JULY 2024

BSP TREASURY & MARKETS MONTHLY MARKET PULSE

GLOBAL MARKETS

In Q2 2024, strong economic momentum supported equity markets, despite initial concerns about US overheating and persistent inflation tempering rate cut expectations. Europe also maintained robust economic momentum amid previous cost-of-living shocks.

COMMODITIES

Commodity prices fluctuated: Brent Crude Oil amid geopolitical tensions, Natural Gas due to weather patterns, Gold on economic uncertainty, Copper with global demand, Arabica Coffee and Cocoa with market conditions, and CPO influenced by economic factors and supply dynamics.

FX MARKETS

PNG's FX market hit a record K5.24 billion turnover with increased exporter activity. BPNG's two auctions totaled US$125 million, down from US$190 million in May, reducing FX orders. The PGK depreciated against the USD by 8 basis points, a slowdown from previous months.

MONEY MARKETS

BPNG's successive CRR increases tightened market liquidity, raising interest rates and pushing the 364-day T-bill yield above 4%, its highest since January 2023. BPNG is expected to pause, evaluating these measures' impact before deciding on next steps to ensure financial stability.

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GLOBAL MARKETS

In Q2 2024, the robust economic momentum from Q1 persisted, marking another positive period for equity markets. Initially, concerns over US overheating dampened investor expectations for central bank rate cuts, despite strong April data. However, as the quarter progressed, these concerns eased and hopes for a soft landing resurged. In Europe, economic momentum remained favorable as the impact of recent cost-of-living shocks diminished.

Persistent inflation tempered the benefits of continued economic growth. Despite fears being somewhat overstated at Q1's end, service sector inflation remained stubbornly above central bank targets. Consequently, markets scaled back their expectations for rate cuts compared to earlier in the year.

Against this resilient backdrop, developed market equities achieved a 2.8% total return for the quarter, driven primarily by larger companies. Conversely, smaller cap stocks and REITs, sensitive to interest rates, underperformed amid expectations of prolonged higher rates. Fixed income investors faced another challenging quarter, with global investment grade bonds posting negative returns of -1.1%.

Companies involved in artificial intelligence continued to lead the market, contributing to another strong quarter for global growth stocks, which posted a 6.4% return. The US tech sector's robust earnings season bolstered this performance. In Europe, Japan, and the UK, value stocks outpaced growth stocks.

GLOBAL MARKETS

Asia

Chinese government efforts to support the real estate sector lifted Chinese equities, complemented by strong gains in Taiwan's AI-focused market. Asia ex-Japan equities surged 7.3% for the quarter, buoyed by the region's substantial weight in emerging markets, which outperformed developed markets with a 5.1% return despite subdued returns in Latin America.

Europe

Following the European parliamentary election, President Macron's call for a snap election in France heightened market volatility. The French equity market declined sharply by -6.4% in June, weighing down broader European returns to just 0.6% for the quarter. Meanwhile, the UK's improving economic outlook contributed to a 3.7% gain for the FTSE All-Share.

US

In Q2, US economic data softened after an initial uptick in April, consistently falling below consensus from early May. Despite this, the Federal Reserve adopted a hawkish stance at its June conference, removing most anticipated rate cuts for 2024. However, weaker US consumer data fostered some investor optimism for policy easing, with markets still pricing in two cuts by year-end. Consequently, despite revised Fed expectations, US Treasury yields ended the quarter unchanged, and US Treasuries were the sole major sovereign market to yield positive returns at 0.1%.

The European Central Bank (ECB) joined other developed markets in cutting interest rates, a move widely anticipated before its June meeting. Persistent services inflation, however, compelled the ECB to emphasize a cautious approach to further policy adjustments contingent on economic data. Despite rate cuts, European sovereign yields rose amid post-election uncertainties, resulting in negative returns for European government bonds during the quarter.

In the UK, sticky services inflation prevented a rate cut in June despite earlier signals from the Bank of England (BoE). Temporary relief in headline inflation returning to target in June was anticipated, but strong wage growth and projected inflation resurgence precluded immediate rate reductions. The BoE indicated potential action in August, while UK Gilts posted negative returns of -1.1% amid rising yields throughout the quarter.

