

# Australian Markets Weekly

## US election prime billing; bulk export prices still rising

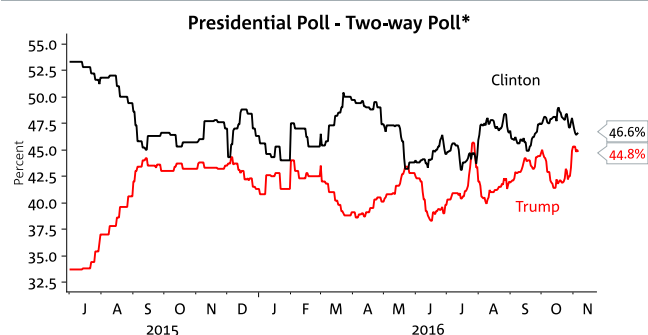
- Elections for the US President (and the Congress) rightly take top billing this week. The latest poll of polls from RealClearPolitics (see the polls [here](#)), including several released over the weekend, has Hillary Clinton at 46.6% and Donald Trump at 44.8%. Veteran pollster Nate Silver has Clinton at a 64.5% chance of winning in a two horse race and Trump at 35.5% (see that poll [here](#)). Since this morning's disclosure by the FBI that the subsequent inquiry into Clinton's emails has found no change to the FBI's previous advice not to lay charges, there has been some swing back to the US dollar against the Euro, Swiss Franc, and the yen. The AUD has been steadier.
- If it's a clear outcome, then recent elections suggest a result could be known from around 3pm AEST Wednesday. A Clinton win would see a return to the "status quo", the market then refocussing on a 15 December FOMC rate hike and near term USD support, including after Friday's solid US non-farm payrolls. There is the possibility that a result may not be known for some time if there are very close results in key swing States. And there is also the possibility that neither candidate might accrue the necessary 270 Electoral College votes needed to win the Presidency in which event it would go to the House of Representatives for determination.
- Friday's RBA Statement on Monetary Policy revealed no material change to the Bank's GDP and inflation forecasts, the RBA still indicating that its forecast for the trimmed mean inflation is for inflation to not get back to 2% until 2018.
- The Bank also laid out its continuing concern about apartment oversupply. The Bank upgraded its assumption for the terms of trade on the back of surging coal prices, though not to the extent as the recent rally, as some of the temporary (and arguably less temporary) factors currently supporting prices are reversed.
- In this Weekly, we delve further into the various factors behind soaring coal prices and steady-to-higher iron ore prices. A combination of structural, cyclical, and temporary/ weather events that have conspired to produce a perfect storm for coal prices. Increases in supply in response to very attractive prices will quell prices, given time.
- Beyond focus on the US election this week, domestic markets see the release of the NAB Business Survey for October tomorrow and the W-MI Consumer Sentiment Wednesday. Offshore, the RBNZ is expected to cut rates on Thursday despite a spate of strong economic reports with focus in their language and cash rate forecasts.

### Key markets over the past week

	Last	% chg week		Last	bp / % chg week
AUD	0.7677	0.9	RBA cash	1.50	0
AUD/CNY	5.20	1.0	3y swap	1.86	3
AUD/JPY	80.0	0.3	ASX 200	5,249	-1.3
AUD/EUR	0.693	-0.1	Iron ore	65.0	1.6
AUD/NZD	1.049	-1.3	WTI oil	44.5	-5.0

Source: Bloomberg

### Chart 1: Still too close to call



\* Excludes third party candidates Johnson and Stein, average of polls  
Source: National Australia Bank, RealClearPolitics

