Morning Report

Thursday, 1 February 2024

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Equities (close & % change)			Sydney Futures Exchange (last & change)					Interest rates (close & change)		
S&P/ASX 200	7,681	1.1%		Last		Overnight Chg		**Australia**		
US Dow Jones	38,150	-0.8%	10 yr bond	4.02		-0.01		90 day BBSW	4.35	0.00
Japan Nikkei	36,287	0.6%	3 yr bond	3.53		-0.01		2 year bond	3.68	-0.15
China Shanghai	2,923	-1.5%	3 mth bill rate	4.25		-0.01		3 year bond	3.57	-0.15
German DAX	16,904	-0.4%	SPI 200	7,559.0		-84		3 year swap	3.75	-0.18
UK FTSE100	7,631	-0.5%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	4.01	-0.13
Commodities (close & change)			TWI	61.6	-	-	61.6	**United States**		
CRB Index	272.4	-1.6	AUD/USD	0.6601	0.6623	0.6552	0.6561	3-month T Bill	5.20	0.00
Gold	2,036.53	-0.5	AUD/JPY	97.44	97.47	96.45	96.56	2 year bond	4.23	-0.11
Copper	8,543.75	57.3	AUD/GBP	0.5200	0.5201	0.5174	0.5177	10 year bond	3.93	-0.11
Oil (WTI futures)	75.81	-2.0	AUD/NZD	1.0762	1.0767	1.0724	1.0733	**Other (10 year yields)**		
Coal (thermal)	118.10	-2.4	AUD/EUR	0.6088	0.6093	0.6061	0.6070	Germany	2.17	-0.10
Coal (coking)	318.00	1.0	AUD/CNH	4.7454	4.7525	4.7103	4.7158	Japan	0.73	0.02
Iron Ore	130.35	0.6	USD Index	103.41	103.74	102.94	103.63	UK	3.79	-0.11

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: US stocks ended firmly in the red as Fed Chair Powell pushed back on the idea of a March rate cut, noting that it would only be appropriate to cut when the Fed gained greater "confidence that inflation is moving sustainably toward 2%."

US Treasury yields dropped following the softer than expected US labour market data and concerns around the health of regional banks. These falls were partly retraced as the Fed's decision and commentary was less dovish than expected. The US dollar was higher, oil fell and gold dipped.

Share Markets: US stocks ended firmly in the red as the Fed's decision and commentary was less dovish than expected. In addition, the shares of big technology companies declined sharply on the back of weaker than expected earnings. There was also concerns around regional banks with NY Community Bancorp falling 46% after reporting "game-changing" losses due to higher loan-loss provisions.

The S&P 500 ended 1.6% lower, the Dow Jones lost 0.8% and the tech heavy Nasdaq lost a large 2.2%.

The ASX 200 gained 1.1% yesterday, closing at a fresh record high. The rally was led by financials, with all sectors finishing in the green. Futures are pointing to a weak open today.

Interest Rates: US bond yields ended lower across the curve but were volatile. The 2-year treasury yield declined 11 basis points to 4.23%. The 10-year yield was 11 basis points lower, at 3.93%.

Interest-rate markets are attaching a 35% chance to a March cut. To the end of 2024, markets are pricing around 140 basis points of cuts, with the first cut fully priced in for May this year.

Australian Government bond yields ended lower following the release of the weaker than expected inflation read. The 2-year bond yield declined by 15 basis points and the 10-year bond yield fell 13 basis points.

Futures slipped further overnight. The 3-year Australian government bond yield (futures) declined by 1 basis point to 3.53%. The 10-year (futures) also declined by 1 basis point to 4.02%.

Interest-rate markets continue to price no chance of a hike from the RBA in February and 65 basis points of cuts by the end of 2024 – this is up from less than 50 basis points of cuts yesterday. The first cut is now expected in June and not August.

Foreign Exchange: The US dollar ended the session higher after swinging between gains and losses. The USD Index ranged between a low of 102.94 and a high of 103.74, before moving to 103.63 at the time of writing.

The AUD/USD pair fell towards 0.6560 after initially rising above 0.6600. With the US dollar receiving yield support given Australia's soft inflation read and US Fed commentary, the pair remains under pressure. The pair ranged between 0.6552 and 0.6623 and was trading at 0.6561at the time of writing.

Commodities: Oil prices declined with the West Texas Intermediate (WTI) futures price falling to US$75.81.

Australia: The moderation in inflation is occurring more quickly than expected. Headline inflation advanced by 0.6% over the December quarter, the slowest rate in almost three years. In annual terms inflation is running at 4.1%, much lower than the 4.5% the Reserve Bank (RBA) was expecting. The trimmed mean measure, which excludes the smallest and largest price movements, moderated to 4.2%, again lower than the 4.5% the RBA was expecting.

The global disinflationary impulse has arrived. For the first time in three years, the prices of globally traded goods declined. Tradable inflation fell by 0.4% over the quarter, to be 1.3% higher in annual terms. The prices of household goods, fuel, clothing all fell over the quarter.

