Morning Report

Wednesday, 1 November 2023

Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	6,781	0.1%		Last		Overnight Chg		**Australia**		
US Dow Jones	33,053	0.4%	10 yr bond	5.00		0.05		90 day BBSW	4.35	0.01
Japan Nikkei	30,859	0.5%	3 yr bond	4.48		0.05		2 year bond	4.46	0.03
China Shanghai	3,165	-0.1%	3 mth bill rate	4.44		0.02		3 year bond	4.40	0.04
German DAX	14,810	0.6%	SPI 200	6,818.0		35		3 year swap	4.64	0.03
UK FTSE100	7,322	-0.1%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	4.93	0.05
Commodities (close & change)			TWI	60.3	-	-	60.3	**United States**		
CRB Index	281.2	0.4	AUD/USD	0.6374	0.6377	0.6315	0.6337	3-month T Bill	5.30	0.00
Gold	1,983.95	-12.1	AUD/JPY	95.04	96.17	94.85	96.14	2 year bond	5.09	0.03
Copper	8,094.00	37.5	AUD/GBP	0.5238	0.5242	0.5209	0.5216	10 year bond	4.93	0.03
Oil (WTI futures)	81.36	-1.0	AUD/NZD	1.0910	1.0914	1.0878	1.0879	**Other (10 year yields)**		
Coal (thermal)	131.10	-6.3	AUD/EUR	0.6003	0.6007	0.5967	0.5992	Germany	2.81	-0.02
Coal (coking)	333.25	-2.8	AUD/CNH	4.6692	4.6745	4.6356	4.6531	Japan	0.95	0.05
Iron Ore	121.95	0.4	USD Index	106.14	106.86	105.91	106.74	UK	4.51	-0.05

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

Main Themes: Stronger-than-expected wage growth data from the US supported a rise in bond yields overnight, while equity markets and the US dollar were also higher. Investors await the outcome of the US Federal Reserve meeting and comments from Fed Chair Jerome Powell in his press conference as the 2-day meeting began.

The Bank of Japan (BoJ) announced a tweak to its yield curve control policy – placing a less rigid cap on 10-year Japanese government bond yields. In Europe, inflation and growth surprised to the downside.

Share Markets: Equity markets were higher despite bond yields rising and robust wages data from the US. The S&P 500 rose 0.6%, the Nasdaq gained 0.5%, and the Dow Jones was 0.4% higher. European equity markets also finished higher, with the Euro Stoxx 50 up 0.8%. The UK FTSE 100 bucked the trend and lost 0.1%.

The ASX 200 rose 0.1% yesterday. Eight of 11 sectors finished up on the day. Real estate led the gains, rising over 1%. Materials was the weakest sector, dropping more than 1%. Futures are pointing to a strong open this morning.

Interest Rates: US bond yields rose across the curve as stronger-than-expected US data supported the case for interest rates to remain higher for longer. The 2-year and 10-year treasury yield both finished 3 basis points higher, at 5.09% and 4.93%, respectively. Interest-rate markets are pricing no chance of hike from the Fed at their meeting. However, markets will be closely watching the statement and press conference for any change in sentiment. Markets have a slightly more than 40% chance of one more hike in this cycle and are pricing just over 3 cuts by January 2025.

Australian government bond yields (futures) broadly mimicked moves in the US. The 3-year and 10-year futures yields both gained 5 basis points, to 4.48% and 5.00% respectively. Interest-rate markets continue to fully price a hike by the RBA by February, with around a 50/50 chance in November. Markets have almost a 70% chance of a second hike by late 2024.

The Japanese 10-year yield rose 5 basis points to 0.95%. This follows the BoJ's announcement that it would alter its yield curve control policy and consider the 1% cap for 10-year bonds as a loose "upper bound" rather than a rigid cap. Markets largely anticipated the decision as bond yields jumped earlier in the day.

Foreign Exchange: The US dollar rose against a basket of major currencies, supported by stronger data and rising bond yields. The USD Index rose from a low of 105.91 to a high of 106.86, before pulling back to 106.74.

The AUD/USD pair fell against a stronger USD but remained in its narrow range. The pair fell from a high of 0.6377 to a low of 0.6315. It was trading at 0.6337 at the time of writing.

The Japanese yen depreciated against the US dollar. The USD/JPY pair rose (i.e. the yen depreciated) to a peak of 151.72 – its highest level in over a year and nearing its highest point in 33 years. This followed the reaction to the BoJ decision and broader overnight moves. It was trading at 151.68 at the time of writing. The depreciation implies that markets were priced for a more hawkish announcement from the BoJ and the yen sold off when the announcement was less hawkish.

