Morning report

Bank of Melbourne

Wednesday, 14 February 2024

Equities (close & % change)		
S&P/ASX 200	7,604	-0.1%
US Dow Jones	38,272	-1.4%
Japan Nikkei	37,964	2.9%
China Shanghai	3,004	1.3%
German DAX	16,881	-0.9%
UK FTSE100	7,512	-0.8%
Commodities (close & change)		
CRB Index	273.0	-0.3
Gold	1,992.53	-27.5
Copper	8,138.24	60.9
Oil (WTI futures)	77.72	0.8
Coal (thermal)	124.00	0.5
Coal (coking)	317.00	0.0
Iron Ore	128.50	0.0

Sydney Futures Exchange (last & change)				
	Last		**Overnight Chg**	
10 yr bond	4.29		0.10	
3 yr bond	3.88		0.13	
3 mth bill rate	4.32		0.00	
SPI 200	7,448.0		-104	
FX Last 24 hrs	**Open**	**High**	**Low**	**Current**
TWI	61.0	-	-	61.0
AUD/USD	0.6531	0.6535	0.6443	0.6452
AUD/JPY	97.54	97.61	97.16	97.29
AUD/GBP	0.5172	0.5173	0.5121	0.5125
AUD/NZD	1.0652	1.0693	1.0647	1.0650
AUD/EUR	0.6063	0.6063	0.6021	0.6026
AUD/CNH	4.7138	4.7139	4.6605	4.6675
USD Index	104.12	104.96	103.97	104.88

Interest rates (close & change)		
Australia		
90 day BBSW	4.35	0.00
2 year bond	3.86	0.01
3 year bond	3.77	0.01
3 year swap	4.08	0.12
10 year bond	4.17	0.01
United States		
3-month T Bill	5.23	0.00
2 year bond	4.65	0.18
10 year bond	4.31	0.14
Other (10 year yields)		
Germany	2.39	0.03
Japan	0.73	0.00
UK	4.15	0.09

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

Main Themes: Investors were surprised and risk sentiment soured overnight as US inflation numbers came in stronger than expected, increasing the risk that inflation may prove somewhat sticky and that interest rates cuts would need to pushed out further into 2024. Bond yields rocketed higher following the result, equities were sold off, and the US dollar jumped against major currencies.

Share Markets: Equity markets sold off across the board following the stronger-than-expected US CPI result. The S&P 500 dropped 1.6%, the Nasdaq lost 1.8% and the Dow Jones was 1.4% lower. European markets also lost ground. The Euro Stoxx 50 dropped 1.2%.

The ASX 200 fell 0.1% yesterday. Seven of 11 sectors were in the red. Health care and communication services were the worst performers – each falling by over 1%. Utilities, financials, consumer discretionary, and energy were higher. Futures are pointing to a large drop on the open today, following the movements overnight.

Interest Rates: Interest rates rocketed higher and Fed rate-cut expectations in 2024 were pared back following the stronger inflation print.

The US 2-year treasury yield surged 18 basis points, to 4.65% – its highest level since mid-December. The 10-year yield jumped 14 basis points, to 4.31% – the highest since early December.

Expectations for Fed rate cuts were pared back. Interest-rate markets expect the first cut to be in June, with 25 basis points priced by the June meeting. This is down from 37 basis points of cuts being priced at the June meeting a day earlier. For 2024, markets now expect around 100 basis points of cuts (i.e. four 25-basis-point cuts). This is down from 112 basis points of cuts being priced for 2024 a day earlier.

Australian interest rates broadly mimicked moves in the US, but to a lesser degree. The 3-year Australian bond yield (futures) rose 13 basis points, to 3.88%. The 10-year (futures) yield was 10 basis points higher, at 4.29%. Interest-rate markets are pricing around 45 basis points of cuts from the RBA by the end of 2024, with the first cut fully priced by September.

Foreign Exchange: The US dollar jumped against major currencies. The pair rose from a low of 103.97 to a high of 104.96 – its highest level since mid-November. The pair ended the session not far from this high, at 104.88.

The AUD/USD pair lost ground against the stronger US dollar. The pair dropped from a high of 0.6535 to a low of 0.6443 – its lowest level since mid-November. It was trading near this low – at 0.6452 – at the time of writing.

