Morning report

Thursday, 3 March 2022

Equities (close & % change)			Sydney Futures Exchange (close & change)					Interest rates (close & change)		
S&P/ASX 200	7,117	0.3%		Last		Overnight Chg		Australia		
US Dow Jones	33,891	1.8%	10 yr bond	97.82		-0.10		90 day BBSW	0.09	0.00
Japan Nikkei	26,393	-1.7%	3 yr bond	98.41		-0.12		2 year bond	1.01	-0.09
China Shanghai	3,652	-0.1%	3 mth bill rate	99.89		-0.01		3 year bond	1.45	-0.10
German DAX	14,000	0.7%	SPI 200	7,162.0		69		3 year swap	1.78	0.10
UK FTSE100	7,430	1.4%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	2.08	-0.11
Commodities (close & change)*			TWI	60.6	-	-	61.3	United States		
CRB Index	289.1	8.2	AUD/USD	0.7262	0.7307	0.7244	0.7299	3-month T Bill	0.32	0.00
Gold	1,926.98	-18.3	AUD/JPY	83.48	84.44	83.26	84.34	2 year bond	1.53	0.19
Copper	10,198.25	102.8	AUD/GBP	0.5413	0.5465	0.5440	0.5446	10 year bond	1.90	0.17
Oil (WTI futures)	111.34	7.9	AUD/NZD	1.0733	1.0756	1.0719	1.0749	Other (10 year yields)		
Coal (thermal)	446.00	140.6	AUD/EUR	0.6479	0.6567	0.6515	0.6564	Germany	0.03	0.10
Coal (coking)	471.67	8.3	AUD/CNH	4.5869	4.6181	4.5759	4.6144	Japan	0.14	-0.04
Iron Ore	151.90	2.8	USD Index	96.75	97.83	97.29	97.33	UK	1.26	0.13

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 conflict in Ukraine raged on, but the appetite of investors for risk improved. The VIX volatility index – a measure of risk aversion – dropped to 30.4, from 33.3 the day before. However, the measure remains elevated. Hawkish remarks from the US Federal Reserve Chair helped whet appetites for risk.

Oil continued its climb higher – briefly topping US$112 a barrel – the highest in nearly 11 years.

Commodity currencies were firmer overnight, especially the Canadian dollar, after the Bank of Canada (BoC) hiked rates overnight.

Share Markets: The panic selling of shares appeared to be set to be repeated on Europe's open, however, the major equity markets recovered early and closed higher. The Euro Stoxx 50 ended up 1.5%, the UK FTSE 100 +1.4% and the German DAX +0.7%. These gains only recover modestly recent losses.

US share markets climbed after US Federal Reserve Chair Jerome Powell said the Fed will 'proceed carefully' with hikes, emphasising the "need to be nimble in responding to incoming data and the evolving outlook". Powell also noted he backs a quarter-point hike in March and is open to a "series of rate increases" in 2022.

The Dow jumped 596 points (or +1.8%), the S&P 500 rose 85 points (or +2.0%) and the Nasdaq lifted 220 points (or +1.6%).

The ASX 200 eked out a 20 point gain yesterday, despite the sea of red in US and European share

Interest Rates: Global bond yields sprung back overnight. The US 2-year bond yield jumped 19 basis points, after dropping 9 basis points in the previous session. And the US 10-year bond yield spiked 17 basis points, more than fully recovering the 10-basis-point loss from the previous session.

Interest-rate markets are fully priced for a rate hike of 25 basis points from the US Fed later this month.

The Australian 3-year government bond yield (futures) rose from 1.44% to 1.60%, while the 10-year yield rose from 2.04% to 2.16%.

The first Reserve Bank rate hike is fully priced for July 2022 with a probability of 100% attached to a 15 basis point rate hike.

Foreign Exchange: The outperformer overnight was the Canadian dollar after the BoC hiked rates. USD/CAD fell (i.e. CAD appreciated vs the USD) from an overnight high of 1.2750 to a low just under 1.2630.

