Morning report

Friday, 17 June 2022

Equities (close & % change)			Sydney Futures Exchange (close & change)					Interest rates (close & change)		
S&P/ASX 200	6,591	-0.2%		Last		Overnight Chg		**Australia**		
US Dow Jones	29,927	-2.4%	10 yr bond	95.88		-0.06		90 day BBSW	1.74	0.04
Japan Nikkei	26,431	0.4%	3 yr bond	96.15		-0.06		2 year bond	3.18	-0.13
China Shanghai	3,443	-0.6%	3 mth bill rate	96.76		-0.02		3 year bond	3.50	-0.19
German DAX	13,038	-3.3%	SPI 200	6,325.0		-135		3 year swap	4.11	0.00
UK FTSE100	7,045	-3.1%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	3.99	-0.21
Commodities (close & change)*			TWI	62.0	-	-	62.7	**United States**		
CRB Index	317.2	2.4	AUD/USD	0.7007	0.7069	0.6944	0.7049	3-month T Bill	1.47	-0.13
Gold	1,857.33	23.5	AUD/JPY	93.78	94.54	91.97	93.29	2 year bond	3.09	-0.10
Copper	9,232.00	5.3	AUD/GBP	0.5757	0.5777	0.5662	0.5705	10 year bond	3.20	-0.09
Oil (WTI futures)	117.59	2.3	AUD/NZD	1.1146	1.1169	1.1036	1.1081	**Other (10 year yields)**		
Coal (thermal)	322.40	1.8	AUD/EUR	0.6707	0.6727	0.6630	0.6676	Germany	1.71	0.07
Coal (coking)	376.50	-7.2	AUD/CNH	4.6767	4.7253	4.6686	4.7123	Japan	0.26	0.00
Iron Ore	126.15	-1.9	USD Index	104.83	105.49	103.42	103.89	UK	2.52	0.05

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: Pessimism over the global economic recovery is taking hold as investors worry about the impact of aggressive central bank tightening on economic growth. Recession fears are growing. The S&P 500 dropped to its lowest level since December 2020. US bond yields continued to decline and the US dollar was weaker.

Share Markets: US equities unwound their post-Fed gains and then some. The S&P 500 fell 3.3% to its lowest level since December 2020. Week to date, the index is down 6.0%, putting it on track for its worst week since March 2020, early in the pandemic. The Dow declined 2.4% in the overnight session, while the tech-heavy Nasdaq dropped 4.1%.

The ASX 200 edged down 0.2% but futures point to a sizeable drop on opening.

Interest Rates: US treasury yields continued to trade in a wide range. The 10-year yield touched as high as 3.49% before dropping to close 9 basis point down over the day at 3.20%. The 2-year yield reached a high of 3.39% before reversing to finish down 10 basis points on the day, at 3.09%. Both the 10-year and 2-year yields are back around their level from 10 June, following the dramatic run-up and fall in yields over the past 5 sessions.

Market pricing is split on whether the Fed will hike 50 or 75 basis points at the July meeting, with pricing currently pointing to a 69 basis point increase in the federal funds rate. Markets expect the Fed to hike rates around another 200 basis points by the end of the year.

Australian 10-year (futures) yield ended unchanged at 4.08% while the 2-year futures yield declined 3 basis points to 3.77%.

Interest-rate markets are 104% priced for a 50 basis point rate hike at the Reserve Bank's July meeting, and expect the cash rate to reach 3.71% by the end of the year.

Foreign Exchange: The AUD/USD rose from 0.7007 to 0.7049, after touching a high of 0.7069, boosted by the weaker US dollar. The stronger-than-expected Australian jobs report had little lasting impact.

Commodities: Oil, gold and copper posted gains, while iron ore slipped.

Australia: The labour market delivered yet another upside surprise in May, showing that the jobs market still holds considerable momentum, despite the shrinking pool of spare capacity. Employment accelerated at its fastest rate since February, adding 60.6k new jobs in May.

In May, the participation rate lifted to a record high of 66.7%. In other words, additional labour market capacity was unlocked as more Australians were drawn into the jobs market.

The unemployment rate held steady at 3.9%, around its lowest level in almost half a century, as the increase in participation offset the rise in jobs.

Across the board, labour market indicators point to a very tight jobs market. As the unemployment rate hovers around full employment, workers are increasingly shifting from part-time to full-time. This continued in May. Plus, hours worked rose to a new record high and the underemployment rate fell to 5.7%, its lowest in nearly 14 years.

Labour shortages are widespread. In April 2022, 18% of employing businesses did not have enough staff, according to a survey conducted by the Australia Bureau of Statistics.

Leading indicators underscore that labour demand remains very strong. We expect the jobless rate to continue to decline over the rest of the year. However, labour shortages and skills mismatches may begin to slow jobs growth as businesses struggle to find suitable hires.

Consumer inflation expectations, as measured by the Melbourne Institute, rose to 6.7% in June - the highest level since July 2008. This follows a reading of 5.0% in May. The result highlights the importance of quickly returning interest rates to a more neutral level, to prevent inflation expectations from rising too sharply.

Europe: The Swiss National Bank surprised with a 50 basis point hike to -0.25%. It was the central bank's first hike since 2007. The Swiss National Bank indicated more hikes may be needed to counter inflationary pressures.

New details are starting to emerge about the European Central Bank's new "anti-fragmentation" instrument. The instrument was announced following the central bank's unscheduled meeting this week after Italian bond yields surged. Any bond-buying will probably involve selling other securities so to minimise inflationary consequences. Officials want the new tool ready for the central bank's July meeting. President Lagarde advised the instrument could be triggered if bond spreads widen too far or too fast.

New Zealand: March quarter GDP growth surprised to the low side as the New Zealand economy contracted 0.2% over the quarter. This compares to consensus expectations of a 0.6% gain. The impact of Omicron weighed heavily on activity in the quarter via lockdowns and workforce disruptions. The result follows a 3.0% quarterly rise in activity in the December quarter and takes the annual pace of growth to 1.2%.

United Kingdom: The Bank of England increased its policy rate by 25 basis points to 1.25%, its highest level in 13 years, as expected. It is the fifth consecutive hike from the central bank, which signalled it is prepared to implement larger hikes if needed. Policymakers flagged they would act "forcefully" if necessary. The central bank raised its forecast for inflation to peak above 11% this year.

United States: The Philadelphia Fed index fell to -3.3 in June, from 2.6 in May, marking the first negative reading since May 2020 in the early months of the pandemic. The components were mixed. Higher employment and faster deliveries indicated an easing in labour and supply constraints but were offset by a drop in new orders.

Housing starts and building permits both fell by more than expected in May. Starts 14.4% in the month to an annualised rate of 1.549 million, their lowest level in 13 months. Meanwhile, permits fell 7.0% to an annualised rate of 1.695 million. The declines reflects ongoing supply disruptions and shrinking sales as mortgage rates rise.

Today's key data and events:

NZ BusinessNZ Mfg PMI May prev 51.2 (8:30am)

EZ CPI May y/y Final exp 8.1% prev 7.4% (7pm)

US Indust. Production May exp 0.4% prev 1.1% (11:15pm)

US Leading Index May exp -0.4% prev -0.3% (12am)

Times are AEDT. 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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