bankSA

Morning Report

Wednesday, 2 June 2021

Equities (close & % change)			Sydney Futures Exchange (close & change)					Interest rates (close & change)		
S&P/ASX 200	7,143	-0.3%		Last		Overnight Chg		**Australia**		
US Dow Jones	34,575	0.1%	10 yr bond	98.37		0.00		90 day BBSW	0.03	0.00
Japan Nikkei	28,814	-0.2%	3 yr bond	99.80		0.00		2 year bond	0.05	-0.01
China Shanghai	3,799	0.3%	3 mth bill rate	99.96		-0.01		3 year bond	0.27	-0.01
German DAX	15,567	0.9%	SPI 200	7,159.0		12		3 year swap	0.37	-0.01
UK FTSE100	7,080	0.8%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	1.69	-0.02
Commodities (close & change)*			TWI	63.5	-	-	63.6	**United States**		
CRB Index	208.4	2.7	AUD/USD	0.7734	0.7741	0.7701	0.7753	3-month T Bill	0.01	0.00
Gold	1,900.44	-6.4	AUD/JPY	84.76	84.91	84.60	84.87	2 year bond	0.15	0.01
Copper	10,236.50	-14.3	AUD/GBP	0.5444	0.5462	0.5432	0.5478	10 year bond	1.61	0.01
Oil (WTI)	67.96	1.6	AUD/NZD	1.0630	1.0661	1.0622	1.0683	**Other (10 year yields)**		
Coal (thermal)	115.25	3.2	AUD/EUR	0.6326	0.6349	0.6320	0.6349	Germany	-0.18	0.01
Coal (coking)	161.00	3.0	AUD/CNH	4.9291	4.9338	4.9058	4.9494	Japan	0.08	0.00
Iron Ore	198.20	0.0	USD Index	89.8	90.1	89.8	89.9	UK	0.83	0.03

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

Main Themes: US share markets were mixed, oil prices rose to their highest level since October 2018, after bullish OPEC remarks and Australian investors are looking ahead to GDP data out later today.

Share Markets: US share markets pared earlier advances after manufacturing data topped estimates while showing ongoing difficulties from supply shortages and labour constraints. The S&P 500 index edged 2 points lower while the Dow rose 45 points (or +0.1%). The Nasdaq lost 12 points.

Interest Rates: US bond yields lifted slightly across the yield curve.

Foreign Exchange: The US dollar lost ground in the European trading session, but then fully recovered in the New York session. The AUD/USD moved to a high of 0.7741 overnight, after a slightly less dovish statement from the Reserve Bank, but could not fully hold on to these gains. The AUD/USD continues to remain trapped within a month-old trading range of 0.7675 – 0.7890.

Commodities: Oil prices rose after OPEC forecast a tightening market. The West Texas Intermediate measure closed at almost $68 a barrel – the highest level since October 2018. OPEC agreed to maintain current production policies until July when it expects to increase production but stated that it did not expect a large impact from Iraq re-entering global supply and that it was not certain if Iran would get a new nuclear deal. Oil prices began rallying after a technical committee within OPEC on Monday confirmed forecasts for a rebound of 6 million barrels per day in world oil demand this year.

COVID-19: Victoria's COVID-19 lockdown, due to end at 11:59pm tomorrow, is widely expected to be extended. There are growing fears about rapid transmission after Chief Health Officer Brett Sutton said yesterday that the virus was moving "faster than any other strain we've dealt with".

Australia: The Reserve Bank (RBA) delivered no surprises at its monthly meeting, leaving policy settings unchanged. However, yesterday's meeting was the entrée to the main meal in July. In July, the Reserve Bank will decide whether to direct its yield-curve control (YCC) program from the April 2024 bond to November 2024 (the next maturity). The RBA will also decide whether to extend its quantitative easing (QE) program.

We are anticipating YCC to be extended to November 2024 and another round of QE, with $100 billion in bond purchases, will be announced. However, in yesterday's statement, the RBA dropped that it "is prepared to undertake further bond purchases to assist with progress towards full employment". This omission raises some possibility that the RBA is signalling its intention to stay at the April 2024 bond and/or begin tapering of QE.

Remarks by the RBA on the hot topics of jobs and house prices were also eyed closely.

On the jobs market, the RBA acknowledged in its board statement for the first time that there are reports of labour shortages. However, the RBA has stuck to its expectation of only a gradual and modest rise in wages growth. The RBA's forecasts for inflation remained unchanged and consistent with their view that they are not expecting to lift the cash rate before 2024.

On housing, the RBA inserted a new sentence to acknowledge "increased borrowing by investors", but the sentence around lending standards remained unchanged. The RBA reiterated it "will be monitoring trends in housing borrowing carefully and it is important that lending standards are maintained". We anticipate the RBA will be watching riskier forms of borrowing, especially by investors. We would not rule out a tightening in macroprudential policy next year, which would put a brake on the ramp up in dwelling prices.

