Morning Report

Wednesday, 20 March 2024

Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	7,703	0.4%		Last		Overnight Chg		**Australia**		
US Dow Jones	39,111	0.8%	10 yr bond	4.09		0.00		90 day BBSW	4.35	-0.01
Japan Nikkei	40,004	0.7%	3 yr bond	3.64		0.01		2 year bond	3.82	-0.05
China Shanghai	3,211	-0.7%	3 mth bill rate	4.26		0.02		3 year bond	3.67	-0.06
German DAX	17,987	0.3%	SPI 200	7,715.0		13		3 year swap	3.87	0.00
UK FTSE100	7,738	0.2%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	4.08	-0.03
Commodities (close & change)			TWI	61.4	-	-	61.4	**United States**		
CRB Index	286.9	-0.4	AUD/USD	0.6559	0.6564	0.6504	0.6532	3-month T Bill	5.21	-0.01
Gold	2,157.59	-2.8	AUD/JPY	97.84	98.62	97.58	98.54	2 year bond	4.68	-0.05
Copper	8,910.07	-115.4	AUD/GBP	0.5153	0.5157	0.5126	0.5135	10 year bond	4.29	-0.03
Oil (WTI futures)	83.47	0.8	AUD/NZD	1.0780	1.0795	1.0762	1.0793	**Other (10 year yields)**		
Coal (thermal)	125.10	-2.7	AUD/EUR	0.6030	0.6036	0.5995	0.6012	Germany	2.45	-0.01
Coal (coking)	280.00	-4.0	AUD/CNH	4.7263	4.7299	4.6909	4.7108	Japan	0.74	-0.03
Iron Ore	106.25	-0.4	USD Index	103.57	104.06	103.56	103.81	UK	4.06	-0.03

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

Main Themes: Financial markets overnight continued to react to the Bank of Japan (BoJ) decision to scrap its negative-interest-rate policy (NIRP), yield curve control (YCC) and purchases of exchange-trade funds (ETFs). Markets are also looking ahead to another key central bank meeting – that of the US Federal Reserve.

Share Markets: US share markets rebounded overnight as tech stocks rebounded. The Dow added 0.8%, the S&P 500 increased 0.6% and the Nasdaq jumped 0.4% at the close.

Interest Rates: US bond yields slid across the curve after a $13 billion auction of 20-year bonds drew strong demand. The 2-year yield dropped 5 basis points and the 10-year fell 3 basis points. It also follows a strong sell off in government bonds (i.e. increases in yields) over the previous six sessions where the US 2-year yield gained 26 basis points and the US 10-year yield gained 25 basis points.

In Australia, shorter-dated physical yields dropped after the RBA decision after rising earlier during trade. Financial markets are still fully priced for a rate-cutting cycle to start in September and the futures markets lifted a tad the probability attached to a September cut.

Foreign Exchange: The initial market reaction to the BoJ decision saw USD/JPY appreciate. The AUD/JPY pair also rose and continued to appreciate through overnight trading, that is, the yen came under selling pressures against both the USD and AUD. It perhaps reflected the BoJ Governor suggesting the rate rise may not mean the start of a hiking cycle.

Commodities: Oil rose and gold slipped overnight.

Australia: The Reserve Bank (RBA) left the cash rate on hold at 4.35% yesterday after its board meeting. This surprised no one. Markets and economists alike expected this on-hold decision.

Last meeting the RBA inserted words in the final and most pertinent paragraph of their one-page statement that suggested they were not ruling out further rate rises – maintaining the tightening bias of the statement. This month, they removed those words. It suggests they've tilted more towards a neutral stance. The threshold for another rate hike would still be high in our view and the November rate hike the last in the hiking cycle.

The RBA has effectively come off the playing pitch and is now sitting on the bench watching the game (i.e. the data) and assessing whether they return to the pitch but with a rate-cutting psyche instead. This position is evidenced by the statement saying "the path of interest rates that will best ensure that inflation returns to target in a reasonable timeframe remains uncertain and the Board is not ruling anything in or out".

