Morning Report

Thursday, 5 October 2023

Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	6,890	-0.8%		Last		Overnight Chg		**Australia**		
US Dow Jones	33,130	0.4%	10 yr bond	4.58		-0.10		90 day BBSW	4.14	-0.02
Japan Nikkei	30,527	-2.3%	3 yr bond	4.07		-0.07		2 year bond	4.14	0.05
China Shanghai	3,261	0.1%	3 mth bill rate	4.23		-0.04		3 year bond	4.13	0.04
German DAX	15,100	0.1%	SPI 200	6,943.0		31		3 year swap	4.26	-0.03
UK FTSE100	7,412	-0.8%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	4.66	0.12
Commodities (close & change)*			TWI	59.9	-	-	59.9	**United States**		
CRB Index	275.4	-6.1	AUD/USD	0.6302	0.6343	0.6287	0.6325	3-month T Bill	5.33	0.00
Gold	1,821.35	-1.7	AUD/JPY	93.91	94.40	93.79	94.32	2 year bond	5.05	-0.10
Copper	7,952.50	-50.5	AUD/GBP	0.5218	0.5237	0.5202	0.5212	10 year bond	4.73	-0.06
Oil (WTI futures)	84.41	-4.8	AUD/NZD	1.0666	1.0723	1.0657	1.0699	**Other (10 year yields)**		
Coal (thermal)	148.85	-4.6	AUD/EUR	0.6020	0.6042	0.6010	0.6021	Germany	2.92	-0.05
Coal (coking)	361.00	11.0	AUD/CNH	4.6159	4.6381	4.6092	4.6293	Japan	0.81	0.04
Iron Ore	115.25	-0.2	USD Index	107.07	107.24	106.51	106.79	UK	4.58	-0.02

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

Main Themes: The bond rout took a breather last night as bond yields dropped after hitting some of the highest levels in decades, but this was after a volatile session and large trading ranges. The moves lower in yields were supported by a weaker-than-expected outcome for private sector jobs data, which suggested that the labour market may be cooling across a range of industries. Bond traders pulled back their expectations of further interest rates hikes from the Fed as a result.

Equity investors also breathed a sigh of relief as stock markets closed in the green. The US dollar eased against a basket of major currencies in line with lower interest rates, supporting the Aussie.

Share Markets: Equity investors took solace from lower interest rates and pushed equity prices higher. The S&P 500 ended 0.8% higher and remained above its 200-day moving average at around 4,200 – a technical indicator watched by many market participants. The Nasdaq gained 1.4% and the Dow Jones rose 0.4%.

The ASX 200 fell 0.8% yesterday, extending its run of losses to three consecutive days. 10 of 11 sectors were in the red, with financials, communication services and energy all falling by more than 1% on the day. Utilities was the only sector to record a gain, rising 0.3%. Futures are pointing to a rise on the open, taking the lead from US markets.

Interest Rates: US bond yields declined but only after long-term yields initially jumped to hit levels not seen for decades. The 10-year yield fell 6 basis points, to 4.73%. That was after it rose to a high 4.88% – the highest level since August 2007. The 30-year yield also hit a milestone, breaching 5% for the first time since August 2007. The 30-year yield later fell sharply to close at 4.86%. Short-term yields were also lower – the 2-year treasury yield dropped 10 basis points, to 5.05%. Real interest rates also took a breather, consistent with the recent trend of these bond moves being driven by adjustments to real interest rate expectations, rather than inflation expectations. The US 10-year real yield fell to 2.40%, from a 14-year high of 2.47%.

Interest-rate markets are pricing around a 42% chance of another Fed hike by the end of the year – down from around 52% a day earlier. Around 3.5 cuts are priced out to January 2025.

Australian government bond yields mimicked the moves in the US. The 3-year government bond yield (futures) fell 7 basis points, to 4.07%. The 10-year futures yield dropped 10 basis points, to 4.58%. Interest-rate markets are pricing around a 93% chance of a hike from the RBA by mid 2024. This is down from a more than 100% probability prior to this week's RBA meeting on Tuesday.

Foreign Exchange: The US dollar dropped against other currencies, in line with lower interest rates. The USD Index fell from a high of 107.24 to a low of

106.51, before closing at 106.79.

The Aussie was supported by a lower US dollar but remains under pressure. The AUD/USD pair rose from a low of 0.6287 to a high of 0.6343. It was trading at 0.6325 at the time of writing.

