Morning report

Thursday, 2 December 2021

Equities (close & % change)			Sydney Futures Exchange (close & change)					Interest rates (close & change)		
S&P/ASX 200	7,236	-0.3%		Last		Overnight Chg		**Australia**		
US Dow Jones	34,022	-1.3%	10 yr bond	98.34		0.08		90 day BBSW	0.05	0.01
Japan Nikkei	27,936	0.4%	3 yr bond	98.92		0.02		2 year bond	0.66	0.02
China Shanghai	3,749	0.4%	3 mth bill rate	99.95		0.00		3 year bond	0.93	0.06
German DAX	15,473	2.5%	SPI 200	7,160.0		-79		3 year swap	1.33	0.04
UK FTSE100	7,169	1.5%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	1.73	0.04
Commodities (close & change)*			TWI	60.2	-	-	60.3	**United States**		
CRB Index	218.4	-0.8	AUD/USD	0.7130	0.7173	0.7095	0.7097	3-month T Bill	0.05	-0.01
Gold	1,779.17	4.7	AUD/JPY	80.59	81.48	80.04	80.05	2 year bond	0.55	-0.01
Copper	9,498.25	-24.3	AUD/GBP	0.5360	0.5383	0.5349	0.5349	10 year bond	1.41	-0.03
Oil (WTI futures)	65.32	-0.9	AUD/NZD	1.0444	1.0460	1.0423	1.0426	**Other (10 year yields)**		
Coal (thermal)	152.25	10.1	AUD/EUR	0.6287	0.6329	0.6272	0.6272	Germany	-0.34	0.01
Coal (coking)	307.50	2.2	AUD/CNH	4.5386	4.5679	4.5226	4.5240	Japan	0.07	0.01
Iron Ore	102.35	-1.1	USD Index	95.84	96.14	95.67	96.11	UK	0.82	0.01

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: Financial markets were volatile overnight, as traders assessed the latest Omicron news and more rhetoric on inflation from the US Federal Reserve Chairman.

The Organisation for Economic Co-operation and Development (OECD) back its global growth forecast for 2021 but stuck to its forecast for 2022 whilst flagging the risks with Omicron.

Share Markets: US share markets traded in a volatile fashion overnight. Share markets were in the green during trade, but finished in the red. The Dow Jones fell 462 points (or -1.3%), the S&P 500 index declined 28 points (or -0.6%) and the Nasdaq pulled back 284 points (or -1.8%).

The ASX 200 index bucked the trend in Asian trade yesterday to finish in the red. The ASX 200 lost 20 points (or -0.3%).

Interest Rates: The US yield curve continued to flatten with the US 2-year yield falling by 1 basis point and the US 10-year yield dropped 3 basis points.

The Australian 3-year government bond yield (futures) fell from 1.12% to 1.08%, while the 10-year yield fell from 1.76% to 1.68%.

Interest-rate markets expect the first Reserve Bank rate hike to be in August 2022; there is a probability of 108% attached to an August move. The probability has risen from 89% the day before after stronger-than-expected GDP data was published yesterday.

Foreign Exchange: After breaking under a crucial support level and falling to a 13-month low of 0.7063 early yesterday, the AUD/USD rebounded sharply off this level. This low (0.7063) was within a whisker of the 38.2% Fibonacci retracement level for the rally in the AUD/USD from 0.5510 last March to 0.8007 this February. So, 0.7053 represents another significant support level for the AUD/USD.

The AUD/USD recovered from 0.7063 to 0.7135 and then received an additional injection of demand from the stronger-than-expected GDP data. This data bolstered the AUD/USD to 0.7163.

In our morning report yesterday, we flagged a close above 0.7160 could signal some strength re-emerging for the AUD/USD. The AUD/USD has not yet closed above 0.7160 but the move back above this level is encouraging. The AUD/USD could not hold its head above 0.7160, as USD strength re-emerged, pushing the AUD/USD pair back to the 0.7100 handle.

Commodities: Oil fell as OPEC+ ministers ended their first day of meetings, deferring output talks to Thursday.

