Morning Report

Friday, 15 December 2023

st.george

Equities (close & % change)		
S&P/ASX 200	7,378	1.7%
US Dow Jones	37,198	0.3%
Japan Nikkei	32,686	-0.7%
China Shanghai	3,102	-0.3%
German DAX	16,752	-0.1%
UK FTSE100	7,649	1.3%
Commodities (close & change)		
CRB Index	258.1	-1.0
Gold	2,035.81	8.1
Copper	8,463.51	217.6
Oil (WTI futures)	71.60	2.1
Coal (thermal)	144.00	-0.8
Coal (coking)	333.50	-0.5
Iron Ore	134.25	0.2

Sydney Futures Exchange (last & change)				
	Last		**Overnight Chg**	
10 yr bond	4.10		-0.03	
3 yr bond	3.75		-0.01	
3 mth bill rate	4.24		-0.01	
SPI 200	7,445.0		47	
FX Last 24 hrs	**Open**	**High**	**Low**	**Current**
TWI	61.1	-	-	61.1
AUD/USD	0.6670	0.6728	0.6656	0.6699
AUD/JPY	95.37	95.51	94.61	94.98
AUD/GBP	0.5282	0.5321	0.5246	0.5248
AUD/NZD	1.0750	1.0816	1.0739	1.0792
AUD/EUR	0.6130	0.6170	0.6090	0.6093
AUD/CNH	4.7618	4.8023	4.7513	4.7711
USD Index	102.90	102.96	101.77	101.93

Interest rates (close & change)		
Australia		
90 day BBSW	4.35	0.00
2 year bond	3.86	-0.17
3 year bond	3.75	-0.19
3 year swap	3.89	-0.04
10 year bond	4.13	-0.15
United States		
3-month T Bill	5.22	-0.01
2 year bond	4.38	-0.04
10 year bond	3.91	-0.10
Other (10 year yields)		
Germany	2.12	-0.05
Japan	0.67	-0.02
UK	3.79	-0.04

Data as at 7:40am AEST. Change is from the previous trading day (excluding the SFE, which is the change during the night session). Source: Bloomberg.

Main Themes: Markets continued to price in more rate cuts in the US in 2024 after the Fed's dovish pivot. There are now six 25-basis point rate cuts fully priced in for next year. Treasury yields continued to fall, led by the longer-end of the curve. The equity market rally continued but lost some steam amid growing speculation that the market has run too far. The US dollar took another sharp leg lower, hitting a fresh 4-month low.

The Bank of England (BoE) and the European Central Bank (ECB) left their policy rates on hold overnight, but moved out of step with the Fed, maintaining their higher for longer rhetoric. Both Central Bank's dug in their heels and pushed back against market pricing for rate cuts.

Share Markets: US equities plumbed fresh 2023 high's overnight but momentum slowed as the knee-jerk reaction to the Fed's policy pivot waned and traders became more cautious of the risk that rate cut pricing had moved too far.

The S&P 500 rose 0.2% and is sitting just 2% shy of its all-time high. The Dow Jones rose 0.3%, while the NASDAQ was the laggard, lifting 0.1%.

The ASX 200 rocketed up by 1.7% yesterday, led by healthcare and materials stocks. All sectors in the index posted gains with 173 of 194 individual stock rising on the day. Futures rose further overnight, pointing to a solid open this morning.

Interest Rates: Treasury yields continued their move down. The 2-year yield reached a low of 4.28%, its lowest level since late May, before rebounding to close down 4 basis points at 4.38%. The 10-year yield dropped 10 basis points to close below 4.0% (3.91%) for the first time since July. The 30-year yield fell further still, shedding 15 basis points to close at 4.03%.

Interest rate markets are fully pricing six rate cuts in 2024, totalling 150 basis points.

Bond yields in the UK and Germany initially slipped sharply at the open following the earlier move in US treasuries. However, yields rebounded following the respective BoE and ECB meetings. The German 2-year Bund closed at 2.55%, 10 basis points lower, while the 2-year Gilt yield fell 4 basis points to 4.33%.

Foreign Exchange: The diverging policy guidance played out in FX markets. The DXY fell, taking another sharp leg lower to its lowest level since August (101.77).

The British Pound jumped from a low of 1.2612 to a near 4-month high of 1.2794. The euro also spiked sharply rising from a low of 1.0874 to a high of 1.1009. The Japanese Yen also hit its highest level against the US dollar since July.

The Aussie dollar strengthened against the US dollar but underperformed on the major crosses, particularly the Pound, euro and Yen. The AUD/USD rose from a low of 0.6656 to a 4-month high of

0.6728 and is currently trading around 0.6699.

Commodities: The International Energy Agency (IEA) slashed its estimates for global oil demand by around 400k barrels per day this quarter. The IEA also expected decelerating demand next year and a 1.2m barrel per day surge in oil production led by non-OPEC producers. The price of oil rose slightly to US$71.6 per barrel.

Australia: Employment growth surprised to the upside again in November, lifting 61.5k. The result follows a sequence of 'hot-and-cold' readings from April to September.

Despite such strong growth in employment, the rise in the participation rate, reflecting both people being drawn into the labour force and continued strong growth in the population, led to the size of the labour force rising by 80.2k in the month. The number of unemployed people rose by 18.8k. The increase in the number of unemployed people relative to the change in the labour force led to the unemployment rate rising to 3.9%, from 3.8%.

There are signs that household income stress is a driving force behind some of the strength in labour supply. Firstly, there is rising participation. The participation rate lifted 0.2ppt to a new record high of 67.2%. Secondly, rising underemployment (up 0.2ppt to 6.5%) highlights a significantly greater demand for work than is currently being met.

