Morning Report

Thursday, 18 May 2023

Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	7,199	-0.5%		Last		Overnight Chg		**Australia**		
US Dow Jones	33,421	1.2%	10 yr bond	3.48		0.05		90 day BBSW	3.92	0.01
Japan Nikkei	30,094	0.8%	3 yr bond	3.18		0.06		2 year bond	3.30	0.04
China Shanghai	3,443	-0.2%	3 mth bill rate	3.98		0.03		3 year bond	3.14	0.03
German DAX	15,951	0.3%	SPI 200	7,260.0		40		3 year swap	3.59	0.05
UK FTSE100	7,723	-0.4%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	3.43	0.02
Commodities (close & change)*			TWI	60.7	-	-	60.7	**United States**		
CRB Index	262.3	2.4	AUD/USD	0.6657	0.6673	0.6629	0.6664	3-month T Bill	5.08	0.05
Gold	1,981.88	0.0	AUD/JPY	90.79	91.79	90.68	91.66	2 year bond	4.15	0.07
Copper	8,107.49	-149.8	AUD/GBP	0.5332	0.5347	0.5324	0.5336	10 year bond	3.56	0.03
Oil (WTI futures)	72.83	2.0	AUD/NZD	1.0685	1.0686	1.0631	1.0662	**Other (10 year yields)**		
Coal (thermal)	174.20	4.1	AUD/EUR	0.6129	0.6157	0.6113	0.6146	Germany	2.34	-0.02
Coal (coking)	238.00	0.3	AUD/CNH	4.6579	4.6742	4.6524	4.6701	Japan	0.37	-0.03
Iron Ore	107.75	-0.4	USD Index	102.61	103.11	102.54	102.86	UK	3.84	0.02

Data as at 7:45am AEST. Change is from the previous trading day (excluding the SFE, which is the change during the night session). Source: Bloomberg.

Main Themes: Risk sentiment improved on the back of speculation a small group of negotiators could help break the impasse on raising the debt ceiling.

US President Joe Biden said he had several productive meetings on the debt ceiling with Speaker McCarthy and Congressional leaders. On the back of those meetings, the President said “I’m confident that we’ll get the agreement on the budget and that America will not default,” Importantly, the President noted Congressional leaders agreed there will be no default. Speaker McCarthy called a deal this week "doable."

Equities increased, bond yields were higher, and the US dollar advanced.

Share Markets: Stock markets climbed as investors grew more confident that the US Government would avoid an unprecedented default. Sentiment was also supported by easing concerns over the health of US regional banks with Western Alliance Bancorp reporting growth in its deposits. Western Alliance Bancorp said deposits had grown by more than $2 billion since the end of March.

The S&P 500 and the Dow Jones both closed 1.2% higher. The Nasdaq closed 1.3% higher.

The ASX 200 fell 0.5% yesterday. Seven of the ASX's 11 sectors finished lower, with mining the biggest loser. Futures are pointing to a positive open today.

Interest Rates: Yields on US government bonds increased across the curve as risk sentiment improved. The US 2-year treasury yield rose 7 basis points to 4.15%. The 10-year yield rose 3 basis points to 3.56%.

Interest-rate markets are pricing in around a 20% chance of a hike at the Fed’s June meeting and expect around 60 basis points of cuts by the end of 2023.

The 3-year Australian government bond yield (futures) rose 6 basis points to 3.18%. The 10-year government bond yield (futures) was 5 basis points higher, at 3.48%.

Interest-rate markets are pricing in little chance of another hike in June. Markets expect the cash rate to be around its current by the end of the year. Yesterday’s wage price index outcome had little impact on market pricing.

Foreign Exchange: The AUD/USD pair recovered early losses as sentiment improved on the back of growing confidence the US would not default. The wage price index came in slightly lower than expected (up 0.8% over the March quarter compared with the expected 0.9% gain) which led to an early sell off. The pair increased from a low of 0.6629 to a high of 0.6673, before settling at around 0.6664.

The US dollar strengthened against major currencies. The USD Index rose from a low of

102.54 to a high of 103.11, before falling back to 102.86.

