Morning report

Bank of Melbourne

Wednesday, 1 July 2020

Equities (close & % change)			Sydney Futures Exchange (close & change)					Interest rates (close & change)		
S&P/ASX 200	5,897.9	1.4%			Last		Overnight Chg	**Australia**		
US Dow Jones	25,812.9	0.8%	10 yr bond		99.08		-0.03	90 day BBSW	0.10	0.00
Japan Nikkei	22,288.1	1.3%	3 yr bond		99.71		-0.01	2 year bond	0.25	0.00
China Shanghai	3,128.5	0.8%	3 mth bill rate		99.86		-0.01	3 year bond	0.25	0.00
German DAX	12,310.9	0.6%	SPI 200		5,885.0		-7	3 year swap	0.23	0.00
UK FTSE100	6,169.7	-0.9%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	0.87	-0.01
Commodities (close & change)*			TWI	60.1	-	-	60.0	**United States**		
CRB Index	138.0	0.9	AUD/USD	0.6867	0.6912	0.6833	0.6902	3-month T Bill	0.13	-0.01
Gold	1,781.0	8.1	AUD/JPY	73.86	74.60	73.61	74.48	2 year bond	0.15	0.00
Copper	6,008.3	53.3	AUD/GBP	0.5583	0.5596	0.5564	0.5567	10 year bond	0.66	0.03
Oil (WTI)	39.8	0.1	AUD/NZD	1.0693	1.0718	1.0680	1.0696	**Other (10 year yields)**		
Coal (thermal)	65.3	0.0	AUD/EUR	0.6108	0.6148	0.6096	0.6144	Germany	-0.45	0.02
Coal (coking)	124.1	1.4	AUD/CNH	4.8591	4.8849	4.8374	4.8796	Japan	0.03	0.01
Iron Ore	98.4	1.0	USD Index	97.5	97.8	97.2	97.4	UK	0.17	0.01

Copper, oil, coal & iron ore prices are based on futures pricing. Source: Bloomberg, Thomson Reuters Eikon.
Data as at 7:30am AEST. Change from previous trading day (excluding the SFE which is the change during the night session).

Main Themes: US share markets bounced overnight, amid quarter-end window dressing and rebalancing. It was the best quarter finish since 1987 for the Dow Jones index. The US dollar was weaker and global bond yields were firmer. Investors also focussed on testimony to Congress from Federal Reserve Chair, Jerome Powell. US data showed improvements in manufacturing and consumer confidence while the downturn in the UK economy in Q1 was deeper than first measured.

Share Markets: US share markets jumped, closing out the best quarter since 1998 for the S&P 500 and the best quarter finish since 1987 for the Dow Jones. Investors chose to focus on improving economic data over rising infections. Momentum was only briefly slowed after the US designated Huawei and ZTE national security threats.

Overnight, the Dow Jones closed up 217 points (+0.9%) and the S&P 500 index firmed 47 points (or +1.5%). For the quarter, the Dow Jones jumped 17.7% and the S&P500 rose 20.0%.

Yesterday, the ASX 200 index closed 83 points higher (or +1.4%).

Interest Rates: US 2-year treasury yields initially slipped further to 1.14%, but later firmed to finish unchanged at 0.15%. Meanwhile, the US 10-year yield rose 3 basis points to 0.66%.

Australian 3-year government bond yields remained at 0.29%, while the 10-year yield rose from 0.89% to 0.93%.

Foreign Exchange: The US dollar mostly fell against the basket of G10 currencies, though the yen retreated. The Australian dollar hugged a very narrow trading range of 0.6883-0.6912 overnight. Indeed, the Australian dollar has been consolidating and trading in a tight range within 0.6775-0.6980 for the past three weeks, after marching up from its 17-year low of 0.5510 on March 19 to an 11-month high of 0.7063 on June 10.

Commodities: Most commodity prices gained ground overnight, including oil and gold.

COVID-19: Ten Victorian postcodes have re-entered lockdown from midnight last night. The restrictions will remain in place until at least July 29. International flights coming into Melbourne will also be diverted elsewhere, as Victoria struggles to contain COVID-19.

The European Union (EU) extended its travel ban for US residents, deeming the American response to the pandemic insufficient. The decree, which will be reassessed every two weeks, signalled that the ban will not be lifted until the US controls the spread. The EU will lift restrictions for Chinese residents as of July 1, on the condition that China confirms that the same applies to EU citizens.

The US director of the National Institute of Allergy and Infectious Diseases, Dr Anthony Fauci, warned COVID-19 cases could double to 100,000 per day if US authorities and the public ail to take steps to suppress the pandemic. Fauci also added he is he is "aspirationally hopeful" that a vaccine will be ready in early 2021.

The number of infections rose to 1.4 million in the US overnight, according to Worldometer data. Worldwide infections rose to 10.6 million.

Australia: Credit to the private sector fell by 0.1% in May, the first decline in nine years. The weakness follows a surge in the earlier stages of the pandemic, as businesses and households looked to build buffers.

Business credit declined 0.6% in May; the largest monthly fall since June of 2011. Weak confidence and uncertainty about the outlook are weighing on the demand for credit. The uncertain outlook will continue to limit spending and borrowing for investing.

Housing credit growth remained subdued, with growth at 0.2%. It has held at this pace for two consecutive months. Meanwhile, “other personal” credit continued its run of extreme weakness, as declines in incomes and restrictions to contain COVID-19 have significantly dented household spending.

