Morning Report

Thursday, 2 November 2023

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Equities (close & % change)		
S&P/ASX 200	6,838	0.8%
US Dow Jones	33,275	0.7%
Japan Nikkei	31,602	2.4%
China Shanghai	3,170	0.1%
German DAX	14,923	0.8%
UK FTSE100	7,342	0.3%

Commodities (close & change)		
CRB Index	279.1	-2.1
Gold	1,982.53	-1.4
Copper	8,051.50	-42.5
Oil (WTI futures)	80.77	0.3
Coal (thermal)	126.50	-0.9
Coal (coking)	326.00	-7.3
Iron Ore	120.75	-0.7

Sydney Futures Exchange (last & change)	Last	Overnight Chg
10 yr bond	4.83	-0.13
3 yr bond	4.34	-0.10
3 mth bill rate	4.42	-0.01
SPI 200	6,896.0	52

FX Last 24 hrs	Open	High	Low	Current
TWI	60.2	-	-	60.2
AUD/USD	0.6337	0.6399	0.6318	0.6393
AUD/JPY	96.13	96.53	95.61	96.52
AUD/GBP	0.5215	0.5266	0.5207	0.5262
AUD/NZD	1.0880	1.0938	1.0849	1.0938
AUD/EUR	0.5992	0.6059	0.5979	0.6049
AUD/CNH	4.6518	4.6930	4.6368	4.6902
USD Index	106.73	107.11	106.61	106.66

Interest rates (close & change)		
Australia		
90 day BBSW	4.35	0.00
2 year bond	4.37	-0.10
3 year bond	4.31	-0.10
3 year swap	4.51	-0.01
10 year bond	4.81	-0.13
United States		
3-month T Bill	5.29	-0.02
2 year bond	4.94	-0.14
10 year bond	4.73	-0.20
Other (10 year yields)		
Germany	2.76	-0.04
Japan	0.96	0.01
UK	4.50	-0.01

Data as at 9:00am AEST. Change is from the previous trading day (excluding the SFE, which is the change during the night session). Source: Bloomberg.

Main Themes: Bond yields plunged as investors reacted to the Fed decision and weaker-than-expected US data. Investors were particularly interested in the communication around the future path of monetary policy and Fed Chair Jerome Powell's press conference. The target rate was left unchanged, at 5.25% - 5.50%, as was widely expected. However, changes to the statement and comments during the press conference were interpreted as dovish and markets wound back the prospect of additional hikes.

Share Markets: Equity markets rallied on hopes that the rate hiking cycle may have peaked. The S&P 500 jumped 1.1%, the Nasdaq surged 1.6% and the Dow Jones was 0.7% higher.

The ASX 200 rose 0.8% yesterday. Futures are pointing to a strong open.

Interest Rates: US bond yields plunged across the curve as markets wound back the prospect of additional hikes from the Fed and on weaker-than-expected US manufacturing data. The 2-year yield plunged 14 basis points, to 4.94%, while the 10-year yield dropped a whopping 20 basis points, to 4.73%.

Interest-rate markets wound back the prospects of further hikes in this cycle. Markets now attach less than a 30% chance of one more hike by January 2024. Regarding cuts next year, markets are pricing almost four cuts by January 2025.

Australian government bond yields (futures) broadly mimicked the moves in the US. The 3-year futures yield dropped 10 basis points, to 4.34%. The 10-year yield was 13 basis points lower, at 4.83%. Markets continue to attach a roughly 50/50 chance of a hike from the RBA in November. In 2024, markets have almost 1.5 hikes priced by the middle of the year.

Foreign Exchange: The US dollar closed slightly lower against major currencies, as bond yields plunged and prospects of additional hikes were wound back. The USD Index fell from a high of 107.11 to a low of 106.61, before recovering to 106.66.

The AUD/USD pair rose against a weaker USD. The pair rose from a low of 0.6318 to a high of 0.6399, before pulling back to 0.6393.

Commodities: Oil was slightly higher on the day, while most other commodity prices pulled back.

Australia: Building approvals declined 4.6% in September, partly unwinding an 8.1% gain in August. The decline reflected a 4.6% slide in private sector house approvals and a 5.1% fall in multi-density approvals (e.g. apartments and townhouses).

