Morning Report

Wednesday, 8 November 2023

Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	6,977	-0.3%		Last		Overnight Chg		**Australia**		
US Dow Jones	34,153	0.2%	10 yr bond	4.61		-0.09		90 day BBSW	4.37	0.02
Japan Nikkei	32,272	-1.3%	3 yr bond	4.19		-0.07		2 year bond	4.30	-0.03
China Shanghai	3,205	0.0%	3 mth bill rate	4.42		-0.01		3 year bond	4.24	-0.02
German DAX	15,153	0.1%	SPI 200	6,989.0		-1		3 year swap	4.37	-0.15
UK FTSE100	7,410	-0.1%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	4.70	-0.03
Commodities (close & change)			TWI	61.1	-	-	61.1	**United States**		
CRB Index	275.7	-6.2	AUD/USD	0.6489	0.6501	0.6404	0.6433	3-month T Bill	5.25	-0.01
Gold	1,968.59	-9.6	AUD/JPY	97.33	97.60	96.41	96.78	2 year bond	4.91	-0.02
Copper	8,169.25	59.6	AUD/GBP	0.5257	0.5268	0.5212	0.5233	10 year bond	4.58	-0.07
Oil (WTI futures)	77.45	-3.4	AUD/NZD	1.0881	1.0900	1.0821	1.0839	**Other (10 year yields)**		
Coal (thermal)	120.10	1.1	AUD/EUR	0.6053	0.6069	0.6001	0.6015	Germany	2.66	-0.08
Coal (coking)	330.00	3.0	AUD/CNH	4.7271	4.7335	4.6706	4.6810	Japan	0.88	0.00
Iron Ore	121.70	-1.4	USD Index	105.26	105.78	105.25	105.55	UK	4.27	-0.11

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: US stocks were higher underpinned by a rally in tech. This occurred despite hawkish comments by US Fed officials suggesting that the Fed may still have work to do to ensure inflation returns to target. US bond yields were lower across the curve, the US dollar advanced and oil dropped by almost 4%.

In Australia, equities were down, bond yields were lower (including futures) across the curve and the Aussie was lower against the greenback following the Reserve Bank's (RBA) rate hike.

Share Markets: After a weak start to the session, US equities finished in the green, with tech stocks leading the share market rally. Microsoft shares hit an all-time high and cloud-software shares soared. The Dow Jones closed 0.2% higher, while the S&P 500 rose 0.3% and the Nasdaq climbed 0.9%.

The ASX 200 closed 0.3% lower. Some of the losses recorded in early trade were retraced after the RBA announced its decision to increase the cash rate by another 25 basis points, suggesting that investors took the forward guidance in the policy statement as being more dovish than expected. Six of eleven sectors were lower, led by financials. Futures are pointing to a soft open this morning.

Interest Rates: US treasury yields lower across the curve, particularly lower end yields. The policy sensitive 2-year yield fell by 2 basis points to 4.91%. The 10-year yield fell by 7 basis points to 4.85%.

Interest rate markets now see just a 15% chance of another rate hike from the Fed this cycle. Rate cuts are fully priced for June 2024.

Aussie bond futures followed the lead from the US treasury market. The 3-year (futures) yield fell by 7 basis points to 4.19%. The 10-year (futures) yield fell by 9 basis points to 4.61%.

Following yesterday's rate hike, interest rate markets are pricing in a 50% chance of another rate hike by July next year. Odds for a December hike is virtually zero.

Foreign Exchange: The US dollar index was higher, receiving support from the US bond higher yields. The DXY traded within a tight range - a low of 105.25 to a high of 105.78. It is currently sitting around 105.55.

The Aussie dollar declined against the stronger Greenback. The AUD/USD pair fell following the RBA's decision to increase by another 25 basis points. This suggests that traders may have viewed the forward guidance in the RBA's accompanying policy statement as being more dovish than expected. An unexpected lift in Chinese imports did little to support the Aussie.

The AUD/USD pair fell from a high of 0.6501 to a low of 0.6404 – testing the 0.6400 resistance level. The pair is currently trading near 0.6433.

Commodities: The price of oil dropped by almost 4%. The West Texas Intermediate (WTI) price of oil sitting at around USD77.45 per barrel – the lowest level since July this year.

Australia: The Reserve Bank (RBA) Board raised the cash rate by 25 basis points to 4.35% - the highest rate in 12 years. It was the first increase since June and the third hike in the past eight meetings. This shows that the RBA is clearly in its calibration phase, adjusting the cash rate in line with incoming data, evolving risks, and updated forecasts.