In a supportive macroeconomic environment, riskier segments of fixed income thrived. Strong Q2 economic activity bolstered corporate earnings, keeping default rates low and spreads tight. European and US high yield bonds led the fixed income sectors with returns of 1.5% and 1.1%, respectively. These sectors benefited from robust coupon payments and lower sensitivity to moderately higher sovereign yields in Europe and the UK.

FOREIGN EXCHANGE MARKETS

PGK/USD

In June, the foreign exchange (FX) market achieved a record turnover of K5.24 billion, marking a robust performance for the first half of the year. This growth was driven primarily by increased exporter activity throughout the month. The Bank of Papua New Guinea (BPNG) conducted two FX auctions totaling US$125 million during June, a notable decrease from May's US$190 million. Consequently, outstanding FX orders in the market decreased significantly, currently estimated at around one billion kina as we enter the second half of the year.

The pace of the PGK's gradual depreciation against the US dollar has slowed notably in the past four weeks. In June, the PGK/USD rate declined by only 8 basis points, averaging a reduction of 2 points per week. This contrasts with declines of 21 points in May and 20 points in April.

PGK/AUD

On June 10th, the PGK reached its highest level of 0.3952 against the AUD for the month, subsequently declining to a low of 0.3891 on June 26th. By the end of the month, the kina concluded at 0.3925 against the AUD. These exchange rate movements reflect the fluctuating dynamics observed in currency markets during the period.

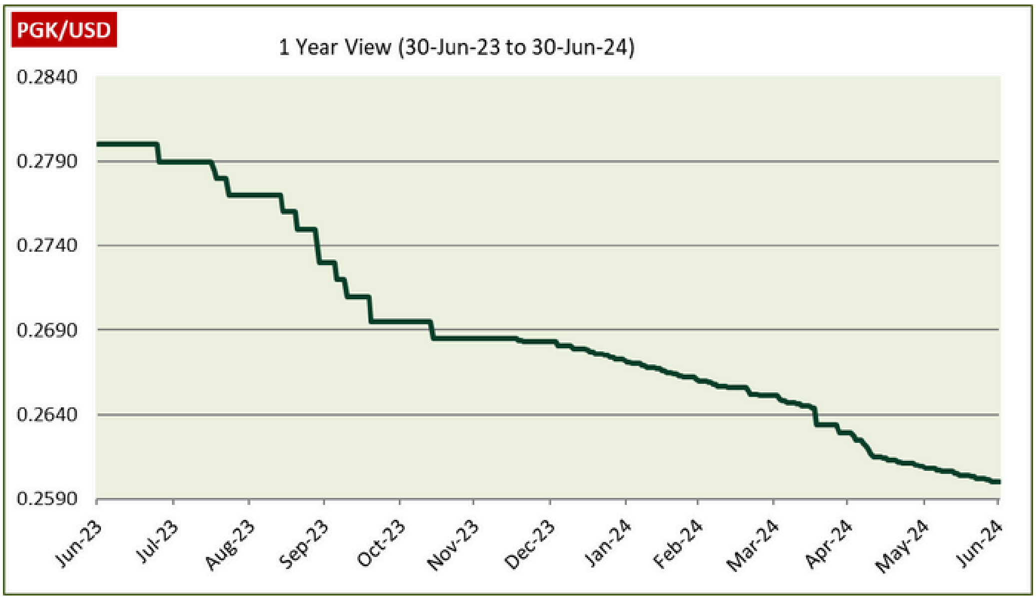
AUD/USD

Australia's recent inflation report, showing a year-over-year increase in headline CPI to 4%, has heightened concerns over rising inflationary pressures. This has raised the likelihood that the Reserve Bank of Australia (RBA) could raise rates by 25 basis points at its August meeting. The Australian government's initiatives addressing the 'cost of living crisis' are also seen as potentially inflationary. While the effectiveness of a rate hike in curbing inflation is debated, the RBA may opt for a preemptive move to demonstrate its commitment to managing inflationary risks. Consequently, the upcoming RBA meeting is expected to adopt a notably hawkish stance, despite the possibility of rates remaining unchanged at 4.35%.