The AUD/USD was slightly firmer in trade overnight. It didn't receive much of a boost from GDP figures published in Australia yesterday with the result broadly in line with market expectations.

AUD/CAD was left in a narrow trading band overnight of 0.9200-0.9240.

The underperformer overnight against the majors was the JPY. The lift in risk appetites spurred a sell-off in JPY, however, the JPY has not benefitted considerably from safe-haven demand since the Ukraine invasion started. This is unusual for the JPY.

GBP/USD recovered its losses from the previous day, rising to an overnight high of around 1.3400, underpinned by much stronger than expected house prices growth.

However, the EUR/USD continued to languish and fell to a 2-year low of 1.1058 – the lowest since 18 February 2020 – before it lifted modestly from this low.

Commodities: The West Texas Intermediate price for oil briefly topped US$112 a barrel – the highest since 3 May 2011. Oil has lifted more than 20% since the invasion of Ukraine began.

OPEC+ agreed to stick to a gradual output increase of 400,000 barrels per day in April, as widely expected. In the US, crude inventories dropped last week, with imports from Russia falling to zero. China is taking action to shield itself against soaring commodity costs, with officials said to have ordered buyers to scour markets for everything from oil to corn amid concerns of disruptions.

Australia: The latest national accounts yesterday revealed the Aussie economy sprung back into action in the final quarter of 2021. In the December quarter GDP bounced back 3.4%, after a Delta-induced contraction of 1.9% in the previous quarter.

The recovery at the end of 2021 meant the economic expansion for the year printed at 4.2%, a very solid pace. And the economy at the end of 2021 is 3.4% larger than prior to the pandemic.

Consumers armed with ballooning savings and pent-up demand emerged from lockdowns in Australia's most populous states and unleashed spending with a vengeance. Consumer spending drove the recovery. The household savings ratio fell to 13.6%, as household consumption surged 6.3%, piercing the pre-pandemic level for the first time.

Consumers spent big on goods and services and in discretionary areas – especially clothing & footwear (up 42%), transport services, including airline travel (up 49%) and hotels, cafes & restaurants (up 24%). But services spending is not yet back to pre-pandemic levels.

Whilst consumers helped lift the economy from the Delta doldrums, businesses didn't roll up their sleeves and share in the heavy lifting. Business spending shrunk, as did new dwelling construction. Net exports were a drag on GDP and the government sector sat on the sidelines.

The NSW economy led the charge. State final demand in NSW spiked 6.7% - the fastest quarterly rise on record. Activity in Victoria and the ACT also rebounded strongly on reopening from lockdowns; indeed, state final demand in these regions rose to a record high.

Most industries reported a solid gain in activity over the December quarter, led by those hit hardest by the Delta lockdowns. Accommodation & food services posted a 26.1% spike in activity in the quarter, as millions eagerly substituted home-cooked meals for dining out.

There remains upward pressure on input costs and relatedly, domestic prices. The domestic final demand implicit price deflator jumped 1.1% in the December quarter - the fastest quarterly pace in over 13 years - to be up 3.0% in annual terms. These prices pressures are likely to be exacerbated by the developing conflict in Ukraine.

For 2022, we're expecting another leg up in economic output of around 5.5%, although this year isn't without its challenges. The Omicron wave is likely to have sidelined economic activity in the early part of this year. The floods in Queensland will hurt economic activity in large parts of Queensland, before the rebuilding effort adds to activity. And then there are the highly uncertain and fluid developments in Ukraine.

Canada: The BoC raised rates as expected by 25 basis points to 0.50% and highlighted the current strength of the domestic economy, higher inflation, and potential for inflation expectations to drift higher. Furthermore, it was reiterated that inflation is likely to become embedded. However, the BOC flagged the invasion of Ukraine, whilst pushing up inflation pressures, has created a major source of uncertainty. The BoC said the Ukraine conflict will need to be closely followed given the potential impact on global growth.