The RBA Governor in the press conference also said there are "risks on both sides" and the risks are "finely balanced". She also repeated on numerous occasions that the Board "can't rule anything in or out".

The RBA is likely to continue to watch services inflation closely. The latest inflation report shows some early signs it is rolling over, but the RBA reiterated "services inflation remains elevated, and is moderating at a more gradual pace". Bullock referred to services inflation being high overseas, likely a reference to the US where persistent price pressures remain a risk in the services sector.

During the press conference, the Governor was asked about the Fair Work Commission's latest decision to grant aged care workers a further pay increase of up to 14% and the impact this might have on the RBA's wages forecasts and services inflation. The Governor characterised the wage increases as being a worthy increase for a historically underpaid sector that is experiencing labour shortages. The Board will be watching for any potential spillovers to other sectors.

Financial markets are fully priced for rate cuts to start in September this year. The Group view matches this market view. With inflation progressing lower but remaining elevated, the RBA will want to be more convinced of inflation returning to its target band of 2-3% per annum before it comes off the bench to play in the rate-cutting field.

The RBA Governor continues to stress a cautious wait-and-see approach, suggesting rate cuts in the near term are not likely and that they would need to be much more confident of inflation coming back into the band before rate cuts are a serious consideration.

Bullock also took a leaf from the book of her predecessor, Philip Lowe, saying she was a firm believer that the Australian economy is "still on a narrow path", suggesting engineering a soft landing for economic activity whilst bringing inflation back to the band remains in reach.

Eurozone: The ZEW measure of expectations lifted to 33.5 in March, from 25.0 in February.

The annual growth rate of labour costs in the euro area economy slowed to 3.4% in the fourth quarter of 2023, from 5.2% in the third quarter.

Japan: Yesterday the Bank of Japan (BoJ) made history. Japan's central bank ended the most aggressive monetary easing program in modern history by scrapping its negative-interest-rate-policy (NIRP) along with its yield curve control (YCC) mechanism and purchases of exchange-traded funds (ETFs). We flagged the possibility of this in our Weekly published on 11 March.

The BoJ set a new policy rate range of between 0% and 0.1%, shifting from an interest rate of -0.1%. The BoJ said that financial conditions will remain accommodative, suggesting that yesterday's decision does not necessarily mean they're embarking on an aggressive rate-hiking cycle.

It's the first hike from the BoJ in almost 17 years and comes as many major central banks around the world are ending or have ended their rate-hiking cycles and are instead considering when to begin cutting.

Financial markets expected a rate hike was a risk yesterday after the BoJ Governor in recent remarks suggested wages growth would be critical to the decision. On Friday, Rengo, Japan's largest umbrella group for labour unions succeeded in an initial wage increase of 5.28% - the highest rise since the early 1990s – setting up the framework necessary for a near term rate hike.

United States: The Federal Reserve Open Market Committee (FOMC) is expected to keep rates on hold tonight. The markets will focus on the updated dot plot and any guidance from the Fed Chair Jerome Powell on when cuts will start.

Single-family housing starts, which account for the bulk of homebuilding, surged 11.6% to an annual rate of 1.129 million units last month – the highest since April 2022. Data for January was also revised up to show single-family starts falling to a rate of 1.012 million units instead of the previously reported 1.004 million units.

The rebound in housing starts were underpinned by mild temperatures and a persistent shortage of previously owned houses on the market. Despite the hurdle created for many first-time buyers by higher mortgage rates, builders are cutting prices and offering other incentives to increase sales. They are also reducing the size of the homes being built to manage higher material costs.

Please refer to the table of data releases over the page.

Today's key data and events:

NZ Current Account Q4 prev -$11.0bn (8:45am)
EZ Construction Output Jan prev 0.8% (9pm)
US FOMC exp 5.25-5.50% prev 5.25-5.50% (5am)

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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