Market indicators suggest a 45% probability of a 25 basis point rate hike at the RBA's next meeting, with overnight index swap rates indicating a more probable 65% chance. Major financial institutions such as Morgan Stanley, UBS, and Citi are advocating for a rate increase.
While attention will be on the RBA minutes scheduled for Tuesday, recent discussions within the RBA have focused on potential rate hikes rather than cuts. However, the direction of the AUD/USD pair is likely to be influenced more by upcoming US economic data, which has shown signs of weakening. If risk appetite remains robust, this could support further gains for the AUD/USD pair.

FOREIGN EXCHANGE MARKETS

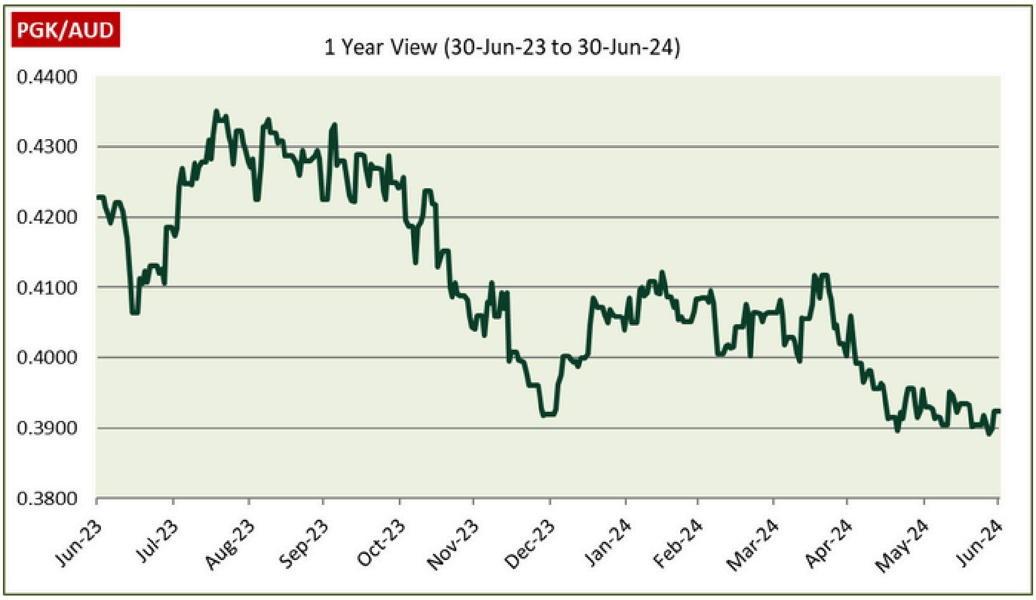
PGK/USD



PGK/USD

The pace of the PGK's depreciation against the USD slowed noticeably over the past 4 weeks. In June, it dropped by 8 basis points, averaging 2 points per week, contrasting with declines of 21 and 20 points in May and April, respectively.

PGK/AUD



PGK/AUD

On June 10th, the PGK peaked at 0.3952 against the AUD, then fell to 0.3891 on June 26th, ending the month at 0.3925. These movements reflect volatility in currency markets.

