Morning report

Bank of Melbourne

Thursday, 28 July 2022

Equities (close & % change)		
S&P/ASX 200	6,823	0.2%
US Dow Jones	32,198	1.4%
Japan Nikkei	27,716	0.2%
China Shanghai	3,433	-0.1%
German DAX	13,166	0.5%
UK FTSE100	7,348	0.6%
Commodities (close & change)*		
CRB Index	289.1	2.6
Gold	1,734.19	16.9
Copper	7,536.25	57.0
Oil (WTI futures)	97.26	2.3
Coal (thermal)	411.20	-15.3
Coal (coking)	203.00	-2.0
Iron Ore	113.15	0.8

Sydney Futures Exchange (close & change)				
	Last		Overnight Chg	
10 yr bond	96.77		0.04	
3 yr bond	97.04		0.08	
3 mth bill rate	97.23		0.05	
SPI 200	6,775.0		52	
FX Last 24 hrs	Open	High	Low	Current
TWI	62.6	-	-	62.9
AUD/USD	0.6956	0.7012	0.6913	0.6993
AUD/JPY	95.06	95.70	94.75	95.51
AUD/GBP	0.5774	0.5775	0.5742	0.5752
AUD/NZD	1.1107	1.1197	1.1094	1.1165
AUD/EUR	0.6806	0.6863	0.6822	0.6855
AUD/CNH	4.6978	4.7250	4.6765	4.7163
USD Index	106.47	107.43	106.26	106.46

Interest rates (close & change)		
Australia		
90 day BBSW	2.29	0.04
2 year bond	2.61	-0.10
3 year bond	2.92	-0.12
3 year swap	3.23	-0.05
10 year bond	3.25	-0.09
United States		
3-month T Bill	2.32	-0.14
2 year bond	3.00	-0.05
10 year bond	2.78	-0.02
Other (10 year yields)		
Germany	0.95	0.02
Japan	0.20	-0.01
UK	1.96	0.04

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: The Federal Reserve hiked rates by 75 basis points for the second consecutive month, as was widely expected. Fed Chair Powell signalled in his press conference that a similar sized move was possible in September and that he did not think that the US economy was in a recession. However, he also noted that at some point it will be "appropriate to slow down" the pace of rate hikes.

Equity markets surged, bond yields declined, and the US dollar ended broadly unchanged against a basket of major currencies.

Share Markets: Equity markets surged following comments from Chair Powell noting that the Fed will slow the pace of rate hikes at some point. Chair Powell also noted that the Fed will provide less "clear guidance" regarding the size of future moves and will consider things on a meeting-by-meeting basis.

The S&P 500 jumped by 2.6%, the tech-heavy Nasdaq surged by 4.1%, and the Dow Jones rose 1.4%.

The ASX 200 closed 0.2% higher yesterday. Futures are pointing to a positive open today.

Interest Rates: Bond yields declined following Powell's press conference. The US 10-year treasury yield fell 2 basis points to 2.78%, after briefly falling to 2.72% in the wake of the Fed's decision. The 2-year treasury yield declined by 5 basis points, to 3.00%, after briefly falling to a low of 2.96%.

Interest-rate markets are currently pricing in around a 79% probability of another 75-basis-point hike at the September meeting.

The Australia 10-year government bond yield (futures) fell 4 basis points to 2.24%. The 3-year government bond yield (futures) declined by 8 basis points to 2.97%.

Foreign Exchange: The Aussie dollar strengthened overnight trading from a low of 0.6913 to a one-month high of 0.7012. The AUD/USD pair is currently trading around 0.6993.

The US dollar was broadly flat against a basket of major currencies. The USD index slipped from a high of 107.43 ahead of the Fed meeting to a low of 106.26 and is currently trading around 106.46.

Commodities: Commodity prices were broadly firmer overnight. The West Texas Intermediate (WTI) price of oil remains below US$100 per barrel.

Australia: Headline inflation rose to a 31½-year high of 6.1% in the year to the June quarter. Underlying inflation stepped up to an annual rate of 4.9% - the fastest since the series began in 2003.

Shortages for building materials and staff, supply-chain disruptions and flooding made an impact.

Inflation has accelerated sharply since hitting a trough in 2020. However, the peak in annual inflation rates won't be struck until later this year. We expect annual headline inflation will peak at around 7-7.5%. Underlying inflation's peak is likely to be 5-5.5%.

The breadth of the inflationary pressures was reflected in price increases occurring in 10 of the 11 major consumer price index (CPI) groups. Clothing & footwear, housing, furnishings, household equipment & services, transportation (incl fuel) and food recorded hefty price rises of over 2% in the June quarter.

Price pressures for non-discretionary items continued to outstrip that of discretionary items. The cost of goods and services necessary for everyday living surged a record 7.6% over the year to the June quarter. Non-discretionary inflation delivered an annual print of 4.0%.

Over 2023, we expect inflationary pressures to unwind as supply-chain disruptions ease and demand slows from the Reserve Bank's (RBA) rate-hiking cycle. However, we expect inflation to stay above the RBA's 2-3% per annum target band until early 2024.

Yesterday's data cements our view that the RBA will hike by 50 basis points next week to take the cash rate to 1.85%. We continue to expect further tightening, with a high chance that by year's end the cash rate has a '3' handle on it.

China: Industrial profits rose 0.8% over the year to June, ending two consecutive months of negative annual growth over May and April. The lift in profits was underpinned by a resumption in manufacturing activity alongside the reopening of Shanghai from COVID-19 lockdowns.

Europe: M3 money supply rose 5.7% over the year to July. This was slightly down on a revised annual increase of 5.8% over the year to June.

United States: The Federal Reserve hiked rates by 75 basis points for the second consecutive month. The move was widely expected by economists and markets and takes the mid-point of the Fed funds rate from 1.625% to 2.375%. The vote was unanimous as all 12 members of the Federal Open Market Committee (FOMC) voted for a 75-basis-point hike. Fed Chair Jerome Powell said after the meeting that it was appropriate for the Fed to front load rate hikes but at some point it will be "appropriate to slow down". This quelled some concerns of rapid over-tightening from the Fed, providing a tailwind for markets.

Durable goods orders jumped 1.9% in June, beating consensus expectations of a 0.4% decline. The result was also an improvement on the 0.8% gain reported in May.

Pending home sales plunged 8.6% in June following a revised 0.4% gain in May. The result was considerably weaker than the 1.0% decline expected by consensus. The result adds to a slew of housing data released yesterday, painting a clear picture of a considerable slowing in the US housing market, as rising interest rates and elevated prices erode affordability.

Today's key data and events:

NZ ANZ Business Confidence Jul prev -62.6 (11am)
AU Retail Sales Jun exp 0.6% prev 0.9% (11:30am)
AU Trade Price Indices Q2 (11:30am)
  Export Prices prev 18.0%
  Import Prices prev 5.1%
EZ Economic Confidence Jul exp 102.0 prev 104.0 (7pm)
EZ Consumer Confidence Jul Final prev -27.0 (7pm)
US GDP Annualised Q2 exp 0.4% prev -1.6% (10:30pm)
US Core PCE Q2 exp 4.4% prev 5.2% (10:30pm)
US Kansas City Fed Index Jul exp 3 prev 12 (1am)

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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The Detail

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