Morning Report

Thursday, 23 March 2023

Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	7,016	0.9%		Last		Overnight Chg		**Australia**		
US Dow Jones	32,030	-1.6%	10 yr bond	3.24		-0.13		90 day BBSW	3.69	0.02
Japan Nikkei	27,467	1.9%	3 yr bond	2.83		-0.13		2 year bond	3.01	0.17
China Shanghai	3,423	0.3%	3 mth bill rate	3.47		-0.09		3 year bond	2.99	0.17
German DAX	15,216	0.1%	SPI 200	6,990.0		-52		3 year swap	3.33	-0.13
UK FTSE100	7,567	0.4%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	3.37	0.18
Commodities (close & change)*			TWI	60.4	-	-	60.4	**United States**		
CRB Index	258.6	1.0	AUD/USD	0.6669	0.6759	0.6660	0.6685	3-month T Bill	4.54	-0.01
Gold	1,970.09	30.0	AUD/JPY	88.38	89.00	87.60	87.87	2 year bond	3.93	-0.23
Copper	8,762.25	61.0	AUD/GBP	0.5459	0.5481	0.5443	0.5450	10 year bond	3.43	-0.18
Oil (WTI futures)	69.94	0.3	AUD/NZD	1.0768	1.0805	1.0736	1.0745	**Other (10 year yields)**		
Coal (thermal)	197.10	0.4	AUD/EUR	0.6193	0.6228	0.6152	0.6158	Germany	2.33	0.04
Coal (coking)	353.00	-0.5	AUD/CNH	4.5856	4.6272	4.5790	4.5865	Japan	0.33	0.08
Iron Ore	121.70	1.4	USD Index	103.21	103.27	102.07	102.53	UK	3.45	0.08

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

Main Themes: Markets were volatile overnight. US equities fell sharply as Treasury Secretary Yellen declared that no consideration had been given to a blanket guarantee for bank deposits, and US Fed Chair Powell said he "just doesn't see" the Fed cutting rates this year.

However, the policy guidance from Fed Chair Powell was also softer. This saw US bond yields decline across the curve. The US dollar declined on the back of the lower yields and a stronger Pound.

A re-acceleration in UK inflationary pressures has economist predicting that the Bank of England (BoE) will increase by another 25 basis points when it meets overnight. There had been speculation that the BoE may have paused, the likelihood of this occurring now is very low.

Global Banking Developments: During her appearance before a US Senate Finance subcommittee, Treasury Secretary Janet Yellen said that the Federal Deposit Insurance Corporation (FDIC) is not considering providing "blanket insurance" for all banking deposits. US regulators will continue to assess bank failures on a case-by-case basis and protect deposits where there a risk of a contagious bank run.

This sent the share prices of US banks down. Aggregate price indices for US Regional Banks declined by around 5.7%, while price indices for larger US banks declined by 3.2%.

The European Central Bank (ECB) is watching for signs of stress in the banking sector from the ongoing financial turmoil.

President Christine Lagarde said the ECB's interest rate hikes may be magnified if banks become more risk averse and start demanding higher rates when lending. This implies that the central bank would need to do less. She said if "banks start to apply a larger 'intermediation wedge' – meaning that at any level of the base rate they demand a higher compensation for the perceived risk they are taking on when lending – then pass-through will become stronger."

The ECB's chief economist, Philip Lane, said the odds of a crisis that completely rewrites the outlook remained long or "pretty much a tail scenario at this point in time."

Share Markets: US share markets were volatile. Shares were up in early trade. However, the tone shifted rapidly when Treasury Secretary Yellen declared that no consideration had been given to a blanket guarantee for bank deposits and US Fed Chair Powell said he just doesn't see the Fed cutting rates this year. The Dow and the Nasdaq ended 1.6% lower, while the S&P 500 ended 1.7% lower.

Yesterday, the ASX 200 rose 0.9 per cent, or 60 points, as investors rushed back to risk assets. The move was the biggest since rising 1.2% in early January.