Approvals have fallen in five out of nine months so far in 2023. Looking through month-to-month volatility, the trend remains weak. Approvals continue to run well below long-run averages. The monthly rate of approvals was a whopping 43% below the March 2021 peak and 24% below the 10-year average. Private sector house approvals are running at almost 15% below the 10-year average, while multi-density approvals are even weaker, at 37% below.

Approvals declined in the month in WA (-11.0%), NSW (-10.5%) and Victoria (-8.9%). Queensland (34.6%) recorded a large jump, driven by a surge in multi-density approvals and SA (5.1%) was also up.

The latest approvals data continues to paint a sombre picture for the supply-side of the housing market. After a surge during the pandemic driven by low rates and policy stimulus, approvals have fallen sharply and are pointing to a muted supply response in the future. This is occurring while demand remains robust, underpinned by record population growth.

The prospect of additional rate hikes and continued challenges for the construction industry are placing additional pressure on approvals. A sustained recovery still appears some time away.

Dwelling prices rose 0.9% in October, up from the 0.7% monthly increase recoded over each of the previous three months. Since bottoming out in January, national dwelling prices are up 7.6%. While the recovery is being led by capital cities (8.9%), it has now become broad based with price gains recorded in the regions (3.5%).

Prices are expected to surpass the historic high recorded in April 2022 by mid-November given the current growth rate, notwithstanding 400 basis points of tightening by the Reserve Bank over the past 18 months. This shows how significant the housing market imbalance has become.

However, there are early indications that the depth of demand is now being tested. October was the first month since February 2023 that we saw more new listings (supply) than sales (demand) – in other words absorption of new listings was below 100%. New listings have increased by an uncharacteristically large 14.9% over the past two months, and at least over October, demand did not keep up.

The key question going forward is whether this imbalance will continue or whether supply will increase sufficiently to outstrip demand (as we saw in October). Overall, we except demand, supported by the record growth in the population, to largely absorb supply, but it could get bumpy month to month the longer rates remain restrictive.

Given these supply and demand dynamics, we see a scenario where dwelling price gains moderate overtime but continue nonetheless. The moderation we are seeing in quarterly growth rates, particularly across capital cities, is consistent with this outlook.

China: The Caixin manufacturing PMI slipped into contractionary territory in October, falling to 49.5, from 50.6 in September. This was below consensus expectations of 50.8. The reading followed the official manufacturing PMI yesterday, which was also weaker than expected and indicated contraction across the manufacturing sector. Both measures suggest that risks to growth remain.

United States: The Federal Reserve left the Fed Funds Rate unchanged at 5.25% - 5.50%, in a unanimous 12-0 vote. The outcome was widely expected. The key change to the statement was the insertion of a reference to financial conditions, in addition to the previously mentioned credit conditions, being "likely to weigh on economy activity, hiring, and inflation". This was interpreted as dovish and supports the view that higher long-term rates will help to reduce the need for additional monetary policy tightening. In his press conference, Chair Powell left the door open to raising rates further, if needed. However, the need for additional hikes is not certain. He noted that "it's fair to say that the question we're asking is 'should we hike more?'".

A key leading indicator of the manufacturing sector pointed to weakness ahead as the sector deals with tighter monetary policy settings. The ISM manufacturing PMI dropped to 46.7 in October, well below consensus expectations for an unchanged reading of 49.0. New orders dropped sharply, to 45.5 from 49.2, as did employment, to 46.8 from 51.2, implying weaker conditions for the sector. Prices paid rose to 45.1, from 43.8, but remained in contractionary territory – signalling that prices continue to contract but at a slower pace.

Private sector employment grew by less than expected in October. The ADP employment gauge showed that private sector employment rose 113k in the month, up from 89k in September. This was below expectations of 150k. The survey has proven to be an unreliable indicator of the more important non-farm payrolls data, due Friday.

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Today's key data and events:

AU Goods Trade Balance Sep exp $10.4bn prev $10.4bn (11:30am)

AU Housing Finance Sep (11:30am)

Investor exp 3.5% prev 1.6%

Owner-occupier exp 4.2% prev 2.6%

Total exp 4.0% prev 2.2%

UK BoE Policy Decision (11:00pm)

Bank Rate exp 5.25% prev 5.25%

US Factory Orders Sep exp 2.3% prev 1.2% (1:00am)

US Durable Goods Orders Sep Final (1:00am)

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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