, including reducing the OCR further, adding other types of assets to the LSAP programme, and providing fixed term loans to banks”. These comments and by Governor Orr later on leave open the door for a negative OCR. While the RBNZ said that a negative OCR cannot be implemented currently due to operational issues at trading banks, Orr said that “we will be assessing the use of negative interest rates along with other tools”.

United States: Federal Reserve Chairman Jerome Powell said that the US economy faced significant downside risks and encouraged further government spending. Speaking online he said “the path ahead is both highly uncertain and subject to significant downside risks” and that “additional fiscal support could be costly, but worth it”.

In the Q&A part of the session, he downplayed the notion of negative interest rates. He said “The committee’s view on negative rates has not changed. This is not something we are looking at”. Powell had previously said that he was confident in the Fed’s toolkit and was prepared to utilise it further if required. In previous discussions about negative rates, Federal Reserve committee members have been in agreement that the effectiveness of negative interest rates was limited and that the costs outweighed the benefits.

Economic data released showed that producer prices fell by the most since 2009 in April, highlighting likelihood of a deflationary episode in the US. Producer prices for final demand fell 1.3% in April following a 0.2% decline in March.

Today's key data and events:

NZ Net Migration Mar prev 8250 (8.45am)

AU Consumer Inflation Expectations May prev 4.6% (11am)

AU Labour Force Apr (11:30am)

- Employment Change exp -450k prev 5.9k
- Participation Rate exp 65.8% prev 66.0%
- Unemployment Rate exp 8.3% prev 5.2%

EZ German CPI Apr final exp 0.4% prev 0.4% (4.00pm)

US Import Price Index Apr ex -3.2% prev -2.3% (10.30pm)

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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