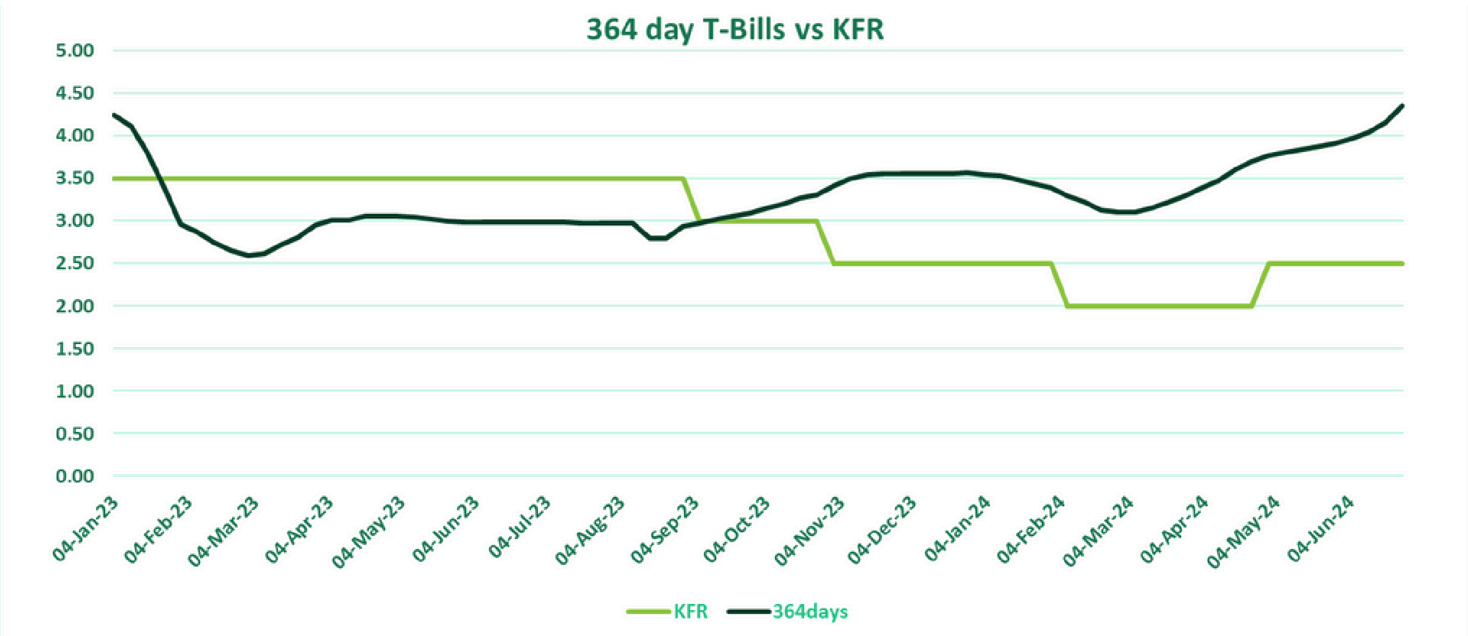
MONEY MARKETS

The Bank of Papua New Guinea (BPNG) has implemented two consecutive increases in the Cash Reserve Ratio (CRR) in May and June, resulting in a tightening of market liquidity and subsequent increases in interest rates. These adjustments have withdrawn PGK 730 million of system liquidity from the market, moving the CRR from 7% of total bank deposits during the Covid-19 period to the current level of 12%.

This adjustment has notably elevated the yield on the 364-day Treasury bill, surpassing 4% and marking its highest level since January 2023.

Given these developments, it is generally anticipated that BPNG may adopt a cautious approach, pausing to assess the effects of these recent policy measures before considering any additional actions. This monitoring phase is crucial to gauging the overall impact on financial conditions and ensuring stability within the monetary framework.

Auction	Central Bank Bills					Treasury Bills					
Date	7	14	28	63	91	28	63	91	182	273	364
Previous	2.50								2.30	2.46	3.92
05-Jun-24	2.50								2.52	2.52	3.97
12-Jun-24	2.50								2.80	-	4.04
19-Jun-24	2.50								3.00	2.52	4.16
26-Jun-24	2.50								-	2.64	4.35
		-	-	-	-						
Movement	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.70	0.18	0.43



COMMODITIES

Brent Crude Oil

In June, Brent Crude Oil experienced notable price volatility influenced by geopolitical tensions and global economic indicators. Prices began the month at $90 per barrel, fluctuating between highs near $95 and lows around $88. Supply disruptions in key producing regions and shifts in demand forecasts amid economic recovery efforts shaped market sentiment. Overall, June saw Brent Crude Oil prices responding dynamically to geopolitical developments and economic data, reflecting ongoing uncertainties in global oil markets.