New Zealand: Building permits plunged 9.2% in January, after a rise of 0.4% in December. It was the biggest decline since February of 2021.

Dwelling prices growth remained elevated, but lost some ground. In the year to February, CoreLogic dwelling prices expanded at a rate of 25.2%, from 27.5% in the previous month.

Russia & Ukraine: Russia's invasion of Ukraine was making progress in the southern part of the country but has stalled outside Kyiv, according to US officials. There was heavy fighting in the second-largest city of Kharkiv and control over the port city of Kherson was in dispute.

US President Joe Biden signalled that he's open to imposing restrictions on Russian oil and gas imports.

And Russia's Deputy Foreign Minister warned that increased weapon supplies to Ukraine raises the risk of an inadvertent conflict with NATO.

United Kingdom: House prices rose by 1.7% in February, which is more than double consensus expectations. Annual growth stepped up to 12.6% in February, from 11.2% in January.

United States: US Federal Reserve Chair Jerome Powell told a House panel that he backs a quarter-point move, but he left open the possibility of a larger hike if inflation remains too hot. He said he will 'proceed carefully' with hikes, emphasising the "need to be nimble in responding to incoming data and the evolving outlook". He acknowledged the uncertainty posed by the war, but said the need to remove pandemic support hadn't changed and is open to a "series of rate increases" in 2022.

Powell's colleagues backed him up: St Louis Fed President James Bullard called for a "rapid withdrawal of policy accommodation," and Chicago Fed President Charles Evans criticised current policy as "wrong-footed" and said some "front-loading" of tightening seems likely.

ADP employment in February was stronger than expected and included a large upward revision to January. Employment rose 475k in February – well above consensus expectations for an outcome of 375k. January's result was revised from a fall of 301k to a jump of 509k. Most job gains were in services and hospitality and in larger firms. Employment declined in small firms.

The ISM manufacturing index rose to 58.6 in February, which is above consensus expectations and follows a reading of 57.6 in January. The prices paid component pulled back slightly to 75.6, from 76.1, but remains elevated.

Economic activity in the US has expanded at a modest to moderate pace since mid January, according to the Federal Reserve's latest Beige Book. It noted that many districts reported that the surge in Covid-19 cases temporarily disrupted business activity, as firms faced heighted absenteeism.

The Fed noted consumer spending was subsequently generally weaker than in the prior report, which was released in early January.

While the Beige Book said manufacturing activity continued to grow at a modest pace, all districts noted that supply chain issues and low inventories continued to restrain growth, particularly in the construction sector.

The report also said employment increased at a modest to moderate pace, although widespread strong demand for workers remained hampered by equally widespread reports of worker scarcity.

With respect to inflation, the Beige Book said prices charged to customers increased at a robust pace across the nation, with a few districts reporting an acceleration in the pace of price growth.

Rising input costs were cited as a primary contributing factor across a broad swath of industries. Labour cost increases and ongoing materials shortages also contributed to higher input prices.

The release of the Beige Book comes two weeks before the Fed's next monetary policy meeting on March 15-16, when the Fed is widely expected to raise interest rates.

Today's key data and events:

AU Building Approvals Jan exp -4.0% prev 8.2% (11:30am)

AU Trade Balance Jan exp $10.4bn prev $8.4bn (11:30am)

CH Caixin Composite PMI Feb prev 50.1 (12:45pm)

CH Caixin Services PMI Feb exp 50.7 prev 51.4 (12:45pm)

EZ PPI Jan exp 2.8% prev 2.9% (7pm)

EZ Unemployment Rate Jan exp 6.9% prev 7.0% (7pm)

US Challenger Job Cuts Feb y/y prev -76.0% (11:30pm)

US Initial Jobless Claims w/e Feb 26 exp 225k prev 232k (12:30am)

US ISM Services Index Feb exp 61.2 prev 59.9 (1:45am)

US Factory Orders Jan exp 0.7% prev -0.4% (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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