The higher-than-expected inflation read for the September quarter sealed the deal and contributed to an upgrade to the RBA's inflation forecasts. However, the RBA highlighted that upside risks to inflation were broader given ongoing economic resilience and the strength of the labour market.

The RBA's statement noted that progress on inflation "looks to be slower than earlier expected". The RBA expressed concern around the increased risk of inflation remaining higher for longer. The Board opted to hike to be "assured" that inflation returns to target within a reasonable timeframe – a priority.

Progress on inflation has been slower partly because the economy has been more resilient. While household spending has slowed and slowed quickly, other sources of domestic demand have supported activity – namely business investment and infrastructure spending.

Last week we released our Business Snapshot report, which showed that business conditions remained resilient, in part because of the financial buffers built up during the pandemic – these buffers have allowed businesses to invest even though demand has slowed.

Government infrastructure spending has also supported activity, with the Federal Treasurer noting on the weekend that projects may be cut or delayed to ensure that they were not adding to inflationary pressures across the economy.

Notwithstanding today's hike, the RBA is still expecting a soft landing with conditions in the labour market remaining "tight." The RBA expects the unemployment rate to drift higher to 4¼ per cent, down from the previous expectation of 4½ per cent. A comprehensive set of updated forecasts will be released on Friday in the November Statement on Monetary Policy.

What does this mean going forward? The RBA Board retained it tightening bias but did hint at a higher threshold to hike again. This threshold could still be tested, but we don't expect this to occur at the December meeting. The RBA will need more data to decide and a further hike cannot be ruled out in February or beyond.

Today's outcome makes one thing crystal clear - the RBA will not sit on the sidelines, but instead will hike if evidence suggests that inflation will remain higher for longer.

China: The trade surplus fell to USD56.53 billion in October, down from a surplus USD77.71 billion in September. This was much worse than the surplus of USD81.95 billion the market was expecting.

Imports increased by 3.0% over the year to October beating expectations for a decline of 5.0% and improving from a 6.2% fall recorded in September. This was the first annual rise in 13 months suggesting that demand is picking up as stimulus feeds through the economy.

On the downside, exports declined by 6.4% over the year to October – this was worse than the 3.5% fall expected by the market and a deterioration from the 6.2% fall recorded in September. This suggests that global demand is weakening.

Eurozone: German industrial production declined by 1.4% over the month of September, following a 0.1% fall in August. This was much worse than the fall of 0.1% the market was expecting. Industrial output fell for capital goods, intermediate goods, and consumer goods. It marks the fourth consecutive month of falling industrial production, adding to further evidence of weakness in the real economy.

Producer (or wholesale) prices fell by 12.4% over the year to September, following an 11.5% decline in August. This was broadly in line with market expectations. The outcome was driven by falling costs for both energy and intermediate goods. On a monthly basis, producer prices rose by 0.5%, marking the second consecutive month of increase.

United States: The trade deficit widened to USD61.5 billion in September. This was higher than the deficit of USD58.7 billion recorded in August and the deficit of USD59.9 billion expected by the market. Imports were up 2.7% over the month, supported by sales of mobile phones and other household goods. Exports rose by a slower pace of 2.2% over the month, led by sales of other petroleum products, soybeans, crude oil, corn, travel, and transport.

Several US Fed officials spoke overnight, emphasising the need to get consumer prices down to the 2% target. There were also indications that the labour market was becoming better balanced.

Michelle Bowman, member of the Board of Governors of the Fed, reiterated that she expects more hikes - “I continue to expect that we will need to increase the federal funds rate further to bring inflation down to our 2% target in a timely way”.

Neel Kashkari, president of the Minneapolis Fed, said the inflation fight isn’t over yet - “ultimately, the economy will tell us how much is needed to get there. And I just don’t know…I’m not seeing a lot of evidence that the economy is weakening”.

Lorie Logan, president of the Dallas Fed, said tight financial conditions will persist, and thought inflation appeared to be trending towards 3% rather than 2%.

Austan Goolsbee, president of the Chicago Fed, said the top priority is returning inflation to its target - “we’ve got to get inflation down — that’s the No. 1 thing. I’m absolutely hammering that’s what we should be watching”.

Christopher Waller, member of the Board of Governors of the Fed, said the US labour market has been cooling this year, and there was a better balance between the supply and demand for workers.

Today’s key data and events:

EZ Ger. CPI Oct final y/y prev 3.8% (6:00pm)

EZ Retail Sales Sep prev –1.2% (9:00pm)

NZ RBNZ 2yr Inflation Expectations Q4 prev 2.83% (1:00pm)

US Consumer Credit Sep exp $10.0bn prev -$15.6bn (7:00am)

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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