Natural Gas

The natural gas market witnessed significant price movements influenced by various factors. Prices started the month strong at $4.50 per million British thermal units (MMBtu) but fluctuated widely throughout the period. Geopolitical tensions, weather patterns affecting demand, and supply dynamics played key roles in shaping market trends. Despite occasional spikes to around $5 per MMBtu due to supply disruptions and increased summer cooling demand, prices moderated towards the end of the month, settling around $4.20 per MMBtu. Overall, June demonstrated the volatility inherent in natural gas markets, driven by a complex interplay of geopolitical events and seasonal demand patterns.

Gold

The price of gold exhibited notable movements amid fluctuating economic indicators and global uncertainties. Beginning the month at $1,900 per ounce, gold prices initially saw volatility influenced by shifts in inflation data and central bank policies. Mid-month, geopolitical tensions spurred safe-haven demand, briefly pushing prices above $1,950 per ounce. However, as economic data suggested mixed signals regarding global growth, gold prices retreated towards the end of June, stabilizing around $1,920 per ounce. Overall, June highlighted gold's role as a hedge against economic uncertainty, with prices responding sensitively to market developments and investor sentiment.

Copper

Copper prices experienced fluctuation influenced by various global economic factors. Beginning the month at $4.50 per pound, copper initially showed strength as demand from infrastructure projects and manufacturing sectors remained robust. However, concerns over supply chain disruptions and geopolitical tensions weighed on market sentiment mid-month, causing prices to dip below $4.40 per pound temporarily. As the month progressed, positive economic data from major economies supported a rebound in copper prices, which closed around $4.55 per pound by the end of June. Overall, June demonstrated copper's sensitivity to economic indicators and global supply dynamics, reflecting its pivotal role in industrial and construction sectors worldwide.

COMMODITIES

Coffee

Arabica coffee prices experienced volatility influenced primarily by weather conditions in key producing regions, particularly Brazil. Starting the month at approximately $2.20 per pound, prices initially surged due to concerns over adverse weather potentially affecting crop yields. However, as mid-month reports indicated improved weather patterns in Brazil, prices retreated to around $2.10 per pound.

The market remained cautious and reactive to ongoing weather updates, which continued to influence sentiment and price movements. Towards the end of June, Arabica coffee prices stabilized around $2.15 per pound as traders awaited further crop assessments and monitored global demand dynamics.

The month underscored the significance of weather forecasts in determining Arabica coffee prices, reflecting the market's sensitivity to supply expectations and their impact on global coffee production.

Cocoa

The cocoa market saw moderate price movements influenced by various factors. Beginning the month at $2,500 per ton, cocoa prices initially showed resilience amid steady demand from confectionery and food industries. Mid-month, concerns over global economic uncertainties and fluctuating currency exchange rates contributed to slight fluctuations, with prices briefly touching $2,480 per ton.

Towards the end of June, market sentiment stabilized as supply expectations from major cocoa-producing countries remained steady. Cocoa prices closed the month around $2,490 per ton, reflecting cautious optimism amidst ongoing economic developments and supply dynamics.

Overall, June highlighted cocoa's sensitivity to economic conditions and market sentiment, with prices responding to both demand fundamentals and external economic factors influencing global trade.

Palm Oil

The Crude Palm Oil (CPO) market saw dynamic price movements influenced by multiple factors. Beginning the month at $1,200 per metric ton, CPO prices benefited from strong demand driven by biofuel and food industries. However, mid-month, concerns over global economic uncertainties and fluctuations in competing vegetable oil prices introduced volatility, with prices briefly declining to $1,180 per metric ton.

Towards the end of June, market sentiment stabilized amid reports of consistent demand from major importers and favorable weather conditions in key palm oil producing regions. CPO prices closed the month around $1,190 per metric ton, reflecting a cautious market outlook amidst ongoing economic developments and supply dynamics.

The month highlighted the CPO market's responsiveness to global economic conditions, competitive vegetable oil prices, and production-related factors, influencing price trends throughout June.

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