Bank of Melbourne

Morning report

Wednesday, 15 November 2023

Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	7,007	0.8%		**Last**		**Overnight Chg**		**Australia**		
US Dow Jones	34,828	1.4%	10 yr bond	4.55		-0.13		90 day BBSW	4.41	-0.01
Japan Nikkei	32,696	0.3%	3 yr bond	4.18		-0.12		2 year bond	4.34	0.00
China Shanghai	3,204	0.3%	3 mth bill rate	4.41		-0.02		3 year bond	4.29	0.00
German DAX	15,614	1.8%	SPI 200	7,116.0		91		3 year swap	4.41	-0.07
UK FTSE100	7,440	0.2%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	4.66	-0.01
Commodities (close & change)			TWI	60.1	-	-	60.1	**United States**		
CRB Index	277.5	-0.2	AUD/USD	0.6379	0.6512	0.6361	0.6508	3-month T Bill	5.23	-0.04
Gold	1,962.86	15.9	AUD/JPY	96.73	97.94	96.48	97.78	2 year bond	4.83	-0.21
Copper	8,126.25	131.8	AUD/GBP	0.5196	0.5208	0.5177	0.5206	10 year bond	4.45	-0.19
Oil (WTI futures)	78.24	0.0	AUD/NZD	1.0845	1.0869	1.0826	1.0829	**Other (10 year yields)**		
Coal (thermal)	126.00	-0.5	AUD/EUR	0.5962	0.5984	0.5938	0.5981	Germany	2.60	-0.11
Coal (coking)	306.50	3.0	AUD/CNH	4.6516	4.7220	4.6449	4.7190	Japan	0.86	-0.01
Iron Ore	130.25	2.1	USD Index	105.66	105.73	103.99	104.03	UK	4.15	-0.16

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: There was a risk on tone overnight with the US inflation print coming in softer than expected. The underlying read suggests that services inflation is also slowing. Markets have increased bets that Fed is now done with the hiking cycle, effectively pricing in zero chance of a hike when the Fed meets next and bringing forward the first full rate cut to June next year from July. This was despite hawkish comments made by several Fed officials suggesting that there's still a way to go in the inflation battle.

US and global equities jumped to finish in the green. US bond yields fell sharply. The US dollar lost value, with the Aussie outperforming on the back of the increased risk sentiment. Oil was broadly unchanged and equity futures are pointing to a strong opening.

Share Markets: US equities jumped to finish in the green. The S&P 500 added 1.9% with more than 95% of the S&P 500 companies increasing in value. Financial shares outperformed. The Dow lifted 1.4% and the Nasdaq rose 2.4%.

The ASX 200 index closed 0.8% higher, after two consecutive days of losses. The gain was led by the mining and energy sectors. Equities are poised to rise sharply today.

European markets also finished in the green with the DAX closing 1.8% higher and the Euro Stoxx 50 up 1.4%.

Interest Rates: US bond yields declined across the curve as more investors increased bets that the Fed's hiking cycle is now done. The US 2-year yield declined by 21 basis points to 4.83%. The 10-year yield declined by 19 basis points to 4.45% - the lowest yield since September.

Interest-rate markets have priced in zero chance of another hike by the US Fed this cycle. A full rate cut is priced in for June 2024, early than July which was previously priced in. There is also a 90% chance of a full cut in May 2024.

Australian government bond yield (futures) also declined overnight. The 10-year (futures) yield fell 13 basis points to 4.55%. The 3-year yield fell by 12 basis points to 4.18%

Interest rate markets have a probability of 58% of a further rate hike from the Reserve Bank by July next year – following the Q1 inflation release.

Foreign Exchange: The US dollar lost value in line with the sharp decline in US bond yields. The DXY index fell from a high of 105.73 to a low of 103.99 and is currently trading at around this low (lowest level since September).

The Aussie outperformed, supported by the increased risk sentiment. The AUD/USD pair shot up from a low of 0.6361 to a high of 0.6512. It is now trading above this 0.6500 level. A stronger than expected wages read today for the September quarter could help the Aussie consolidate gains at this higher level.

Commodities: Commodities were generally higher. The price of oil was unchanged - West Texas Intermediate (WTI) futures prices remained under USD80 a barrel.

Australia: The Westpac-Melbourne Institute consumer confidence index fell 2.6% in November to 79.9 – from 82.0 in October. The move largely unwound the small improvement in October, leaving the index deeply entrenched in pessimistic territory.

The fall follows a 25-basis-point hike in the cash rate from the Reserve Bank (RBA) in November to 4.35%. The hike dashed hopes that interest rates had peaked after a four month pause prior to the November meeting.