Other indicators corroborated the key theme – that growth in labour demand is not keeping up with growth in labour supply. The underemployment, underutilisation, and youth unemployment rates all rose.

The gradual cooling in the labour market is expected to continue into 2024. This comes against a backdrop of still very strong labour supply growth and people looking for more hours. Most of the action is likely to occur in the broader measures of underutilisation that typically receive less attention, such as underemployment.

The Melbourne Institute's consumer inflation expectations measure eased to 4.5% in December, the lowest level since January 2022. This followed a reading of 4.9% in November. This will be welcomed by the RBA who are carefully monitoring the evolution of expectations.

Japan: Core machinery orders rose 0.7% in October, bucking expectations for a 0.4% fall. This followed a strong 1.4% gain in September. In annual terms core machinery orders were down 2.2%, unchanged from the last reading.

October's industrial production numbers were revised higher at final figures. Industrial production rose 1.3% in the month (up from 1.0%) and 1.1% in annual terms (up from 0.9%).

Eurozone: The ECB left its three key policy rates unchanged in December, as widely expected. The press conference following the meeting was where the action happened. ECB President, Christine Lagarde, confirmed that the Governing Council is in no rush to start cutting rates, despite the Fed's decisive pivot yesterday. Lagarde outlined that rate cuts were not discussed at all during the meeting, nor that they wanted to discuss cuts anytime soon.

The Governing Council will bring forward the timing for no longer reinvesting the proceeds of maturing bonds under the pandemic emergency purchase program (PEPP). Over the second half of 2024, the PEPP portfolio will be reduced on average by €7.5bn per month. At the end of 2024, reinvestment of maturing bonds will be discontinued.

New Zealand: The New Zealand economy unexpectedly contracted in the September quarter, falling 0.3%. The economy has moved backwards in three of the last four quarters, taking annual growth to -0.6%. Weakness was centred on the external sector, while domestic demand continued to grow. This was despite a 0.6% slump in consumer spending. The economy is undershooting the Reserve Bank of New Zealand's (RBNZ) growth forecasts, while inflation is also coming down faster than expected. This is bolstering expectations that the RBNZ will shortly pivot towards rate cuts.

United Kingdom: The BoE left the policy rate unchanged at 5.25% in December, as widely expected. However, the messaging in the statement stood in stark contrast to the Fed's meeting yesterday.

The BoE stood firm on its higher for longer messaging and pushed back against market pricing for rate cuts. The voting outcome was telling, 6-3 in favour of keeping rates on hold. The three dissenters voted for another 25-basis point hike - this was unchanged from the last meeting.

Recall yesterday's Fed 'dot-plots' which showed no committee member has another rate hike as their base case. Put simply, the Fed has consensus that rates have likely peaked, while BoE members are not yet convinced.

A pivot from the BoE is inevitable but the timing is unclear. Sticky inflation remains a challenge, but the growth outlook is equally gloomy. Reflecting this the minutes noted that some members perceived the risk of overtightening had increased.

United States: Retail sales surprised to the upside in November, increasing 0.3%. This followed a downwardly revised 0.2% fall in October and beat expectations for a 0.1% fall. Excluding auto vehicles, sales lifted 0.2% after a flat result in October. Retail sales ex autos has been positive or flat for eight consecutive months. The control group, which feeds into the National Accounts, was particularly strong running at double consensus expectations. The control group rose 0.4% in November, accelerating on October's 0.2% reading. The takeaway, consumers are continuing to hold up better than expected.

Both import and export prices eased in November, reflecting the ongoing disinflation pulse. Import prices dropped 0.4% in the months to be 1.4% lower in annual terms. Export prices slipped 0.9% in the month to be 5.2% lower in annual terms. The fall in imports was smaller than expected, while export price falls broadly met consensus.

Business inventories eased 0.1% in October, while September's 0.4% gain was trimmed in half (0.2%) following a sharp revision.

Today's key data and events:

NZ BusinessNZ Mfg PMI Nov prev 42.5 (8:30am)
UK GfK Cons. Sentiment Dec exp -22 prev -24 (11:01am)
CH Industrial Production Nov exp 5.7% prev 4.6% (1pm)
CH Retail Sales Nov y/y exp 12.5% prev 7.6% (1pm)
EZ HCOB Services PMI Dec Prel. exp 49.0 prev 48.7 (8pm)
EZ HCOB Mfg PMI Dec Prel. exp 44.6 prev 44.2 (8pm)
UK Markit Mfg PMI Dec Prel. exp 47.5 prev 47.2 (8:30pm)
UK Markit Serv. PMI Dec Prel. exp 51.0 prev 50.9 (8:30pm)
EZ Trade Balance Oct exp €10.2bn prev €9.2bn (9pm)
UZ NY Empire Mfg Dec exp 2.6 prev 9.1 (12:30am)
US Indust. Production Nov exp 0.3% prev -0.6% (1:15am)
US Markit Mfg PMI Dec Prel. exp 49.5 prev 49.4 (1:45am)
US Markit Serv. PMI Dec Prel. exp 50.7 prev 50.8 (1:45am)

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.

Jameson Coombs, Economist
Ph: +61 401 102 789

Contact Listing

Chief Economist
Besa Deda
dedab@stgeorge.com.au
+61 404 844 817

Senior Economist
Jarek Kowcza
jarek.kowcza@stgeorge.com.au
+ 61 481 476 436

Senior Economist
Pat Bustamante
pat.bustamante@stgeorge.com.au
+61 468 571 786

Economist
Jameson Coombs
jameson.coombs@stgeorge.com.au
+61 401 102 789