COVID-19: Victoria reported 1,179 new COVID-19 cases. NSW recorded 251 cases yesterday, including 6 cases of the Omicron variant. Queensland reported 1 new case.

The World Health Organisation (WHO) said vaccines will probably protect against severe cases of the Omicron variant.

Australia: GDP shrunk 1.9% in the September quarter. It was the third largest fall on record but critically it was less than the 2.7% fall expected by consensus. It was also a lot less than the fall feared when the country was during the lockdowns last quarter.

The fall in economic activity in the September quarter was led by falls in household spending in the lockdown-affected regions of NSW, Victoria and the ACT. Indeed, household spending fell 8.4% collectively in these regions but rose 0.7% in the rest of Australia.

The falls in household spending were most stark for transport services (-41%), hotels, cafes & restaurants (-21%), arts & recreation (-12%).

Industries that are least sensitive to lockdowns and restrictions – mining and agriculture – outperformed. The hardest hit industry was accommodation & food services.

A fall in business spending also drove the fall in GDP in the quarter, as businesses pressed the pause button during lockdown in the big states. Inventories was the other category that dragged output lower.

A very encouraging feature of yesterday's data is the household savings ratio. It surged to nearly 20% to be just shy of the record high posted last year. Consumers are feeling optimistic, which suggests consumers could run down these savings to spend more in the economy.

An economic recovery is now underway in Australia and the next set of national accounts should show growth returned in the December quarter. We expect the economic recovery to ramp up over 2022 and above-trend growth to materialise.

Other data from CoreLogic yesterday showed the housing price boom has continued. Dwelling prices recorded another month of solid, above-average growth of 1.3% in November. However, the monthly pace of growth has slowed from the peak of 2.8% in March. In fact, monthly price growth was at its softest since January.

In annual terms, dwelling prices surged 22.2% in November. Annual price growth has accelerated for 12 consecutive months and is at its highest in over 32 years.

A divergence across regions continued to emerge. Conditions across the most expensive markets are slowing, while growth in the more affordable cities of Brisbane and Adelaide accelerated.

House prices growth has continued to outrun growth of apartment prices. Indeed, the gap between the two using median prices is at its widest ever and especially wide in Sydney.

China: The Caixin manufacturing purchasing manager's index (PMI) fell marginally to 49.9 in November, from 50.6 in October. The fall moves the index back into contractionary territory. However, the outcome was at odds with China's official manufacturing PMI release yesterday, which moved into contractionary territory.

Eurozone: The final Markit reading for the manufacturing PMI was revised lower (like the results for the US and UK) to 58.4, from the preliminary reading of 58.6. The final outcome is up from the 58.3 result in October.

News reports suggest some officials from the European Central Bank (ECB) want to delay a decision on post-pandemic bond purchases to the February 3 meeting. The Governing Council is in agreement to end the Pandemic Emergency Purchase Program (PEPP) in March and a formal decision is still slated for December 16. But given Omicron and the inflation outlook, the decision on how to adjust bond buying could be postponed.

New Zealand: Building consents fell 2.0% over October. It is the second consecutive fall in as many months, following a revised 2.0% drop in September. Despite the monthly fall, approvals are up a record 26.0% compared with a year prior.

United Kingdom: The final Markit reading for the manufacturing PMI was revised lower (like the results for the Eurozone and US) to 58.1, from the preliminary reading of 58.2. The final outcome is up from the 57.8 result in October.

United States: US Federal Reserve Chair, Jerome Powell, warned that the risks of persistent elevated inflation have "clearly risen". Powell was speaking to the House Panel. He stressed that policy "will continue to adapt" to keep rising prices in check, while reiterating that officials will consider speeding up the tapering process. He said he didn't expect the winding down of asset purchases to disrupt markets because the Fed has "telegraphed it."

The Federal Reserve Beige Book said the US economy grew at a "modest to moderate" pace this fall. The Beige Book added that supply-chain issues and labour shortages were holding back growth, despite strong demand. It includes strong consumer spending held back by low inventories.