Unsurprisingly, the increase in the cash rate dented confidence the most for those with a mortgage. Views on family finances over the next 12 months dropped by 7.3%, no doubt reflecting concerns over higher mortgage repayments.

Views on the labour market deteriorated. However, this remains around the long-run average and strong employment conditions continue to be a key support for households.

Weak sentiment points to risks around consumer spending heading into the Christmas period.

A material recovery in consumer sentiment remains some time away. More progress on inflation and a clearer view on the interest rate outlook will likely be necessary prerequisites for a material uplift in confidence.

Business confidence fell into negative territory in October for the first time in four months, falling 3 points to -2 index points. Confidence has been hovering around or just below the zero level (which separates optimists from pessimists) for most of 2023.

Despite falling confidence, business conditions rose 1 point to +13 index points and remained above the long-run average. Taken together with today's consumer sentiment release, the dichotomy between the aggregate and per capita economy and current conditions compared to the outlook remains. This has been a key theme through 2023.

Looking at the sub-indices, profitability and trading conditions rose. Employment conditions fell for the second consecutive month but remain above average – consistent with a still tight but gradually easing labour market.

Capacity utilisation was broadly unchanged and remains well-above average, reflecting resilient demand and conditions. This is supporting business investment and credit growth. Other leading indicators point to a slowdown in the period ahead. Forward orders fell to be just in negative territory and have been negative for four of the past six months.

The survey points to a continued easing in cost pressures. Quarterly growth in labour and purchase costs both slowed to 1.8% in October, from 2.1% and 2.0%, respectively, in September. Growth in final prices also slowed to 1.0% – the slowest pace since February 2021.

New Zealand: Food prices fell 0.1% over the month of October, following an increase of 0.2% in September. In annual terms, food prices were 6.3% higher, moderating from the 8.0% increase recorded in September. The annual price increase was driven by grocery food, mainly fresh eggs, potato crisps, and yoghurt.

United Kingdom: The unemployment rate remained at 4.2% over the three months to September 2023. This was unchanged from the April to June period. The number of unemployed individuals rose by 9k to 1.448 million. Annual growth in regular pay eased to 7.7%, down slightly from the 7.9% recorded over the previous period (April to June). Annual growth in total pay slowed to 7.9% from the 8.2% recorded in the previous period. This was stronger than the 7.3% the market was expecting and remains inconsistent with the inflation target. These statistics were derived using experimental collection methods.

United States: Inflation broadly slowed in October, which markets took as an indication that the Fed is done hiking rates.

The headline price index was unchanged over October - the weakest read in fifteen months. Core inflation, which excludes food and energy costs, increased 0.2% over October. This was lower than the 0.3% the market was expecting. Annualized, core inflation is running at 2.8% — not far from the Fed's 2% target.

The services super core inflation rate, which excludes housing and energy, increased 0.2% over the month, down from the 0.6% recorded in September. This was the slowest read in nearly two years. Core goods prices declined 0.1%, the fifth consecutive decline. That was driven by a drop in car prices.

Finally, housing, which make up about a third of the overall CPI index, climbed 0.3%. This was half the prior month's pace. A sustained moderation in this category is key to bringing core inflation down to the Fed's target.

Chicago Fed President, Austan Goolsbee, called the report "slow but clear progress" stating that "we still have a way to go. With goods inflation already coming down and non-housing services inflation typically slow to adjust, the key to further progress over the next few quarters will be what happens to housing inflation."

Richmond Fed President, Tom Barkin, remained cautious "I'm just not convinced that inflation is on some smooth glide path down to 2%. The inflation numbers have come down, but much of the drop has been partial reversal of Covid-era price spikes, which were driven by elevated demand and supply shortages. Shelter and shelter inflation remain higher than historic levels, so does services inflation."

Today's key data and events:

AU Wage Price Index Q3 (11:30am)
  q/q exp 1.3% prev 0.8%
  y/y exp 3.9% prev 3.6%
CH Ind. Production Oct y/y prev 4.5% (1:00pm)
CH Retail Sales Oct y/y prev 5.5% (1:00pm)
EZ Ind. Production Sep prev 0.6% (9:00pm)
EZ Trade Balance Sep prev €11.9 (9:00pm)
JN GDP Q3 prev 1.2% (10:50am)
NZ Net Migration Sep prev 9980 (8:45am)
UK CPI Oct y/y prev 6.7% (6:00pm)
US Retail Sales Oct prev 0.7% (12:30am)
US PPI Oct prev 0.5% (12:30am)
US NY Empire Mfg Nov prev –4.6 (12:30am)
US Business Inventories Sep prev 0.4% (2:00am)

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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