Commodities: Commodities were generally higher, led by oil and coal. Copper and iron ore were down. The West Texas Intermediate (WTI) futures contract closed at US$72.83 per barrel.

Australia: The Wage Price Index (WPI) increased 0.8% over the March quarter to be 3.7% in annual terms. The WPI has now grown at a quarterly rate of 0.8% over the last two quarters - consistent with annual wages growth of around 3.4%.

While the quarterly aggregate rate has stayed unchanged, the composition is shifting in a way we anticipated. Public sector wage growth has accelerated from low levels as more enterprise agreement are renegotiated. On the other hand, private sector wages growth has moderated.

The key question is: will the compositional shift continue, keeping wages growth around 3.5% - 4%? There's reason to believe underlying private sector wages growth will moderate – record growth in migration and the slowdown in household spending should see wage pressures ease.

On the other hand, public sector wages growth should continue to catch up, as governments relax wage caps in a controlled manner (i.e. requiring productivity offsets) and implement one off decisions such as the Fair Work Commission (FWC) aged care decision.

The key unknown is the impact of the FWC minimum wage increase for 2023-24. Unions are asking for an increase of around 7%. The number of people the decision impacts will be as important as the recommended increase. If the decision only impacts minimum wage earners, the aggregate impact could be modest. If it also includes award earners, the aggregate impacts would be larger – last year, minimum wage earners received a 5.2% increase while most award earners received a 4.6% increase; this led the WPI to grow by 1.1% in the September quarter.

Outside of this minimum wage increase, quarterly growth has average 0.8% over the past year – much lower than the rates recorded overseas and relatively subdued compared to history.

Japan: Economic activity expanded by 0.4% over the March quarter, after being flat over the December quarter. The preliminary outcome was stronger than the 0.2% the market was expecting. Household consumption and business investment underpinned the better-than-expected outcome. Economists are of the view that growth will slow over the June quarter on the back of weak external demand and falling real wages that should cap the recovery of household consumption.

Industrial production rose by 1.1% over the month of March. This was stronger than the flash reading of 0.8%. Motor vehicles, production machinery, and chemicals, excluding inorganic, organic chemicals, and medicine drove the outcome. However, on an annual basis, industrial output fell 0.6% in March, the fifth consecutive period of decrease. This shows that underlying momentum in the economy remains subdued.

Eurozone: The consumer price index (CPI) increased by 7.0% through the year to April., confirming earlier estimates. The rate of inflation remained significantly above the European Central Bank's target of 2.0%. Energy prices rebounded by 2.4%, while the cost of services increased by 5.2%. The core index, which excludes volatile items such as food and energy, eased slightly to 5.6% but remained near the all-time high of 5.7% recorded in March. Headline inflation is expected to fall over the rest of 2023, as energy prices are expected to stabilise. Core inflation could prove more persistent, as wage gains keep services inflation elevated.

United States: Housing starts increased by 2.2% to an annual rate of 1.401 million in April, broadly in line with 1.4 million the market was expecting. Data for March was revised lower to 1.37 million from 1.42 million. Single-family housing starts, which account for the bulk of homebuilding, increased 1.6% to a four-month high of 846,000. Starts in buildings with five units or more surged by 5.2% to 542,000.

Building permits decreased by 1.5% to an annual rate of 1.416 million in April. However, there were pockets of strength. Single-family building permits rose 3.1% to an annual rate of 855,000, the highest level since last September. This was offset by permits for housing projects with five units or more, which dropped 9.7% to a rate of 502,000, the lowest level since December 2020.

There are signs the housing market is stabilising, in part due to a fall in average mortgage rates. The average rate on the popular 30-year fixed mortgage has dropped from a peak of 7.08% in November, to around 6.35% last week, according to data from mortgage finance agency Freddie Mac.

Today's key data and events:

AU Labour Force Apr (11:30am)
  Employment Change exp 25k prev 53.0k
  Unemployment Rate exp 3.5% prev 3.5%
  Participation Rate Apr exp 66.7% prev 66.7%
NZ PPI Q1 prev 0.9% (8:45am)
US Philadelphia Fed Index May prev -31.3 (10:30pm)
US Existing Home Sales Apr prev -2.4% (12am)
US Leading Index Apr prev -1.2% (12am

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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