### Author:

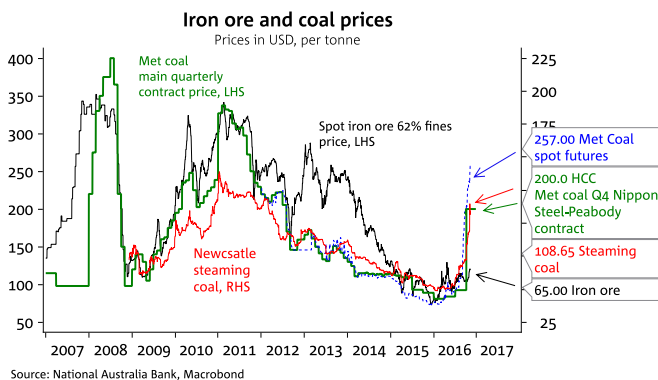
David de Garis, Director, Economics

## A perfect storm for bulk commodity prices this year

While developments in the apartment market remains a source of close interest for markets and the RBA, another big story for the Australian economy this year has been the strength in bulk export commodity prices, including steep rises in coal prices.

Friday saw further increases in coal prices, hard coking coal – used in steel production – rising another \$3.50/t to \$US257/t, up 6.1% so far this month and a staggering 3½ fold from \$72/t at the end of last year. The price of thermal coal – used to generate electricity – also rose, the benchmark Newcastle futures price back up \$2.15/t to \$US108.65/t. Thermal coal prices have been unchanged in net terms so far this month, having more than doubled so far this year from December’s \$50.60/t. Iron ore prices have not had the same spectacular performance, but have remained resilient, up a net 1.0% so far this month to \$65.00/t and up 49.2% from its closing level of \$43.57/t.

### Chart 2: Coal prices still soaring



In 2015-16, iron ore exports were 2.9% of GDP, coking coal 1.2% and thermal coal 0.9%, and together constituting 5% of nominal GDP; by comparison new private dwelling investment was 5.4% of GDP last financial year. Given the substantial price increase for commodities, their share of nominal GDP is likely to increase further with implications for the Trade Balance, with the possibility of a trade surplus – the first since early 2014.

### Structural, cyclical and temporary factors at play

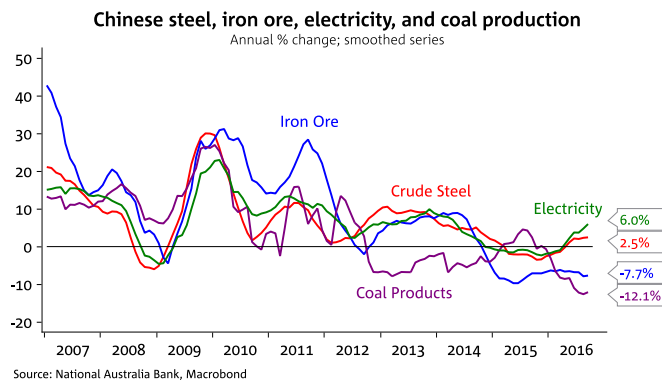
A big part of the story behind coal price developments this year has been Chinese policy efforts to reform steel and coal, together with the still strong performance of the economy.

On the policy-reform side, earlier this year, the Chinese government singled out over-capacity in its steel and coal industries for reform. The authorities sought to cut capacity in the steel industry by 13% and to reduce coal capacity by around 9% by cutting inefficient, higher cost, and lower quality output.

In the coal industry, the Government announced that production would be restricted to 276 days for the year to advance its “reform” program. This has been evidenced by steeper falls in Chinese coal production. The question then is, how much will stay closed. Given the nature of sometime painful adjustment, it seems reasonable to assume for now

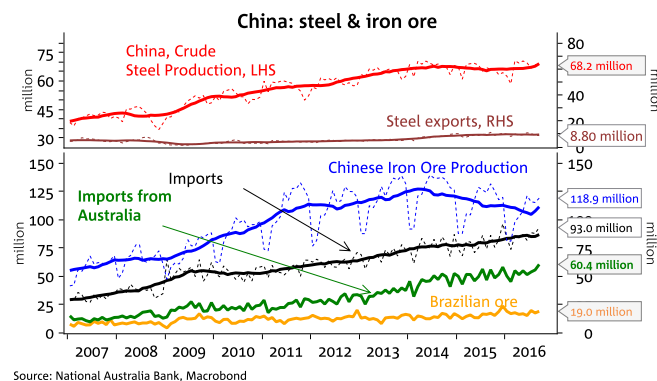
that a good portion will remain closed. We do though note recent statements from the authorities that they will permit some easing in restrictions for some producers to support supply and quell prices. It remains to be seen how quickly and to what extent Chinese coal supply will respond in addition to signs that at least two Australian mines will be re-opened in response to recently more attractive prices.

