Morning Report

Wednesday, 21 July 2021

Equities (close & % change)			Sydney Futures Exchange (close & change)					Interest rates (close & change)		
S&P/ASX 200	7,252	-0.5%		Last		Overnight Chg		Australia		
US Dow Jones	34,512	1.6%	10 yr bond	98.81		-0.01		90 day BBSW	0.02	0.00
Japan Nikkei	27,388	-1.0%	3 yr bond	99.72		0.00		2 year bond	0.04	-0.01
China Shanghai	3,707	-0.1%	3 mth bill rate	99.97		-0.01		3 year bond	0.24	-0.04
German DAX	15,216	0.5%	SPI 200	7,251.0		22		3 year swap	0.38	0.00
UK FTSE100	6,881	0.5%	FX Last 24 hrs	Open	High	Low	Current	10 year bond	1.18	-0.06
Commodities (close & change)*			TWI	61.8	-	-	61.4	United States		
CRB Index	209.0	3.4	AUD/USD	0.7344	0.7357	0.7300	0.7331	3-month T Bill	0.04	0.00
Gold	1,810.36	-2.3	AUD/JPY	80.39	80.60	79.85	80.56	2 year bond	0.20	-0.02
Copper	9,203.50	-202.8	AUD/GBP	0.5370	0.5387	0.5355	0.5380	10 year bond	1.22	0.03
Oil (WTI)	67.42	1.0	AUD/NZD	1.0573	1.0615	1.0571	1.0596	Other (10 year yields)		
Coal (thermal)	127.75	0.1	AUD/EUR	0.6224	0.6234	0.6206	0.6223	Germany	-0.41	-0.02
Coal (coking)	209.00	0.8	AUD/CNH	4.7708	4.7724	4.7402	4.7569	Japan	0.01	-0.01
Iron Ore	208.30	1.1	USD Index	92.8	93.2	92.8	93.0	UK	0.56	0.00

Data as at 7:00am. Change from previous trading day (excluding the SFE which is the change during the night session). Source: Bloomberg.

Main Themes: Risk sentiment across global share markets recovered as investors saw the recent falls as a buying opportunity.

Share Markets: US share markets erased most of Monday's losses as they posted their biggest gains since March. The S&P 500 rose 1.5% and the NASDAQ rose 1.6%. Cyclical stocks and small caps were the big winners on the day, with the small cap Russell 2000 index rising by 3.0%.

European market also rose. The Euro Stoxx was up 0.7% and the FTSE was up 0.5%.

The ASX 200 fell 0.5% yesterday. ASX futures suggest the index is likely to open higher today following the lead from global share markets.

Interest Rates: US 10-year Treasury yield rose 3 basis points to close at 1.22%, recovering some of yesterday's 10 basis-point fall. The US 2-year yield fell 2 basis points to 0.20%.

The Australian 3-year government bond yield (futures) rose 1 basis point to 0.29%, while the 10-year yield (futures) rose from 1.19% to 1.20%.

Foreign Exchange: The US dollar rose against most major currencies last night. The USD Index rose from a low of 92.8 to a high of 93.2. It is currently trading near this high at 93.0.

The AUD/USD pair fell overnight from a high of 0.7357 to a low of 0.7300, its lowest level since November 2020, before recovering to around 0.7331. The AUD spent most of last night in a tight trading range, suggesting some consolidation after losing around 2 US cents since mid July.

Commodities: Oil rose by 1.5% overnight alongside broader market movements. Iron ore and coal edged higher while gold fell.

COVID-19: South Australia entered a 7-day lockdown yesterday. This comes after the state recorded 4 new COVID-19 cases yesterday.

NSW recorded 78 infections yesterday, which is the third consecutive day that daily cases have fallen. Victoria recorded 13 new cases, with the current lockdown extended to July 27.

Australia: Minutes from the Reserve Bank (RBA) July meeting were released yesterday. At this meeting, the RBA announced it will begin tapering bond purchases under its quantitative easing (QE) program from September. It also revealed it will keep yield curve control (YCC) pegged to the April 2024 bond. The cash rate was left unchanged.

However, the minutes released yesterday need to be interpreted against a near-term deterioration in the economic outlook since the meeting. At that time, the NSW lockdown was expected to last only two weeks.

As flagged last week, we expect the economy will contract in this current September quarter; we currently estimate the contraction will be 0.7% in size. In contrast, we expected GDP growth of almost 1.0% prior to the outbreak. We expect growth will return in the December quarter, assuming the lockdown in NSW does not last beyond 7-8 weeks and assuming there are no further significant spillovers to the rest of Australia. It means we now expect annual growth to be closer to 4%, from almost 5% prior to the outbreak. Annual growth of over 4% remains a very solid rate of expansion.

The recent developments with infections and lockdowns means it is increasingly likely that the RBA will opt to hold off tapering QE in September.

The RBA announced it would reduce the rate of bond purchases from $5 billion to $4 billion per week because “economic outcomes had been materially better than earlier expected and the outlook had improved”. This no longer holds true.

Given the severity of the economic hit, another possibility is that the RBA actually lifts the rate of bond purchases to more than $5 billion per week in September.

There was no fresh news on the path of the cash rate in the minutes with identical language to the statement following the meeting, noting the RBA’s “central scenario” is that conditions for a cash rate hike won’t be met until 2024.

We still expect that the first cash rate hike will come in 2023, although acknowledge there is some risk this time frame could be pushed out if the lockdowns are dragged out. This is consistent with our expectation that activity will rebound rapidly once restrictions lift, and that the economy was in good shape heading into this period.

However, the renewed outbreaks are a moving beast. We don’t know how long the lockdowns will last or how harsh the measures will be, and as a result there is still substantial uncertainty over the extent of the economic hit. The response of the RBA will ultimately hinge upon how the lockdowns impacts jobs and inflation.

United Kingdom: In comments to the Treasury Committee of the UK Parliament, Catherine Mann, member of the Bank of England’s Monetary Policy Committee said that policy makers should “not be premature in terms of tightening monetary policy”.

She spoke of the lessons policymakers can take from the GFC to not tighten too early in the recovery from COVID. She noted that “the recovery from COVID is more fragile than might appear”.

United States: Housing starts increased by 6.3% to 1,643k in June, from 1,572k in May. This result was above consensus expectations of 1,590k. Housing starts are now up over 29% from last year, when the pandemic caused a reduction in activity. This is a strong result amid rising building costs and shortages of skilled labour.

However, building permits fell by 5.1% to 1,598k, below consensus expectations of 1,696k. This suggests that housing starts may fall in future months.

Today’s key data and events:

AU WBC Leading Index Jun prev -0.06% (10:30am)

AU Retail Sales Jun Prel. exp -0.2% prev 0.4% (11:30am)

NZ Credit Card Spending Jun prev 8.5% (1pm)

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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