Payroll jobs and wages continued to stabilise in June, but the pace of recovery slowed. Jobs increased by 1.0% in the four weeks to June 13. However, the pace of recovery has slowed. Payroll jobs rose 0.1% in the two weeks to June 13. It was the weakest fortnightly result since April 25 when the economy remained in the grips of a lockdown.

Reserve Bank (RBA) Assistant Governor Guy Debelle yesterday spoke of the RBA’s bond purchases and the resulting increased liquidity in the system. Debelle said that he did not see any risk of these actions “generating excessively high inflation in the foreseeable future”, and that it was more likely that inflation will remain below the RBA’s target. Debelle also did not see any issue with the capacity of the Government to repay the bonds it had issued to fund debt. He added while the yield on government debt is less than the long-run growth rate in the economy, fiscal sustainability was not an issue because growth in the economy will work to lower government debt.

Debelle also noted the increased growth in deposits in the system, but that some of that increase was likely temporary reflecting businesses drawing down on precautionary lines of credit and putting those funds into deposits.

Debelle noted that the actions were acting to bring down borrowing rates for households, businesses and governments. Debelle said the RBA “stands ready to do more as the circumstances warrant”.

China: Purchasing managers’ indexes for services and manufacturing both improved further in June. The manufacturing index rose from 50.6 in May to 50.9 in June, the fourth consecutive reading above 50. The non-manufacturing index rose from 53.6 in May to 54.4 in June, also the fourth consecutive month above 50. The data is suggesting a further recovery in economic activity after lockdown measures were lifted in February.

China asserted broad new powers over Hong Kong, laying out a new national security law that activists and business groups warned endangered the city’s appeal as a financial hub. The legislation passed by lawmakers in China and signed by President Xi Jinping allows for potential life sentences for crimes including subversion of state power and collusion with foreign forces.

Europe: June consumer price inflation in the euro areas was in line with expectations. Headline CPI rose 0.3% in the year to June and core CPI rose 0.8% over the same period.

Japan: Japan’s jobless rate lifted further from 2.6% in April to 2.9% in May. While seemingly very low by international standards, it was the highest since 2017. A worrying sign is a further decline in industrial production in May, falling 8.4% after a 9.8% decline in April. Industrial production has declined for four straight months. The weakness in industrial output was despite the lifting of the nationwide state of emergency, highlighting the detrimental impact from weak global demand.

New Zealand: Business confidence was revised lower from -33.0 to -34.4 in the final reading for June, but it was still an improvement from May’s result of -41.8 and April’s low of -66.6. Business confidence has improved, but businesses remain cautious about the outlook.

United Kingdom: The UK second estimate for GDP revealed that the economy showed a bigger-than-expected contraction, arriving at -2.2% for the quarter in the first quarter of 2020 versus -2.0% recorded in the first estimate. On an annualised basis, the UK’s economy shrunk 1.7% in Q1, down from a fall of 1.6% in the first reading.

United States: Us Federal Reserve Chair, Jerome Powell, and US Treasury Secretary, Steven Mnuchin, walked a fine line before Congress, welcoming the recent economic rebound while warning the pandemic remains a significant risk.

Fed Chair Powell said the economy's path forward is "extraordinarily uncertain and will depend in large part on the success in containing the virus". And he reiterated that "a full recovery is unlikely until people are confident that it is safe to reengage in a broad range of activities." He did note that incoming data were reflecting a resumption in activity, though he noted the challenges in keeping the virus in check amid the re-openings. He concluded the testimony by reiterating that the Fed is committed to using its full range of tools to support the economy and to help assure that the recovery from this difficult period will be as robust as possible.

The Federal Reserve President of New York, John Williams, spoke overnight. Williams said there have been signs that the US may be past the worst of the extreme economic distress and there are early indications of a recovery starting to emerge. However, he warned the economy is still far from healthy and a full recovery will likely "take years to achieve". During the question and answer session, Williams said he would not say the Fed would never use negative rates as a tool, but said he preferred other tools.

The Conference Board measure of consumer confidence beat estimates (of 91.4) with a rise to 98.1 in June. It is up from 85.9 in May, but remains well below pre-COVID levels. The current conditions index improved from 68.4 to 86.2 and the expectations index lifted from 97.6 to 106.0 in the month. Faced with an uncertain outlook, it is too soon to say that consumers have turned the corner.

The Chicago Fed's purchasing managers' index (PMI) recovered slightly in June to 36.6, after falling to a 38-year low of 32.3 in May. Consensus had expected a stronger improvement. Any reading below 50 indicates worsening conditions. In a special question, more than half of the manufacturers plan a hiring freeze.

Today's key data and events:

NZ Building Permits May prev -6.5% (8.45am)

AU AiG Perf of Manufacturing Jun prev 41.6 (8.30am)

AU CoreLogic Dwelling Prices Jun exp -0.7% prev -0.5% (10.00am)

AU Bldg Approvals May exp -10.0% prev -1.8% (11.30am)

CH Caixin Mfg PMI Jun prev 50.7 (11.45am)

JN Tankan Large Mfg Index Q2 exp -31 prev -8 (9.50am)

US ADP Employm. Jun exp 2850k prev -2760k (10.15pm)

US Constr. Spending May exp 1.0% prev -2.9% (12.00am)

US ISM Mfg Jun exp 49.7 prev 43.1 (12.00am)

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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