Morning Report

Thursday, 13 April 2023

Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	7,344	0.5%		Last		Overnight Chg		**Australia**		
US Dow Jones	33,647	-0.1%	10 yr bond	3.23		-0.01		90 day BBSW	3.65	-0.01
Japan Nikkei	28,083	0.6%	3 yr bond	2.86		-0.01		2 year bond	2.92	0.03
China Shanghai	3,488	0.4%	3 mth bill rate	3.62		0.00		3 year bond	2.91	0.03
German DAX	15,704	0.3%	SPI 200	7,357.0		-3		3 year swap	3.30	-0.06
UK FTSE100	7,825	0.5%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	3.24	0.02
Commodities (close & change)*			TWI	60.2	-	-	60.2	**United States**		
CRB Index	275.7	1.0	AUD/USD	0.6653	0.6723	0.6649	0.6693	3-month T Bill	4.82	-0.04
Gold	2,014.93	11.3	AUD/JPY	88.94	89.36	88.84	89.09	2 year bond	3.96	-0.06
Copper	8,854.50	50.8	AUD/GBP	0.5354	0.5394	0.5349	0.5361	10 year bond	3.39	-0.04
Oil (WTI futures)	83.26	1.7	AUD/NZD	1.0744	1.0780	1.0737	1.0769	**Other (10 year yields)**		
Coal (thermal)	202.40	-2.6	AUD/EUR	0.6097	0.6122	0.6084	0.6089	Germany	2.37	0.06
Coal (coking)	288.33	-0.7	AUD/CNH	4.5873	4.6220	4.5836	4.6044	Japan	0.47	0.01
Iron Ore	117.35	-0.9	USD Index	102.12	102.16	101.45	101.52	UK	3.57	0.03

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: Weaker-than-expected US headline inflation results led to initial sharp falls in bond yields and the US dollar. However, bond yields recovered some of their falls later in the session as investors digested the detail from the US CPI release, which indicated that core inflationary components were still too sticky for the Fed's liking and added weight to the risks of further tightening in May. Equity markets reversed initial gains to close lower by the end of the session.

Share Markets: Equities were initially higher during the trading day but ended lower as investors digested the March US CPI data, which showed that inflationary pressures were reducing, but likely remained still too high. The S&P 500 fell 0.4%, the Nasdaq dropped 0.9%, and the Dow Jones was 0.1% weaker.

The ASX 200 rose 0.5% yesterday. Futures are pointing to mild fall on the open today.

Interest Rates: Bond yields ended the session lower as weaker-than-expected headline inflation flowed through into investor expectations around the probability of future Fed rate hikes. However, there was a large degree of volatility during the day, as investors digested the CPI data and as the core inflationary measures suggested less optimism.

The 2-year bond yield ended 6 basis points lower, at 3.96%. This followed an initially drop to a low of 3.87% shortly after the release of the inflation data. The 10-year bond yield ended 4 basis points lower, at 3.39%, after trading as low as 3.35% during the session.

Interest-rate markets are pricing a 71% chance of another 25-basis-point hike at the upcoming Fed May meeting. However, markets continue to price aggressive cuts later in 2023, with an expected rate of 4.12% in January 2024.

Australian bond yields also declined, but to a lesser degree than in the US. The 3-year and 10-year Australian government bond yield (futures) both fell by 1 basis point, to 2.86% and 3.23%, respectively.

Interest-rate markets continue to price only a small probability of an additional hike from the RBA, with around 8 basis points of hikes priced over the next two meetings. Markets expect rate cuts begin in late 2023, with around 15 basis points of cuts priced to the end of 2023.

Foreign Exchange: The US dollar was sold off sharply on the release of the CPI data and continued to trade around its session lows, even as bond yields recovered some of their initial sharp drops. The USD Index fell from a high of 102.16 to a low of 101.45, before settling at 101.52.

The weaker US dollar contributed to a jump in the AUD/USD pair, the pair rose from a low of 0.6649 to a high of 0.6723 after the release of the inflation data. It later consolidated and settled at 0.6693.

Commodities: Oil prices rose and closed at their highest levels since late 2022. The West Texas Intermediate (WTI) oil futures price rose to USD83.26. Copper and gold were also higher, while coal and iron ore declined.

Australia: There were no major data releases yesterday.