### Chart 3: China’s sifting supply and demand



On the demand side, notwithstanding the announced reforms to over-capacity of the Chinese steel industry, production levels have been rising this year, thanks to higher levels of residential construction, infrastructure investment, and motor vehicle production.

### Chart 4: Steel and iron ore supply

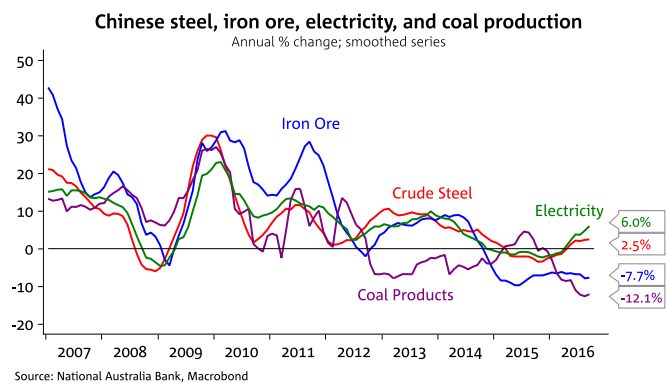


Chinese steel prices and production have been rising this year, supporting the demand for iron ore and hard coking coal. Developments in Chinese property markets remain important to the outlook for iron ore and coking coal prices.

We would also observe that while selective efforts at reforming over-capacity in key old heavy industries have been evident, the speed and depth of reform is always balanced against the over-arching growth objectives. Rising construction and infrastructure spending have combined with “reform” in the coal industry to the benefit of Australia’s market share. Chinese production of iron ore has also been declining.

The fundamentals behind thermal coal prices present a not dissimilar story of how rising demand and reduced Chinese supply have spurred prices. On the demand side, electricity production in China has been increasing, at a time of diminishing Chinese coal production, leading to increased demand for imports, including from Australia.

## Chart 5: China's evolving demand and supply



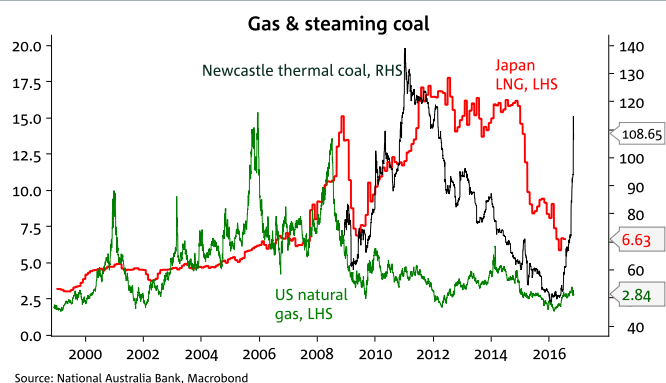
### Outlook: Demand and supply at play still

The outlook for Australian coal export prices will be contingent on the speed and depth of supply rising from among global producers in response to the very attractive prices on offer. To the extent that short-term supply disruptions affecting production in distribution in China and even in Australia from the very wet spring have also pushed up prices, such effects would be expected to be fully unwound, in time. Even beyond this, supply will respond, given time.

In the case of iron ore, it's also been evident through most of this year that China's domestic production has been cut in response to previously low prices, higher domestic production costs and generally lower iron ore content. However, there are tentative signs that Chinese output – allowing for the large seasonal swings and other short term volatility in production – might be beginning to stabilise.