Growth in some domestic prices continue to remain elevated, including the cost of dwelling construction, rents, and insurance. More broadly we are seeing growth in prices across market services slow. We expect this to continue as growth in the population eases – there will be less pressure on rental markets and the capital stock will catch up to the increase in labour supply, boosting labour productivity, and reducing unit labour costs.

At the same time, recent activity indicators make clear that monetary policy is working and spending is slowing – this will limit the pricing power of businesses.

Today’s release also confirmed that Australia’s disinflationary journey is on par with that of our global peers. We expect inflation be running at 3.2% over 2024 in both headline and core terms. Today’s outcome suggests that there are some downside risks to these forecasts. It also suggests that when the RBA reviews their forecasts, they could even start to tilt the balance of risks for inflation to the downside with the potential for inflation to be back to around the mid-point of the band within their forecast horizon.

Private sector credit expanded 0.4% in December, to finish the year 4.8% higher. Credit growth struck a consistent rhythm in 2023, growing at 0.3%-0.4% in nine of the twelve months of the year. The annual pace represents a relatively solid growth rate; nothing to ring home about, but certainly a resilient number given the underlying economic backdrop.

Business credit growth remains solid. It expanded 0.5% in December, growing 6.6% through the year. Over the second half of 2023 business credit grew at an annualised rate of around 6.9%, well above the 10-year average of 4.7%. This was also stronger than the first half of 2023, where credit expanded at an annualised pace of 6.3%.

Robust growth in business credit reflects solid investment activity, as businesses look to expand capacity for a growing population, accelerate technological adoption and replenish their capital stock. Surveyed investment intentions and capacity utilisation remain strong, pointing to further resilience in business borrowing.

Housing credit rose 0.4% in December and 4.1% in annual terms. The expansion in housing credit has run at a steady pace, growing 0.4% consecutively over the last four months of 2023. The rate of growth is a little below par compared to the 10-year average of 5.7%, but it is still respectable given affordability pressures from higher interest rates and elevated dwelling prices.

A steady pace of credit expansion is likely to continue over the first half of 2024, given there is no clear catalyst for a big shift from here. The second half of the year could see credit appetite take another leg higher alongside legislated tax cuts and a possible easing in monetary policy.

China: The Manufacturing Purchasing Managers' Index (PMI) was at 49.2 index points in January, edging higher from the 49.0 index points recorded in December. The outcome was in line with market expectations. It was the fourth straight month of contraction in factory activity. There were falls in new orders, foreign sales, and employment. Input cost eased to a seven-month low, with output prices falling further.

The Non-manufacturing PMI edged up to 50.7 index points in January 2024, from 50.4 index points in December. The outcome was in line with market expectations. It was the thirteenth straight month of expansion in services activity. Input cost fell for the fourth successive month while output prices decreased further.

United Kingdom: House prices rose by 0.7% in January, stronger than the flat outcome recorded in December and better than the 0.1% the market was expecting. Demand has received a boost from mortgage rates edging lower, as markets have generally revised down expected future interest rates.

New Zealand: The Business Outlook Index jumped to 36.6 index points in January, from 33.2 points in December. Own activity outlook remained relatively solid but there were further declines in intentions for investment and employment. Inflation expectations were lower, but expectations held up for costs and output price.

United States: The US Fed left its policy interest rate target unchanged at 5.25 – 5.50%. In the policy statement accompanying the decision, the Fed dropped its tightening bias for the first time this hiking cycle, leaving out language of a possible hike. This is because the Fed now sees risks to achieving employment and inflation goals as "moving into better balance." The policy statement also noted that it will "not be appropriate" to cut until the Fed has gained greater "confidence that inflation is moving sustainably toward 2%."

At the press conference after the decision was released, Fed Chair Powell said if there is an unexpected weakening in the labour market, that would certainly call for cutting rates sooner.

Recent economic indicators suggests that the economy is slowing including job figures released overnight. Private businesses hired 107k workers in January, below the 158k recorded in December and the 145k expected by the market. Growth in pay continued to slow. Job-stayers recording a 5.2% annual pay increase, below the 5.4% recorded in December. Job changers recorded a 7.2% annual pay increase, the smallest since May 2021.

Consistent with these wage outcomes the Employment Cost Index (like our wage price index) increased 0.9% over the December quarter, down from the 1.1% recorded in the September quarter and lower than the 1.0% expected by the market. This was the smallest quarterly increase since the second quarter of 2021.

Today's key data and events:

AU CoreLogic Dwelling Prices Jan exp 0.5% prev 0.4% (12:01am)

AU Trade Price Indices Q4 (11:30am)

Import Prices exp 0.2% prev 0.8%

Export Prices Q4 exp 3.3% prev -3.1%

AU Dwelling approvals Dec exp –0.5% prev 1.6% (11:30am)

CH Caixin Mfg PMI Jan prev 50.8 (12:45pm)

EZ CPI Jan y/y (9pm)

EZ Unemployment Rate Dec prev 6.4% (9pm)

UK BoE Policy Decision prev 5.25% (11pm)

US Construction Spending Dec exp 0.6% prev 0.4% (2am)

US ISM Mfg Jan exp 47.5 prev 47.4 (2am)

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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