New Zealand: Retail card spending rose 0.7% in March, up from a revised 0.1% fall in February. Looking beyond the retail sector, total card spending was 3.1% higher over the month, following a 1.8% drop in the prior month.

In annual terms, total card spending was up by 16.1% over the year to March.

The monthly gain for total spending reflected an 11.3% surge in non-retail sectors, which includes travel and tour arrangements. Services spending also posted a 2.0% gain. Retail spending was boosted by a recovery in hospitality, which was negatively impacted in the prior month by Cyclone Gabrielle. On the other hand, spending on consumables dropped 1.2%, reflecting an unwind from the impact of households stocking up ahead of the cyclone in the prior month.

United States: Headline inflation, as measured by the consumer price index (CPI) slowed by more than expected in March. The monthly pace of inflation slowed to 0.1% in March, down from 0.4% in February. The annual pace dropped by a full percentage point due to base effects impacting the numbers. Annual inflation dropped from 6.0% in February to 5.0% in March. Both outcomes were below consensus expectations of 0.2% for the monthly read and 5.1% for annual inflation. Continued monthly declines in energy and used car prices, -3.5% and -0.9%, respectively, contributed to disinflation in the headline rate.

Core inflation, excluding the volatile items of food and energy, remained elevated, but was in line with consensus expectations. Core inflation rose by 0.4% in March and 5.6% over the year. This followed a monthly outcome of 0.5% and an annual pace of 5.5% in February. Encouragingly, rent inflation, a very sticky component of inflation, slowed to 0.5% in March, from 0.7% in February. This component is expected to continue to slow as lower advertised rents gradually flow through to the stock of rents.

The reading initially provided positive news that inflationary pressures were receding. However, when looking further into the detail, the numbers showed that key components of core inflation watched by the Fed remained uncomfortably sticky. The 'supercore' measure often referred to by the Fed, which removes shelter costs in addition to food and energy, rose by 0.3% in the month. This was an acceleration from 0.2% over the previous two months and 0.1% per month over October to December. In fact, on a three-month annualised basis, supercore inflation was at 4.4% in March. This remains uncomfortably high for the Fed and adds weight to arguments for an additional hike in May.

The minutes from the Fed's March meeting showed that members engaged in extensive discussion over banking issues and the impacts that may have on the economy. The minutes showed that "developments in the banking sector that had occurred late in the intermeeting period affected their views of the economic and policy outlook and the uncertainty surrounding that outlook." This led to members scaling back their expectations of future rate hikes. Members also stressed vigilance around signs of a credit crunch.

It was noted that the banking issues "increased the already-high level of uncertainty associated with the outlooks on economic activity."

However, following the discussions, all members ultimately supported the policy decision of a further 25 basis point hike. Additionally, the minutes stated that "Some participants noted that given persistently high inflation and the strength of the recent economic data, they would have considered a 50 basis point increase…" had the banking concerns not occurred. Looking forward, members were less convinced around another hike in May.

Around the outlook for inflation, members noted their continued concerns around supercore inflation, stating: "Regarding prices for core services excluding housing, participants agreed that there was little evidence pointing to disinflation in this component. Participants generally judged that some more easing in labor market tightness and slowing in nominal wage growth would be necessary for sustained disinflation."

Updated Fed staff projections included a "mild recession starting later this year, with a recovery over the subsequent two years".

Fed members spoke overnight, with Thomas Barkin noting that "we still have a way to go" to get on top of inflation. Mary Daly sounded a less hawkish tone, suggesting that the economy may be able to slow enough to get inflation down without further hikes being needed.

Today's key data and events:

AU MI Inflation Expectations Apr prev 5.0% (11am)
AU Labour Force Mar (11:30am)
  Employment Change exp 25K prev 64.6k
  Unemployment Rate exp 3.5% prev 3.5%
  Participation Rate exp 66.6% prev 66.6%
CN Exports Mar y/y exp -7.1% prev -1.3% (TBC)
CN Imports Mar y/y exp -6.4% prev 4.2% (TBC)
CN Trade Balance Mar exp US$40.0bn prev US$16.8bn (TBC)
EZ Ger. CPI Mar Final exp 0.8% prev 0.8% (4pm)
EZ Industrial Production Feb exp1.0% prev 0.7% (7pm)
US PPI Final Mar y/y exp 3.0% prev 4.6% (10:30pm)

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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