Morning report

Bank of Melbourne

Friday, 18 June 2021

Equities (close & % change)			Sydney Futures Exchange (close & change)					Interest rates (close & change)		
S&P/ASX 200	7,359	-0.4%		Last		Overnight Chg		**Australia**		
US Dow Jones	33,823	-0.6%	10 yr bond	98.39		0.05		90 day BBSW	0.02	0.00
Japan Nikkei	29,018	-0.9%	3 yr bond	99.57		0.00		2 year bond	0.02	0.01
China Shanghai	3,695	0.2%	3 mth bill rate	99.96		-0.01		3 year bond	0.37	0.11
German DAX	15,728	0.1%	SPI 200	7,305.0		38		3 year swap	0.41	0.00
UK FTSE100	7,153	-0.4%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	1.64	0.10
Commodities (close & change)*			TWI	63.5	-	-	63.3	**United States**		
CRB Index	204.2	-5.9	AUD/USD	0.7611	0.7645	0.7540	0.7555	3-month T Bill	0.03	0.00
Gold	1,773.50	-38.0	AUD/JPY	84.22	84.61	83.07	83.29	2 year bond	0.21	0.00
Copper	9,302.25	-350.0	AUD/GBP	0.5441	0.5464	0.5420	0.5425	10 year bond	1.50	-0.07
Oil (WTI)	71.04	-1.1	AUD/NZD	1.0789	1.0804	1.0744	1.0785	**Other (10 year yields)**		
Coal (thermal)	115.30	1.5	AUD/EUR	0.6346	0.6373	0.6333	0.6344	Germany	-0.20	0.06
Coal (coking)	170.75	0.0	AUD/CNH	4.9005	4.9102	4.8711	4.8786	Japan	0.06	0.01
Iron Ore	208.50	-0.6	USD Index	91.4	92.0	91.3	91.9	UK	0.78	0.04

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: The US dollar continued to appreciate after yesterday's hawkish Federal Reserve meeting. However, US share markets ended mixed and longer-dated US bond yields fell.

Domestically, data yesterday showed jobs surged in May and the unemployment rate fell to pre-COVID-19 levels. It throws into doubt the Reserve Bank's 'mantra' that they will wait until 2024 to raise the cash rate.

Share Markets: US share markets finished mixed, a day after the US Federal Reserve's hawkish tone. The Dow fell 210 points (or -0.6%) and the S&P 500 index ended little changed (down just 2 points). The Nasdaq lifted 122 points (or 0.9%).

In the US tonight, the quarterly event known as "triple witching" occurs, which is when options and futures on indexes and equities expire. This witching event could cause extra volatility.

Interest Rates: Longer-dated US bond prices jumped, bucking the trend in other global bond markets. The US 10-year bond yield dropped 7 basis points to 1.50%. The US 2-year yield rose a touch to 0.21% - the highest rate since June 2022, as financial markets priced a 50% chance to the Us Fed hiking rates by September 2022.

The Australian 3-year bond (futures) yield traded around 0.43%, preserving the gains after the Fed meeting and the very strong Australian jobs data. The Australian 10-year futures yield, however, fell 5 basis points to 1.61%.

Foreign Exchange: The US dollar appreciated against every major currency except the Japanese yen, as expectations the US Fed will raise rates as soon as 2022 boosted demand for the greenback.

The Australian dollar fell sharply against the US dollar after the Fed's hawkish tone the night before. The Australian dollar continued to drift lower, reaching a low of 0.7540 overnight – its lowest since April 1. The jobs data yesterday gave the AUD/USD only temporary respite from the selling. The AUD lifted around 30 pips after the jobs data, but then continued its trend lower versus the USD. The AUD/USD had been stuck in a trading range for the past month, but the Fed has put the cat among the pigeons and pushed the AUD outside of the range to the downside.

Commodities: Oil prices fell overnight, as the US dollar strengthened and as officials in Iran hinted that a deal is close. Iran is holding presidential elections later today. The frontrunner has said he backs nuclear talks. Meanwhile, gold dropped below US$1,800 an ounce.

