Morning report

Friday, 25 February 2022

Equities (close & % change)			Sydney Futures Exchange (close & change)					Interest rates (close & change)		
S&P/ASX 200	6,991	-3.0%		Last			Overnight Chg	**Australia**		
US Dow Jones	33,224	0.3%	10 yr bond	97.76			-0.08	90 day BBSW	0.08	0.00
Japan Nikkei	25,971	-1.8%	3 yr bond	98.29			-0.05	2 year bond	1.16	-0.09
China Shanghai	3,595	-1.7%	3 mth bill rate	99.91			0.00	3 year bond	1.61	-0.10
German DAX	14,052	-4.0%	SPI 200	7,029.0			85	3 year swap	1.91	-0.04
UK FTSE100	7,207	-3.9%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	2.16	-0.11
Commodities (close & change)*			TWI	60.8	-	-	60.5	**United States**		
CRB Index	269.0	0.7	AUD/USD	0.7231	0.7235	0.7095	0.7168	3-month T Bill	0.29	-0.06
Gold	1,902.81	-6.2	AUD/JPY	83.14	83.21	82.01	82.82	2 year bond	1.57	-0.04
Copper	9,910.50	-50.8	AUD/GBP	0.5339	0.5363	0.5311	0.5355	10 year bond	1.96	-0.03
Oil (WTI futures)	93.20	1.1	AUD/NZD	1.0679	1.0729	1.0666	1.0701	**Other (10 year yields)**		
Coal (thermal)	247.00	34.9	AUD/EUR	0.6396	0.6428	0.6378	0.6402	Germany	0.17	-0.06
Coal (coking)	445.33	1.3	AUD/CNH	4.5644	4.5664	4.4904	4.5318	Japan	0.20	0.00
Iron Ore	136.75	-2.0	USD Index	96.23	97.74	96.18	97.07	UK	1.45	-0.03

Data as at 8:00am AEDT. Change from previous trading day (excluding the SFE, which is the change during the night session). Source: Bloomberg.

Main Themes: The Russian invasion of Ukraine has deepened amid reports that Kyiv may fall within hours. The conflict is dominating the attention of financial markets and spurring significant volatility in markets. Investment flows to safer-haven asset classes, such as government bonds increased. It is also leading investors to reassess the economic outlook for world growth and the pace of future tightening from major central banks, as the conflict hits confidence and pushes up commodity prices (especially oil).

Share Markets: Global share markets were very volatile overnight. US markets initially fell significantly, as the war in Ukraine lifts uncertainty about the outlook. However, US share markets reversed their falls and ended the day higher after US President Joe Biden outlined a new round of sanctions against Moscow. The Dow Jones closed up 92 points (or 0.3%), the S&P 500 erased losses of as much as 2.6% to close 63 points (or 1.5%) higher. The Nasdaq shifted from losses of as much as 3.4% during trading to a gain of 3.3% by the close.

The falls were significantly sharper in Europe. The major share indexes in Europe fell between 3% and 4% overnight. Russian equity markets plunged by over 30%.

Interest Rates: Investor fears about the outlook for Europe amid the Russian invasion of Ukraine has led to stronger demand for government bonds. US 10-year bond yields have lost 3 basis points to 1.96%. The US 2-year yield has eased 4 basis points to 1.57%. Investors have now all but ruled out a larger half-percentage-point rate increase at the Fed's March meeting.

Foreign Exchange: The Australian dollar weakened to 0.7095, its lowest level in almost a fortnight against the US dollar as Russia's invasion of Ukraine triggered a flight to safety in global financial markets. However, it subsequently recovered to trade around 0.7168 at the time of writing.

The US dollar rose sharply against a basket of major currencies. The USD Index rose to a high of 97.74, its highest level since June 2020. The index subsequently pulled back to be around 97.07 at the time of writing.

The euro was one of the hardest hit G10 currencies. EUR/USD fell from a high yesterday of 1.1313 to an overnight low of 1.1106. The pound also fell sharply, the GBP/USD pair falling from a high of 1.3550 to a low of 1.3273.

The ruble fell to a record low.

Commodities: Russia's invasion of Ukraine by land, air and sea threatens to disrupt exports of commodities such as grains and oilseeds from both countries. And sanctions against Russia could disrupt energy and metals supplies. Oil jumped above US$100 a barrel for the first time since 2014 before pulling back to around $93.

Gold initially jumped to over $1,974 an ounce on safe-haven demand, its highest level since September 2020, before pulling back to close slightly lower on the day. This follows a sharp run up in gold prices in the leadup to the invasion.