Interest Rates: US bond yields declined sharply across the curve. This comes on the back of the softening in guidance on future rate hikes. The yield on 2-year bonds declined by a significant 23 basis points, to 3.93%. The 10-year yield declined by 18 basis points, to 3.43%.

Interest-rate markets are currently pricing in 12 basis points of hikes at the Fed's next meeting in May. Markets are now expecting one full rate cut of 25 basis points in September this year. This is at odds with the Fed's own projections.

These sharp moves had implications for Aussie bond yields. The 3-year Australia government bond yield (futures) declined by 13 basis points to 2.83%. The 10-year Australia government bond yield (futures) both declined by 13 basis points to 3.24%.

Interest-rate markets are pricing in a full rate cut by the end of 2023. According to markets, the RBA's hiking cycle has now ended, with the last hike of the cycle occurring in March.

Foreign Exchange: The US dollar declined against a basket of major currencies. Softer guidance on future hikes as well as support for the Pound on the back of the strong inflation read saw the US dollar lose value. The USD index fell to a low of 102.53, before settling at 102.53.

The AUD/USD reached a high of 0.6759 during the New York session. The pair traded between a low of 0.6660 and a high of 0.6759, before settling at 0.6685.

Commodities: Commodities were higher except for coking coal. The West Texas Intermediate (WTI) futures contract closed higher at just under USD 70 per barrel.

Australia: The Westpac-Melbourne Institute Leading Index lifted slightly to -0.94% in February from -1.04% in January. This was the seventh consecutive negative print, pointing to below-trend growth in 2023. Both domestic and international factors drove the outcome with; softening confidence in the labour market; falling commodity prices; and declining US industrial production all contributing to the weak outcome.

United Kingdom: The Consumer Prices Index (CPI) rose by 10.4% in the 12 months to February, up from the 10.1% recorded in January. Core CPI, which excludes volatile price movements, increased by 6.2% over the year to February, up from the 5.8% recorded in January. This was much stronger than the 5.7% the market was expecting. Services inflation, tied to wages growth, drove the upside surprise in inflation. This outcome may see the Bank of England hiking by another 25 basis points when it meets tomorrow. Markets suggest that this outcome all but guarantees that the Bank of England will deliver another 25 basis point hike on Thursday. UK two-year yields jumped on the back of this result while the British pound also increasing.

Eurozone: The current account surplus was €17.1 billion in January 2023, an increase of around €4 billion from the downward revised €13.3 billion current account surplus recorded in January. Surpluses were recorded for services (€14 billion), goods (€11 billion) and primary income (€1 billion).

United States: The US Federal Reserve increased the target for the Fed Funds rate by another 25 basis points. The decision lifts the target range for the Fed's Fund rate to 4.75% - 5.0%. This outcome was expected by most economist and priced in by the market.

In his press conference following the announcement, Federal Reserve Chair Powell, said a pause was considered and acknowledged that the recent banking sector developments "are likely to result in tighter credit conditions for households and businesses and to weigh on economic activity, hiring and inflation".

However, Powell reiterated that the US banking system was fundamentally sound. In addition, the strength of the labour market and elevated inflation meant there was unanimous support for a further rate hike.

The Chair's guidance for future hikes was soften somewhat. He said "additional policy firming may be appropriate" which is a shift from the more definite additional "policy firming will be necessary" which characterised the Fed's previous guidance.

The dot plot, which the Fed uses to signal its outlook for the path of interest rates, remained broadly unchanged. It shows that the median year-end projection for the Feds Funds rate was for one more 25 basis points rate hike. The estimate for the end of 2024 is 4.3%. Powell said that "we just don't" see rate cuts this year – this is at odds with interest rate markets that have firmly priced in cuts this year.

Today's key data and events:

AU RBA Dep Gov Appearance Before the Parliamentary Joint Committee on Corporations and Financial Services
EZ Consumer Confidence Mar (2:00am)
UK BoE Policy Decision exp 4.25% prev 4.00% (11pm)
US Chicago Fed Nat Act Index Feb prev 0.23 (11:30pm)
US New Home Sales Feb prev 7.2% (1:00am)
US Kansas City Fed index Mar prev 0 (2:00am)

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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