Commodities: Oil prices dropped sharply in line with weaker-than-expected US labour market data adding to concerns around the implications for growth. The West Texas Intermediate (WTI) futures price dropped almost US$5 per barrel, to under US$85 per barrel. Copper, gold, thermal coal and iron ore were also lower. Coking coal moved sharply higher, rising to well above levels hit after Russia invaded Ukraine.

Australia: There were no major data releases yesterday.

Eurozone: Retail sales fell 1.2% in August, following a 0.1% fall in July as higher rates and a slowing economy impact the spending capacity of households. The outcome was lower than the 0.5% drop expected by consensus. In annual terms, sales fell 2.1% to August. Falls were evident across all major categories, with mail orders & internet (-4.5%) and auto fuel & speciality stores (-3.0%) recording the largest monthly falls.

The producer price index rose 0.6% in August, up from a 0.5% fall in July. The outcome was in line with consensus expectations and was the first monthly increase in producer prices in 2023. The result was driven by a 2.5% increase in energy prices. Excluding energy, producer prices fell in the month, down 0.2%.

In annual terms, producer prices dropped 11.5% through the year to August – in line with expectations. This reflects a 30.6% plunge in energy prices from extremely elevated levels a year ago. Excluding energy, producer prices were 1.0% higher through the year.

The September services PMI was finalised at 48.7, not far away from the 48.4 preliminary reading. The result follows a 47.9 reading in August and was the second consecutive month of reading below 50.

New Zealand: The Reserve Bank of New Zealand (RBNZ) left the policy rate unchanged at 5.50%. The move was widely expected, with all 22 economists surveyed by Bloomberg expecting a pause. However, the tone of the statement was more dovish than expected, contributed to a pullback in expectations for future hikes. The statement noted that interest rates “may need to remain at a restrictive level for a more sustained period of time” to bring inflation under control. Inflation is still expected to decline to within the 1-3% target band by the second half of 2024. The statement noted that GDP growth had been stronger than expected in the first half of 2023. Despite this, the RBNZ remains confident that activity will slow sufficiently such that inflation will gradually reduce to the target band. Upside risks remain and interest-rate markets continue to price a 100% probability of another hike by around the middle of 2024. However, this is down from prior to the meeting. Markets also have a 42% chance of a hike in November – down from 62% prior to the meeting.

United Kingdom: The final services PMI reading was revised higher to 49.3 in September, up from 47.2 in the preliminary reading. The outcome suggests that contraction in the services sector was not as material as first reported. Despite the upward revision compared to the preliminary reading, the outcome was the lowest since January and marks the second consecutive month of contraction in the services sector.

United States: Private sector jobs growth, as reported by ADP, surprised to the downside in September. Employment grew by 89k in the month – the fewest since early 2021. The result was well below expectations for 150k. The outcome was also significantly lower than the 180k reading in August. Leisure & hospitality added 92k jobs in the month, while professional & business services were the biggest drag (-32k). The outcome provides support for views that the US labour market is cooling, reducing the chances of further interest rates hikes by the Fed. The release also comes ahead of official payrolls data on Friday. However, the ADP report has been volatile compared to official estimates and has proved to be an unreliable indicator on previous occasions. Investors will be watching for confirmation of this slowdown from official data on Friday.

Services sector activity slowed in September but remained in expansionary territory. The ISM services PMI slipped to 53.6 in September, from 54.5 in August. Readings above 50 indicate expansion. The outcome was in line with expectations, which centred on a 53.5 reading. Employment pulled back to 53.4, from 54.7. New orders recorded a larger fall to 51.8, from 57.5 in August – remaining marginally above 50. Worryingly for the Fed, the prices paid component was unchanged from the previous month, at 58.9. This suggests that inflationary pressures in the services sector are remaining sticky.

Separately, the S&P version of the services PMI was finalised largely in line with the preliminary reading. The September services PMI was finalised at 50.1, compared to the 50.2 flash estimate.

Factor orders in August rose 1.2%, partly reversing a 2.1% drop in the prior month. This was above consensus expectations of 0.3%. Excluding transport, factor orders rose 1.4%, up from a 0.9% gain in July and above expectations of a 0.2% rise.

Durable goods orders for the month of August were finalised slightly below the preliminary reading. Orders grew 0.1% in the month compared to the preliminary estimate of 0.2%. Capital goods orders, excluding defence and aircraft, which are a key leading indicator of business investment, rose 0.9% in August, following a 0.4% fall in July.

Today's key data and events:

AU Trade Bal. Aug exp $7.7bn prev $8.0bn (11:30am)

US Trade Bal. Aug exp -$59.8bn prev -$65.0bn (11:30pm)

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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