Furthermore, the Beige Book said that strong demand allowed firms to raise prices with "little pushback" from consumers and increases were widespread throughout the economy.

Payroll processing group ADP reported that private sector jobs grew by 534,000 in November, just ahead of the Bloomberg consensus forecast of a 525,000 total. This data precedes the official non-farm payrolls report on Friday. Consensus expects a rise in payrolls of 545,000 in November, a result that would be above October's outcome of 531,000.

The ISM manufacturing purchasing managers' index (PMI) for November rose 0.3 percentage points to 61.1%. This figure indicates expansion in the overall economy for the eighteenth month in a row after a contraction in April 2020.

The new orders sub index registered 61.5%, up 1.7 percentage points compared to the October reading. The production sub index increased to 61.5%, from 59.3% in October. Meanwhile, the prices index fell 3.3 percentage points to 82.4%.

The report suggests the US manufacturing sector remains in a demand-driven, supply chain-constrained environment. There were some indications of a slight improvement in labour and supplier delivery. But all segments of the manufacturing economy continue to be impacted by very long raw materials and capital equipment lead times, continued shortages of critical lowest-tier materials, high commodity prices and difficulties in transporting products.

In other data, construction spending rose 0.2% in October, rebounding less than expected in October as a decline in homebuilding blunted a surge in outlays on public projects. It follows a dip of 0.1% in September.

The final reading for November for the Markit manufacturing PMI was revised down to 58.3, from the preliminary reading of 59.1. The final result was a touch lower than October's outcome of 58.4, but still indicates expansion in the manufacturing sector in the US lies ahead.

World: The OECD dialled back its global growth outlook for 2021 to 5.6% from 5.7% in September, mainly because of slower expansion in the US, China and Japan than previously predicted. It stuck to the forecast of a 4.5% increase in world GDP for next year, raising the outlook for the US and Japan while trimming it for the euro area and China.

Overnight, the OECD warned Western governments could be forced to bring in fresh emergency financial support for businesses and households if the Omicron coronavirus variant causes a severe global slowdown. The OECD said a renewed wave in the pandemic threatened to add to the existing strain on the world economy from persistently high levels of inflation.

It also added should Omicron prove more transmissible than other variants or more resistant to existing vaccines, it could exacerbate disruption to already battered supply chains and risk driving up inflation for a prolonged period. And further, if it takes a more severe turn, it could also force governments to impose tighter mobility restrictions, hurting demand for goods and services, and leading to a sharp fall in economic activity and lower inflation.

The OECD Chief Economist said there were two scenarios facing the world economy as Omicron adds to the uncertainties in the recovery from the COVID-19 crisis. One is where it creates more supply-chain disruptions and prolongs higher inflation for longer. And the other is where it is more severe and governments need to impose more mobility restrictions, in which case demand could decline and inflation could recede much faster than expected.

Today's key data and events:

NZ Terms of Trade Q3 exp 2.0% prev 3.3% (8:45am)

AU Trade Bal. Oct exp $10.8bn prev $12.2bn (11:30am)

AU Housing Finance Oct (11:30am)

Total exp 4.0% prev -1.4%

Owner Occupier exp 3.0% prev -2.7%

Investor exp 6.0% prev 1.4%

EZ Unemployment Rate Oct exp 7.3% prev 7.4% (9pm)

EZ PPI Oct y/y exp 19.0% prev 16.0% (9pm)

US Initial Jobless Claims w/e 27 Nov exp 240k prev 199k (12:30am)

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.

Besa Deda, Chief Economist
Ph: 02 8254 3251

Contact Listing

Chief Economist
Besa Deda
dedab@banksa.com.au
(02) 8254 3251

Economist
Matthew Bunny
matthew.bunny@banksa.com.au
(02) 8254 0023

Senior Economist
Jarek Kowcza
jarek.kowcza@banksa.com.au
0481 476 436

Associate Economist
Jameson Coombs
jameson.coombs@banksa.com.au
0401 102 789