In the thermal coal space, lower oil and US natural gas prices of late might begin to weigh on thermal export prices. Lower US natural gas prices increases the price competitiveness of US electricity generated from gas as opposed to coal. To the extent there is switching, this would only accelerate the attractiveness for US coal producers to chase currently soaring Asian import prices to the extent they are able to re-direct sales.

### Chart: Gas and thermal coal prices



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# Calendar of Economic Releases

Country	Economic Indicator	Period	Forecast	Consensus	Actual	Previous	GMT	AEDT
<b>Monday, 7 November 2016</b>								
AU	AIG Perf of Construction Index	Oct				51.4	23.30	9.30
JN	Labor Cash/Real Earnings YoY	Sep		0.2		-0.1/0.5	1.00	11.00
AU	ANZ Job Advertisements MoM	Oct				-0.3	1.30	11.30
CH	Foreign Reserves	Oct		3132.5		3166.4	1.30	11.30
GE	Factory Orders MoM/YoY	Sep		0.2		1.0/2.1	8.00	18.00
UK	Halifax House Prices MoM/3m YoY	Oct		0.2		0.1/5.8	9.30	19.30
FALSE	ECB's Constancio on Panel at EU Macro-Prudential Hearing						10.15	20.15
EC	Sentix Investor Confidence	Nov		8.6		8.5	10.30	20.30
EC	Retail Sales MoM/YoY	Sep		-0.3		-0.1/0.6	11.00	21.00
CA	Bloomberg Nanos Confidence	Nov 4				56.2	16.00	2.00
US	Labor Market Conditions Index Change	Oct				-2.2	16.00	2.00
US	Consumer Credit	Sep		17.5		25.9	21.00	7.00
<b>Tuesday, 8 November 2016</b>								
NZ	ANZ Truckometer Heavy MoM	Oct				-1.4	22.00	8.00
AU	ANZ Roy Morgan Weekly Consumer Confidence Index	Nov 6				114.1	23.30	9.30
UK	BRC Sales Like-For-Like YoY	Oct		0.6		0.4	1.10	11.10
AU	NAB Business Conditions/Confidence	Oct				8/6	1.30	11.30
CH	Trade Balance	Oct		51.7		42.0	2.00	12.00
CH	Exports/Imports YoY	Oct		-5.9/-1		-10.0/-1.9	2.00	12.00
JN	Leading Index CI	Sep P		100.5		100.9	6.00	16.00
AU	RBA's Chris Ryan, Head of International Department speaks at Asian Regulatory Summit in Hong Kong						7.15	17.15
GE	Industrial Production SA MoM/YoY	Sep		-0.5/2		2.5/1.9	8.00	18.00
GE	Current Account Balance	Sep		24.5		17.9	8.00	18.00
UK	Industrial Production MoM/YoY	Sep		0/0.8		-0.4/0.7	10.30	20.30
UK	Manufacturing Production MoM/YoY	Sep		0.4/-0.1		0.2/0.5	10.30	20.30
CH	Foreign Direct Investment YoY CNY	Oct		2.5		1.2	10.25	20.25
US	NFIB Small Business Optimism	Oct		94.1		94.1	12.00	22.00
US	Fed's Evans Speaks on Economy and Policy in New York						13.45	23.45
CA	Housing Starts/Building Permits MoM	Oct		195/-4.3		220.6/10.4	14.15	0.15
UK	NIESR GDP Estimate	Oct				0.4	16.00	2.00
US	JOLTS Job Openings	Sep		5469		5443	16.00	2.00
US	Fed's Evans Speaks on Economy and Policy in New York						18.20	4.20
US	<b>Presidential and Congressional elections (result expected through Wednesday Asia time)</b>							
<b>Wednesday, 9 November 2016</b>								