Separately, housing data showed the housing boom charged ahead in May. CoreLogic's national home value index jumped 2.2% in May and the annual pace spiked to an 11-year high of 10.2%. Dwelling prices are now 10.2% higher than their previous peak in April 2020.

Low mortgage rates, elevated consumer confidence and the recovery in the labour market are continuing to propel prices higher.

There are growing signs that the heat is returning to capital cities with dwelling prices up 7.1% over the three months to May, outstripping the 6.5% growth in regional areas. Sydney is rapidly remerging as the nation's housing hotspot with housing prices up 9.3% in the past three months. This is the fastest growth rate over a three-month period in 32 years!

The low level of housing stock remains a key driver of the surge in prices. The total number of advertised listing remains around 25% lower than its average over the past 5 years.

Other data yesterday showed building approvals fell 8.6% in April, although they remain elevated relative to historical levels. However, it will take some time for sufficient supply to come on the market to materially lift the housing stock.

In yet more data, the business indicators survey revealed business inventories jumped 2.1% in Q1 compared to a flat outcome in Q4.

Company profits contracted 0.3% in Q1 to be up 11.9% over the year. The unknown here is whether the end of some government assistance programs impacted profits.

The balance of payments was also published yesterday. The current account surplus reached another record high of $18.3 billion in Q1, driven by strong commodity prices. This is a historic moment as Australia has now achieved a record 8th consecutive quarterly surplus. Export volumes increased by 2.0% in the quarter, and imports rose by 3.3%. Meanwhile, terms of trade rose 4.8% in the quarter, delivering an income injection to the Australian economy from the rest of the world.

Yesterday's data wraps up the economic indicators ahead of the GDP release later today. Our GDP forecast for the March quarter is 1.6%, which is a solid outcome, but a slower quarterly pace than in the last two quarters. In year-on-year terms, we expect the economy grew by 0.7%.

The consensus is for GDP to show a quarterly rise of 1.5% in Q1, but the range of forecasts is very wide, ranging between a rise of 0.5% and a gain of 2.1%.

We see the risks to the forecasts tilted to the upside. The key uncertainties and risks are around services spending by consumers; in particular, to what extend was this affected by the snap lockdowns and the floods in Q1.

China: China's manufacturing sector expanded in May at the fastest pace in five months, despite the surge in prices for raw materials. The Caixin manufacturing purchasing managers' index (PMI) rose modestly in May to 52.0, from 51.9 in April.

New Zealand: Building permits continued to rise in April, lifting by 4.8%, which followed a revised 19.7% increase in March. On a year-on-year basis, the monthly number of building permits in the month of April was up 84%. Auckland is at the centre of this increase, with over 18,000 new dwellings approved over the past year.

Europe: The eurozone unemployment rate fell 0.1 percentage point to 8.0% in April, even as COVID-19 restrictions continued leading many businesses to reduce or suspend services.

Eurozone inflation sped up faster than anticipated last month, revving up to 2.0% from 1.6%. Consensus was for 1.9%. The core gauge picked up to 0.9% from 0.7%, in line with consensus expectations.

United Kingdom: According to Rightmove data, house prices rose 1.8% in May. On a year-on-year basis, house prices rose 10.9%, the biggest annual increase in nearly seven years.

United States: Factory activity is picking up. The ISM manufacturing index rose more than expected in May to 61.2 from 60.7 in April, propelled by stronger growth in orders — which factories are having trouble satisfying because of supply shortages and labour constraints. However, there was a slight decline in prices paid to 88.0 (from 89.6) but this index remains high. There was also a fall in the employment index to 50.9, from 55.1.

The final reading for Markit's manufacturing PMI increased to a new record high of 62.1, from the preliminary flash reading of 61.5. Output and new orders increased, but supply chain issues remain elevated.

The Dallas Federal Reserve's manufacturing survey remained expansionary but the main index fell to 34.9 in May, from 37.2 in April.

Today's key data and events:

NZ Terms of Trade Q1 exp -0.3% prev 1.3% (8:45am)

AU RBA's Head of Economic Analysis, Bradley Jones, Gives Speech in Canberra (9:30am)

AU GDP Q1 (11:30am)

q/q exp 1.6% prev 3.1%

y/y exp 0.7% prev -1.1%

EZ PPI Apr y/y exp 7.3% prev 4.3% (7:00pm)

AU RBA Deputy Gov. Debelle and Ass. Gov Bullock Appear Before the Senate Economics Legislation Committee (7pm)

US Federal Reserve's Beige Book (4:00am)

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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