Commodities: Oil, gold and coal prices were lower on the day. Copper and iron ore rose.

Australia: Private sector credit expanded 0.5% in September, accelerating on the 0.4% gain in August. This was the fastest monthly increase in private credit in five months. In annual terms, growth continued to moderate (4.9%) but remains around the average of the last 10 years.

The solid result was underpinned by a robust acceleration in business credit, which expanded 0.8% in the month. This followed another strong reading of 0.7% over August. Over the past three months business credit growth has averaged 0.6%. This is a step down from the rapid growth recorded through much of 2022 but it is comfortably above the 10-year average of 0.4%.

Business credit continues to be supported by resilient demand, elevated capacity utilisation and a catch-up in investment following the pandemic. Additionally, strong financial buffers accumulated during the pandemic are giving businesses a strong base to invest and grow.

The underlying pulse of housing credit looks to have settled at a steady pace following a pull-back in recent quarters. Housing credit expanded 0.4% in September, following nine consecutive monthly readings of 0.3%. The current pace is solid given the sharp increase in interest rates.

Demand for housing credit remains strongest for owner-occupiers, where credit grew 0.4% in September. This compares to investor credit growth which printed at 0.2%. Investor and owner-occupier credit accelerated in 3-month average terms, suggesting a slight uptick in momentum.

Other personal credit (e.g. credit cards and personal loans) continued to expand at a solid clip, rising 2.3% over the year to September. This was the largest increase since November 2010. The increase could be an early sign that some households are turning to credit to help with budget challenges. But it could equally reflect the delayed delivery, and financing, of motor vehicles.

Brad Jones, Reserve Bank (RBA) Assistant Governor (Financial System) gave a speech about emerging threats to financial stability over the next decade. His speech outlined six key financial stability risks, three of which could emerge from inside the financial sector and three from outside. Inside risks include rapid deposit runs in the digital age, spillovers from entities that are not individually systemically important, and higher interest rate volatility. Outside risks include geopolitics, operational risks, and climate change. A key point from his speech was that financial stability risks over the next decade are likely to be different to those faced over the previous decade.

China: Manufacturing and services activity indicators surprised to the downside, adding to risks to the outlook for economic growth. The official manufacturing purchasing managers index (PMI) printed at 49.5 in October – below the 50 mark that separates contraction from expansion. This followed a 50.2 outcome in September and was below consensus expectations for an unchanged result. Manufacturing activity has been in negative territory for six of the past seven months. The result demonstrates that the economy continues to face challenges and adds to calls for additional policy support from authorities. Output slowed in the month but remained in expansionary territory (50.9) while new orders slipped into contraction (49.5 in October compared to 50.5 in September). Employment and inventories of raw materials both declined slightly and remained in contractionary territory.

Services sector activity also surprised to the downside. The official services PMI slipped to 50.6 in October, from 51.7 in September. Consensus expectations centred on a 52.0 reading. New orders fell further into contractionary territory (46.7) and have been below 50 for six consecutive months. Input and output prices both moved into contractionary, from expansionary, territory.

Eurozone: Inflationary pressures are slowing faster than expected as the consumer price index (CPI) rose 0.1% in October. This was below consensus expectations for a 0.3% reading and followed 0.3% price growth in September. The weaker-than-expected outcome contributed to the annual pace slowing to 2.9% – the slowest pace in over two years and below consensus expectations of 3.1%. The annual pace slowed materially from 4.3% in September as the numbers were impacted by significant base effects, particularly for energy, which plunged by 11.1% over the year. Food, alcohol & tobacco (7.5%), services (4.6%), and non-energy industrial goods (3.5%) added to inflation over the year.

While headline inflation surprised to the downside, core inflation (excluding food and energy prices) was in line with expectations. Core inflation slowed to 4.2% in the year to October, from 4.5% in the year to September.

Real activity data showed that GDP growth surprised to the downside. GDP contracted 0.1% in Q3, missing expectations for a flat outcome. The reading follows 0.2% growth in the prior quarter. In annual terms, the economy eked out meagre growth of only 0.1% over the year to the third quarter. This was down from 0.5% annual growth in the previous quarter and was below expectations of 0.2% growth.

The weaker-than-expected inflation and growth result supports current market pricing for the European Central Bank to remain on hold and begin cutting rates earlier than other central banks.

