Morning report

Bank of Melbourne

Friday, 26 February 2021

Equities (close & % change)		
S&P/ASX 200	6,834	0.8%
US Dow Jones	31,402	-1.8%
Japan Nikkei	30,168	1.7%
China Shanghai	3,758	0.6%
German DAX	13,879	-0.7%
UK FTSE100	6,652	-0.1%
Commodities (close & change)*		
CRB Index	194.6	-0.5
Gold	1,771.50	-33.6
Copper	9,428.25	102.3
Oil (WTI)	63.41	0.2
Coal (thermal)	79.60	1.1
Coal (coking)	147.50	0.8
Iron Ore	166.63	1.2

Sydney Futures Exchange (close & change)				
	Last		**Overnight Chg**	
10 yr bond	98.05		-0.22	
3 yr bond	99.64		-0.06	
3 mth bill rate	99.96		-0.02	
SPI 200	6,696.0		-97	
FX Last 24 hrs	Open	High	Low	Current
TWI	65.0	-	-	65.4
AUD/USD	0.7965	0.8007	0.7859	0.7871
AUD/JPY	84.33	84.95	83.51	83.63
AUD/GBP	0.5634	0.5653	0.5611	0.5618
AUD/NZD	1.0696	1.0741	1.0671	1.0677
AUD/EUR	0.6547	0.6556	0.6461	0.6468
AUD/CNH	5.1354	5.1617	5.1039	5.1071
USD Index	90.1	90.3	89.7	90.3

Interest rates (close & change)		
Australia		
90 day BBSW	0.02	0.01
2 year bond	0.13	0.01
3 year bond	0.12	0.00
3 year swap	0.36	0.10
10 year bond	1.73	0.12
United States		
3-month T Bill	0.04	0.00
2 year bond	0.17	0.05
10 year bond	1.51	0.14
Other (10 year yields)		
Germany	-0.23	0.07
Japan	0.15	0.03
UK	0.78	0.05

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 rout in global bonds continued. The US 10-year yield hit its highest level since early last year. Global share markets were spooked by the rise in bond yields. The AUD broke above US 80 cents for the first time in over three years.

Share Markets: The spike in global bond yields spooked global share markets last night. In the US, the Dow fell 560 points (or -1.8%) and the S&P 500 lost 96 points (or 2.5%). The Euro Stoxx 50 index shed 21 points (or -0.6%).

Interest Rates: The bond rout continued overnight (i.e. bond prices lower and yields higher). Yields globally are now at levels last seen before the coronavirus spread worldwide. Indeed, US bond yields continued to climb, despite assurances from US Federal Reserve members that tapering is not on the horizon any time soon. The US 2-year bond yield rose 5 basis points to a three-month high of 0.19%. The US 10-year yield surged to 1.61% - its highest level since February 2020 – before closing at 1.51%, 14 basis points higher on the previous session's close.

Bond markets were spooked by an auction of US 7-year Treasuries, which had the weakest demand in ten years.

Australian 3-year government bond yields (futures) rose from 0.29% to an 11-month high of 0.35% and the 10-year yield rose from 1.72% to 1.95% - the highest since March 2020.

Foreign Exchange: The AUD broke above 80 US cents overnight to reach a high of 0.8007. It is the first time the AUD has been above 80 US cents since 2 February 2018. The AUD/USD did not stay above 0.8000 for long, quickly selling off to 0.7880.

We remain of the view that the AUD/USD will move higher over the near term and medium term. The fundamentals suggest a stronger AUD is likely. A clean break above 0.8045 (a key technical level) suggests that the AUD/USD is headed to the mid 80s area by the middle of this year. The possibility of the AUD flirting with the 90 cent level later this year also opens up. The move higher with the AUD will not be without volatility, especially given the rout in bond markets currently underway.

Commodities: The close for the West Texas Intermediate quote for oil closed at its highest level since January 2019 at US$63.35 a barrel. The rise reflects optimism of swiftly depleting global oil inventories. In the US, crude inventories are near the lowest levels in about a year.

Meanwhile, iron ore prices rose to their highest level in nearly 10 years, supporting a stronger Australian dollar, which broke above US 80 cents overnight.

COVID-19: Queensland's Premier yesterday announced that the state would reopen to Greater Melbourne from 1am Saturday.