Australia: New private capital expenditure (capex) ticked up 1.1% in the December quarter. This follows a 3.3% decline in the previous quarter, alongside the Delta lockdowns. Investment was still 9.8% higher over the year and spending was broadly in line with pre-pandemic levels.

Machinery & equipment spending edged down 0.1% in the quarter, perhaps reflecting lingering effects from the Delta lockdowns and supply disruption. Spending on buildings rose 2.2% in the quarter.

Capex growth was mixed by region in the quarter. Growth was strongest in the ACT and NSW, while at the same time there were sizeable declines in Tasmania and WA.

Spending plans continue to point to strong growth in investment over the coming years. Estimate 5 for expenditure plans over 2021-22 came in at $140.7 billion, 15.9% higher than Estimate 5 in 2020-21.

The outlook for business investment is robust. Generous tax incentives will continue to bolster investment. Plus, businesses balance sheets are in good shape and businesses remain mildly optimistic despite challenges.

Eurozone: The immediate economic risk from the conflict in Ukraine appears largest for Europe. European Central Bank policymakers convened overnight in a previously scheduled "informal" gathering.

United States: US Federal Reserve officials overnight began taking stock of how the conflict in Ukraine might influence the economy and the shift to tighter monetary policy. Oil and commodity-price shocks and a possible blow to global growth are clear risks. Cleveland's Federal Reserve President Loretta Mester said the implications of the "unfolding situation in Ukraine for the medium-run economic outlook in the US will also be a consideration in determining the appropriate pace" for raising interest rates.

Richmond Fed President Thomas Barkin said the invasion puts the global economy in "uncharted territory". He further said the case for US rate increases remained "robust," but also called the invasion an "unsettling" event that would force policymakers to think through what might happen. He added that the risks could be as obvious as high oil prices weighing on consumer spending and raising inflation even further, or as unknowable as how Russia might respond to US sanctions.

A few hours before the invasion was reported, San Francisco Fed President Mary Daly said that with US inflation as high as it is and the labour market strong, the Fed should go ahead with rate hikes even with the uncertainty of a Ukraine-Russia conflict. But Fed officials may now tread a touch more carefully until the breadth of Russia's actions, and how they affect oil prices, financial markets, and the broader economy, become clearer.

Updated data overnight showed the US economy grew at slightly faster 7.0% annual pace in the fourth quarter. The upgrade was due to higher household spending. It was also led by stronger growth in business investment after businesses rebuilt their stockpile of goods when inventories fell to low levels.

New home sales fell 4.5% to an annual rate of 801,000 units in January, as rising mortgage rates and higher prices sidelined buyers from the market. December's sales pace was also revised higher to 839,000 units from the previously reported 811,000 units. On a year ago, sales tumbled 19.3% after sales peaked at a rate of 993,000 units in January 2021 (which was the highest since the end of 2006).

Manufacturing activity in the central region of the US accelerated in February compared with the previous month, according to a survey from the Federal Reserve Bank of Kansas City released overnight. The tenth district manufacturing survey's composite index rose to 29 in February, from 24 in January. The result was above consensus expectations.

World: Russia formally invaded Ukraine mid-afternoon Sydney time yesterday. Russian President Putin ordered a special military operation to demilitarize the country, targeting Ukrainian military infrastructure.

Ukraine President Zelenskyy confirmed missile strikes had been carried out on infrastructure and border guards, and declared martial law.

Western nations were quick to condemn the action. US President Joe Biden warned that further severe sanctions would follow.

Today’s key data and events:

NZ Trade Balance Jan prev -$477m (8:45am)
NZ Retail Sales Volumes Q4 exp 6.1% prev -8.1% (8:45am)
UK GfK Cons. Sentiment Feb exp -18 prev -19 (11:01am)
EZ M3 Money Supply Jan exp 6.7% prev 6.9% (8pm)
EZ Economic Confidence Feb exp 113.0 prev 112.7 (9pm)
EZ Consumer Confidence Feb Final prev -8.8 (9pm)
US Personal Income Jan (12:30am)
US Durable Goods Orders Jan Prel. exp 1.0% prev -0.7% (12:30am)
US Personal Spending Jan exp 1.6% prev -0.6% (12:30am)
US PCE Core Jan exp 0.5% prev 0.5% (12:30am)
US Pending Home Sales Jan exp -0.5% prev -3.8% (2am)
US UoM Cons. Sent. Feb Final exp 61.7 prev 61.7 (2am)

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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