NZ	Card Spending Total MoM	Oct	flat	0.4		2.0	22.45	8.45
AU	Westpac Consumer Conf Index/MoM	Nov				102.4/1.1	0.30	10.30
JN	BoP Current Account Adjusted	Sep		1630		1975.7	0.50	10.50
AU	NAB Commercial Property Survey	Q3					1.30	11.30
CH	CPI/PPI YoY	Oct		2.1/1		1.9/0.1	2.30	12.30
JN	Bankruptcies YoY	Oct				-3.4	5.30	15.30
JN	Eco Watchers Survey Current/Outlook	Oct		44.4		44.8/48.5	6.00	16.00
UK	Trade Balance	Sep		-3950		-4733.0	10.30	20.30
EC	European Commission Economic Forecasts						11.00	21.00
JN	Machine Tool Orders YoY	Oct P				-6.3	0-14 Nov release	
US	Wholesale Inventories/Sales MoM	Sep F		0.2/0.5		0.2/0.7	16.00	2.00
US	Fed's Kashkari Speaks in Eau Claire, Wisconsin						19.30	5.30
<b>Thursday, 10 November 2016</b>								
NZ	RBNZ Official Cash Rate	Nov 10	1.75	1.75		2.0	21.00	7.00
JN	Machine Orders MoM/YoY	Sep		-1.5/4.1		-2.2/11.6	0.50	10.50
AU	Consumer Inflation Expectation	Nov				3.7	1.00	11.00
UK	RICS House Price Balance	Oct		18		17.0	1.10	11.10
AU	Home Loans/Investment Loans MoM	Sep	-0.6	-1.6		-3.0/0.1	1.30	11.30
US	Fed's Williams Speaks on Economic Outlook in San Francisco						3.00	13.00
NZ	REINZ House Sales YoY	Oct				-9.5		
CH	New Yuan Loans CNY	Oct		680		1220.0	10-15 Nov release	
CH	Aggregate Financing CNY	Oct		987		1720.0	10-15 Nov release	
CA	New Housing Price Index MoM/YoY	Sep		0.2		0.2/2.7	14.30	0.30
US	Initial Jobless Claims	Nov 5		260		265.0	14.30	0.30
US	Fed's Bullard Speaks on U.S. Economic Outlook in St. Louis						15.15	1.15
US	Bloomberg Consumer Comfort	Nov 6				44.6	15.45	1.45
EC	Schaeuble, Weidmann Attend VOeB Public Bank Lobby Event						18.00	4.00
US	Monthly Budget Statement	Oct		-78.45		33.4	20.00	6.00
<b>Friday, 11 November 2016</b>								
NZ	BusinessNZ Manufacturing PMI	Oct				57.7	22.30	8.30
NZ	Food Prices MoM	Oct	-0.9			-0.9	22.45	8.45
JN	PPI MoM/YoY	Oct		0/-2.6		0.0/-3.2	0.50	10.50
AU	RBA's Debelle Panel Participation at FINSIA Regulators Panel in Melbourne						2.00	12.00
JN	Tertiary Industry Index MoM	Sep		-0.2		0.0	5.30	15.30
GE	CPI MoM/YoY	Oct F		0.2/0.8		0.2/0.8	8.00	18.00
GE	CPI EU Harmonized MoM/YoY	Oct F		0.2/0.7		0.2/0.7	8.00	18.00
UK	Construction Output SA MoM/YoY	Sep		0/-0.4		-1.5/0.2	10.30	20.30
JN	Machine Tool Orders YoY	Oct P				-6.3	11-14 Nov release	
US	U. of Mich. Sentiment/5-10 Yr Inflation	Nov P		87.9/		87.2/2.4	16.00	2.00
<b>Upcoming Central Bank Interest Rate Announcements</b>								
New Zealand, RBNZ		10-Nov	1.75%	1.75%		2.00%		
Australia, RBA		1-Dec	1.50%	1.50%		1.50%		
Canada, BoC		7-Dec				0.50%		
Europe ECB		8-Dec				0.00%		
US Federal Reserve		15-Dec	0.25-0.50%	0.25-0.50%		0.25-0.50%		
UK BOE		15-Dec				0.25%		
Japan, BoJ		20-Dec				-0.1% to +0.1%		

GMT: Greenwich Mean Time; AEDT: Australian Daylight Savings Time



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