Yesterday, Auckland was also declared a hotspot;

quarantine-free travel from the city was suspended.

Elsewhere, Israel has crossed a major threshold with half of the population receiving at least one dose of vaccine. Moderna is recruiting a new chief medical officer and scaling up shot production, while Pfizer-BioNTech are testing the effect of a third dose on variants. On a grimmer note, global fatalities surpassed 2.5 million.

Australia: Business spending on capital equipment picked up in the December quarter as social-distancing restrictions were eased and the economic outlook improved. Private capital expenditure (or capex) increased 3% but remains weak at 7.5% below its level in the same quarter in 2019.

The increase in investment has been directed to equipment and machinery, which was up 5.7% in the quarter. This suggests that government tax incentives introduced in the October Federal budget are feeding through to investment. Investment in buildings and structures was flat in the December quarter.

Average adult weekly ordinary time earnings (or AWOTE) stood at $1,711 or $89,000 per year in November 2020, a rise of 3.2% on a year ago. The separate and preferred measure of wages, the wage cost index, suggests wages growth remains soft.

The remit change from the Reserve Bank of New Zealand (RBNZ) yesterday has prompted news stories from Australian media around why such a shift may not be seen in Australia.

Europe: Several confidence indicators for February were released overnight, including for services, industrial and economic. Each of these indexes recorded an improvement from the previous month.

The European Council's three-day (video) conference is underway with the initial focus on their pandemic response.

New Zealand: New Zealand's Finance Minister Grant Robertson has instructed the RBNZ to consider the impact its monetary policy decisions will have on house prices. The RBNZ's main objectives remain targeting inflation and employment. However, a new clause in its remit will require it to assess the effect of its monetary policy in the context of supporting more sustainable house prices, including dampening investor demand for existing housing stock.

United States: Durable goods orders lifted 3.4% in January, almost three times more than expected by consensus. It is the ninth consecutive increase, boding well for US manufacturing prospects. Core orders, excluding aircraft and defence products, rose 0.5% in January. Orders, excluding transportation, another volatile category, rose 1.4% in the month.

Pending home sales dropped 2.8% in January amid a continued shortage of houses available for sale. Compared to the same time one year ago, pending home sales are 8.8% firmer. Pending home sales have been out of alignment with existing home sales, which have been solid. This misalignment could be due to the different sample sizes.

Manufacturing activity in the tenth US Federal Reserve district, Kansas, expanded in February. Future expectations also lifted. The Kansas Fed index rose from 17 in December to 24 in February, also beating consensus expectations for a reading of 15.

The second reading for GDP in the December quarter of 2020 was revised up to an annualised pace of 4.1%, from the initial estimate of 4.0%. However, the outcome missed consensus expectations, which centred on a revision higher to 4.2%.

There were upward revisions to residential fixed investment and government spending, but this was partly offset by a downward revision to personal consumption expenditure.

Turning to the job market and new unemployment filings produced some cheer. Initial jobless claims fell by more than 100,000 to 730,000 last week. Consensus was for a much less impressive decline to 825,000. Continuing claims also did better than expected, slipping to 4.42 million.

There were more Fed speakers overnight and more reinforcement of the message that easy policy isn't ending any time soon.

The Federal Reserve's Raphael Bostic said that the mandate is full employment not the size of GDP, emphasising that labour market progress has stalled in the past few months.

The Federal Reserve's James Bullard said the spike 10-year Treasury yields reflects growing optimism about the economy but added that the central bank will be less pre-emptive to tighten than in the past.

Today's key data and events:

NZ Trade Jan exp $2.7bn prev $2.9bn (8:45am)
NZ RBNZ Governor Orr Speech (10:30am)
AU Private Sector Credit Jan exp 0.2% prev 0.3% (11:30am)
AU ABS Business Conditions & Sentiments Feb (11:30am)
US Personal Income Jan exp 9.5% prev 0.6% (12:30am)
US Personal Spending Jan exp 2.5% prev -0.2% (12:30am)
US PCE Core Jan exp 0.1% prev 0.3% (12:30am)
US MNI Chicago PMI Feb exp 61.0 prev 63.8 (1:45am)
CH Non-mfg PMI Feb exp 51.8 prev 52.4 (6pm Sun 28 Feb)
CH Mfg PMI Feb exp 51.1 prev 51.3 (6pm Sun 28 Feb)

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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