COVID-19: In Australia, the AstraZeneca vaccine will now only be recommended for use in people aged 60 and over. Previously the vaccine was recommended for people over 50.

Yesterday, NSW recorded 4 additional cases of community transmission.

Australia: Yesterday's jobs data was nothing short of amazing. Jobs surged 115.2k in May, well above the consensus forecast of 30.0k. It more than makes up for the loss of 30.7k jobs in April. What is even more remarkable is that job gains over the twelve months to May summed to 987.2k – just shy of one million and the best on record.

The unemployment rate fell 0.4 percentage points to 5.1% – the lowest rate since December 2019. An unemployment rate with a '4' in front of it is now within reach this year. The Reserve Bank's recent forecasts for unemployment to fall to 5.0% in December 2021 and 4.5% in December 2022 are likely to be reached sooner than anticipated.

Encouragingly, the tightening of the labour market was accompanied by more people re-joining the labour force. The participation rate increased to 66.2%, just shy of a record high.

Other indicators of the health of the labour market were encouraging. The rise in jobs was driven by a record rise in full-time employment of 97.5k. Underemployment fell to a 7½-year low and hours worked rose.

Businesses have been reporting labour shortages. These reports might become more prominent alongside the faster-than-expected tightening in the labour market, although the Reserve Bank is still expecting wages growth to be slow and gradual.

In our opinion the jobs data means the risk of the Reserve Bank (RBA) starting a rate-hike cycle before 2024 has materially increased.

The RBA Governor Lowe delivered a speech yesterday. He said that many businesses are in a cost-control mindset, as feel as they are operating in a very competitive marketplace and have little ability to raise prices. This has resulted in businesses focusing on lowering costs as the only way to increase profits, which in turn makes wages and prices less responsive to economic conditions.

Lowe also talked about labour shortages. He spoke about the two approaches firms could take to deal with these shortages. One is to lift wages. The other is to use non-wage strategies to attract staff, which he said many firms are choosing to use. He added that some firms are also adopting a 'wait and ration' approach, possibly waiting for international borders to open.

Eurozone: The final report for consumer prices in the eurozone showed the annual headline inflation rate unchanged at 2.0% for May. The core annual inflation rate was revised up marginally to 1.0%, but remains very subdued.

New Zealand: GDP rose by 1.6% in the March quarter, following a 1.0% fall in the December quarter. This was well above median consensus expectations of 0.5% growth. From a year earlier, the economy expanded 2.4% against expectations of 0.9% growth. Economic growth continues to be supported by strong domestic activity, especially in housing.

United States: Labour market momentum sagged. New jobless claims reversed direction last week, rising to 412,000 from a revised 375,000, defying consensus for a drop. The jump was concentrated in three states: Pennsylvania, California and Kentucky.

Factory activity in the US mid-Atlantic region declined for the second consecutive month in June after hitting its highest level in nearly half a century in April. The business activity index fell to 30.7 in June, from 31.5 in May and 50.2 in April. Any reading above zero indicates expansion in the region's manufacturing. The employment index rose to 30.7 in June, from 19.3 in May. Additionally, the prices paid index rose for the second straight month to 80.7, from 76.8 in the month prior, its highest reading since June 1979.

The leading index rose 1.3% in May, meeting consensus expectations.

US Treasury Secretary Janet Yellen dismissed the possibility of hyperinflation in the US while saying she's watching price trends carefully. Yellen told a House panel that unemployment benefits are only one reason keeping workers at home, citing childcare and healthcare concerns as other possibilities. She also said the US economy is suffering from a series of supply bottlenecks in semiconductors and lumber and that it is going to be a "bumpy reopening".

Today's key data and events:

JN CPI May y/y exp -0.2% prev -0.4% (9:30am)

JN BOJ Policy Decision June exp -0.10% prev -0.10%

UK Retail Sales May exp 1.5% prev 9.2% (4:00pm)

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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