Commodities: Oil was higher during the session, as was coal and copper. Gold slipped. The compliance of OPEC members is in focus as a report showed that only Kuwait and Algeria implemented previously agreed supply cuts. The International Energy Agency (IEA) predicts demand to rise to 1.2 – 1.3 million barrels per day in 2024, with moderate prices for the year.

Australia: Consumer sentiment jumped 6.2% in February, to 86.0. This was the largest monthly gain in sentiment since April 2023 and took the index up to its highest level since June 2022.

Slowing inflation and the prospect that rates have peaked supported confidence.

The release follows the February Reserve Bank (RBA) Board meeting, where the cash rate was left unchanged at 4.35%. However, the commentary that followed from the RBA was interpreted as hawkish. Specifically, the RBA didn't rule in or out the prospect of any further hikes potentially being needed. Consumers took notice – survey responses after the RBA's decision were materially weaker than those prior to the decision.

All five sub-indices were higher in the month. Views on the time to buy a major household item jumped 11.3%, to 86.8, after being deeply in negative territory through this cycle.

Expectations of economic conditions over the next 12 months and five years were up 8.8% and 4.4%, respectively. Views on family finances also improved, both for the past 12 months and for the next 12 months.

Housing affordability continues to be one of the major issues for households. The time to buy a dwelling index rose in the month but remains at a very weak 74.2. Despite affordability pressures, households continue to expect prices to keep rising as the house price expectations index rose further, hitting a cycle high of 161.4.

Business confidence rose in January to be slightly in positive territory. Confidence came in at +1 index points in the month, up from a neutral reading (i.e. 0 index points) in December. Confidence has been hovering around the neutral level for over a year.

Business conditions continued to slide, falling to +6 index points in January, from +8 in December. Conditions are being impacted by the continued slowing in the economy, as tight monetary policy negatively impacts aggregate demand. Despite the fall, conditions remain around average levels compared to the history of the series.

All three sub-indices – trading, profitability, and employment – fell in the month. Trading conditions have now been below average for two consecutive months. Profitability remains around average. In contrast, employment conditions remain above average, in line with the still robust – but slowing – labour market.

Forward orders – a key leading indicator – rose in January but remained in negative territory.

Cost pressures generally rose in the month. Growth in purchase costs and final prices was higher in January, while labour cost growth was unchanged from the December reading. While higher in the month, cost pressures have been trending lower for many months and one month of acceleration does not indicate a trend. The result is unlikely to be of major concern for the RBA at this stage, but the evolution of prices will continue to be closely watched through 2024.

Eurozone: The ZEW expectations survey rose in February to 25.0. This was up from a 22.7 reading in January. The survey has been trending higher over the second half of 2023 and has been in positive territory for five consecutive months.

United Kingdom: Labour market data surprised to the upside, suggesting that the labour market remains tight. The unemployment rate for the December quarter fell to 3.8%. This followed a 3.9% reading for the three months to November and was below expectations of a rise to 4.0%.

Other labour market indicators also suggested continued robustness. Employment rose 72k in the three months to December – down from the previous reading of 108k but above expectations for a larger slowdown to 50k.

Wages growth also slowed but was still stronger than expected. Average weekly earnings slowed to 5.8% in annual terms in the December quarter. This was down from 6.7% in the previous reading but above expectations for a larger fall to 5.6%.

United States: The January inflation reading was stronger than expected, suggesting that getting inflation back to the Fed's 2% is likely to be a bumpy process and may take some time.

The monthly headline inflation read came in at 0.3% for January, up from a downwardly revised 0.2% reading in December (initially reported as 0.3%). The result was above consensus expectations of 0.2%. This meant that the annual pace remained above 3% in January. The annual reading came in at 3.1%. This was down from a 3.4% annual reading in December but above expectations of 2.9%.

More importantly, core inflation (excluding food and energy) – which the Fed monitors closely –

accelerated in the month. The monthly pace of core inflation rose to 0.4% in January, above December's reading and expectations – both of which were 0.3%. This resulted in the annual pace in January remaining unchanged at 3.9% from its December result, above expectations of 3.7%.

Today's key data and events:

EZ GDP Q4 exp 0.0% prev 0.0% (9pm)
EZ Industrial Production Dec exp -0.2% prev -0.3% (9pm)
UK CPI Jan exp -0.3% prev 0.4% (6pm)

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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