Japan: The Bank of Japan (BoJ) left its policy rate unchanged at -0.10%, as widely expected. However, investors were keenly watching communication from the BoJ around its yield curve control policy. This followed some speculation ahead of the meeting that the BoJ may announce significant changes, including allowing bond yields to fluctuate by a larger margin or exiting the policy altogether. The BoJ announced that it would maintain the 10-year bond yield target at 0%, with a 1% upper tolerance band. However, this would be considered a loose "upper bound" rather than a rigid cap, implying that yields may be allowed to trade above this level. The BoJ also dropped its commitment to defend the target by buying an unlimited amount of bonds.

The BoJ also raised its forecasts for inflation for fiscal year 2023 and beyond. It expects inflation of 2.8% in 2023 and 2024, before slowing to 1.7% in 2025. This compares with previous expectations of 2.5%, 1.9%, and 1.6%, respectively.

Industrial production grew by 0.2% in September, following a 0.7% drop in August. The outcome was below expectations, which centred on growth of 2.5%. The weaker-than-expected outcome adds to downside risks for economic growth in Q3. Production was dragged down by weak production machinery output, while automakers reported growth.

The jobless rate fell to 2.6% in September, in line with consensus expectations. The result follows a jobless rate of 2.7% in August.

New Zealand: Building permits fell 4.7% in September, following a downwardly revised 7.0% drop in August. The outcome reflected a fall in multi-dwelling permits, as house approvals rose 0.3% in the month. In annual terms, approvals plunged 20% to 40,408.

Business confidence surged to 23.4 in October, from 1.5 in September. The outcome was the strongest result since June 2017 and was only the second result above zero for over two years. It follows the outcome of the New Zealand election, where the previous Labour government lost power. Most activity indicators accelerated in the month. The surge was driven by the outlook for activity jumping to 23.1, from 10.9 in September. Exports and investment both moved from negative to positive territory in the month. In a positive sign for the inflation outlook, firms' estimates of selling prices in three months went sideways at 2.1%. However, cost growth is expected to be higher, at 3.9%. The survey's measure of inflation expectations remained broadly unchanged, at 4.94%.

United States: The employment cost index rose by 1.1% in Q3. This was up from a 1.0% rise in Q2 and beat expectations for an unchanged result. The reading suggests that wage pressures may be stronger than expected and adds to the recent run of data showing continued economic resilience. Wages & salaries rose 1.2% in the quarter, up from 1.0% in the previous quarter. Compensation growth in the public sector recorded the largest increase, jumping to 1.5% in the quarter from 1.0% in the previous quarter. Compensation growth in the private sector remained unchanged at 1.0%.

House prices continued to rise in August. The FHFA house price index gained 0.6% in the month, beating consensus expectations for 0.5% and following a 0.8% reading in the previous month. Separately, the S&P CoreLogic Case-Shiller 20-city house price index rose 1.0% in the month. This followed a 0.8% gain in the prior month and was above expectations of 0.8%. The annual pace accelerated to 2.2%, from 0.2% in the prior month.

The MNI Chicago PMI remained in contractionary territory for the 14th consecutive month. It came in at 44.0, broadly unchanged from the 44.1 prior reading and below expectations. Price paid rose at a faster pace, while new orders continued to decline, but at a slower pace.

The Conference Board consumer confidence index dropped to 102.6 in October – its weakest reading in five months. This was down from 104.3 in September. However, confidence was above expectations, which centred on a 100.5 reading. Concerns around inflation and high prices continue to weigh on confidence, as did less optimistic views of future business conditions. Views on the present situation and expectations both declined relative to September.

Today's key data and events:

AU CoreLogic Dwelling Prices Oct exp 1.0% pre 0.9% (12:01am)

AU Building Approvals Sep exp 5.0% prev 7.0% (11:30am)

CN Caixin Mfg PMI Oct exp 50.8 prev 50.6 (12:45pm)

Labour Force Survey Q3 (8:45am)

Employment exp 0.4% prev 1.0%

Unemployment Rate exp 3.9% prev 3.6%

Pvt. Wages Ex. Overtime exp 1.0% prev 1.1%

US ADP Employment Chg. Oct exp 150k prev 89k (11:15pm)

US Markit Mfg PMI Oct Final exp 50.0 prev 50.0 (12:45am)

US ISM Mfg PMI Oct exp 49.0 prev 49.0 (1am)

US FOMC Meeting Decision (5am)

Federal Funds Rate exp 5.25% - 5.50% prev 5.25% - 5.50%

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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