Central Bank Weekly April 14th: Previewing RBA minutes, China LPR; Reviewing ECB, BoC, BNZ, BoC, BoK, CBRT

14th April 2022:

RBA MINUTES (TUE): The focus of the minutes will likely be around more information regarding the timing of a rate hike. As a reminder, a hawkish hold by the RBA saw the Cash Rate maintained at 0.1%, but the reference to a “patient” monetary policy approach was scrapped. The statement made it clear that it had shifted more aggressively to focus on inflation. The statement made no direct hints as to the timing of any rate hikes. However, last Friday, the RBA Financial Stability Review said it is important that borrowers are prepared for an increase in interest rates, and global asset markets are vulnerable to larger-than-expected rate increases. Any colour around this will attract the most attention.

CHINESE LPR (WED): The PBoC will decide on its benchmark lending rates next week where participants will be eyeing whether the central bank will reduce or maintain the 1-Year Loan Prime Rate at the current 3.70% level and with the 5-Year Loan Prime Rate at 4.60% which is the reference for mortgages. There are expectations for the PBoC to resume policy loosening to support a slowing economy caused by the pandemic and China’s strict zero-COVID approach that has resulted in city-wide lockdowns in some areas including China’s most populous city of Shanghai, while global demand is also seen softening owing to the Ukraine war and as several major central banks across the world begin to normalise policy. As such, many anticipate the PBoC will reduce interest rates with 15 out 20 analysts surveyed by a major newswires expecting a reduction in the Medium-term Lending Facility as early as this Friday which if lowered, would virtually guarantee a cut to the LPR next week, while Chinese press reports have also noted that a RRR cut was likely during Q2 and Citi even see the possibility for China to reduce RRR this Friday which would free up CNY 1.2tln of funds. Conversely, some economists see a narrower scope for a rate cut given the recent firmer than expected inflation data for China and after China’s 10yr government bond yield briefly fell beneath its US counterpart for the first time in 12 years earlier this week, therefore, effectively lowering the appeal for Chinese bonds and which policymakers may want to avoid further exacerbating.

ECB REVIEW: As expected, the ECB refrained from tweaking its monetary policy settings with rates left unchanged and the parameters of its bond-buying operations maintained. As such, the ECB will lower purchases under APP to EUR 30bln from EUR 40bln in May and then to EUR 20bln in June before concluding in Q3. Elsewhere, policymakers opted to include a new line in the statement which states "the Governing Council will maintain optionality, gradualism and flexibility in the conduct of monetary policy". The initial market reaction to the statement was a dovish one with a lack of specificity on when in Q3 purchases will conclude, serving as a disappointment to some who had been hoping for greater clarity. An end in "early Q3" would have opened the door for some of the more hawkish expectations in the market which had pencilled in two 25bps hikes by year-end. At the accompanying press conference, introductory remarks from Lagarde stated that several factors point to low growth ahead, new pandemic measures in Asia are contributing to supply chain issues and inflation pressures have intensified across many sectors. Furthermore, risks remain tilted to the downside and risks have intensified. On policy measures, Lagarde refrained from providing any greater clarity on when in Q3 purchases under APP will conclude and reiterated her line from the previous press conference that the "some time" linkage between the end of APP and start of rate hikes could mean "weeks" or "several months". Furthermore, Lagarde didn't add anything to reporting last week which suggested that the Bank was looking at crafting a crisis tool if bond yields were to jump. Overall, with the ECB avoiding providing much in the way of signalling for when to expect any adjustments in the normalisation process, all eyes are now on the June meeting which will be accompanied by the latest round of economic projections and should see policymakers provide greater clarity on what to expect heading towards H2. That said, messaging from the ECB is very much one of "flexibility" at this stage of the process.

RBNZ REVIEW: RBNZ hiked the OCR by 50bps to 1.50% (exp. 25bps increase) and said it will remain focused on ensuring that current high consumer price inflation does not become embedded into longer-term inflation expectations. The RBNZ’s decision to hike rates for a fourth consecutive meeting was unsurprising and fully priced in by OIS and although the consensus was for just a 25bps increase, there were outside calls for a more aggressive move of 50bps including from ANZ Bank which also expect a consecutive 50bps hike in May. The central bank stuck with a hawkish tone as the Committee agreed that their policy 'path of least regrets' is to increase the OCR by more now rather than later and noted that further increases in the OCR are needed in order to meet their mandate. However, the RBNZ said it remains comfortable with the outlook on the OCR as outlined in the February MPS which suggested that the more aggressive move could just be front-loading and that its view of the destination for rates remains unchanged which resulted in an unwinding of the initial hawkish reaction. Nonetheless, Westpac suggested the RBNZ was focused on explaining the decision rather than providing a signal and that there was nothing in the statement that explicitly argued against a consecutive 50bp hike in May, while both ASB Bank and Kiwibank have joined in on the calls for 50bps increase next month.

BOC: The Bank of Canada lifted interest rates by 50bps, taking its Policy Interest Rate to 1.00%; while the rate hike was in line with expectations, some had expected a smaller 25bps move. The BoC also announced it is to end reinvestments of maturing bonds, and will begin the process of quantitative tightening at the end of April. The central bank expects inflation to return to 2% in 2024, in line with analyst expectations. However, it noted there was an increasing risk that expectations of elevated inflation could become entrenched. The bank noted that the policy rate remains its primary tool and QT will complement rate increases. It also reiterated that policy will be determined by its ongoing assessment of the economy and its commitment to bring inflation to target. In its Monetary Policy Report, the bank revised inflation forecasts upwards, pencilling in an inflation rate of 2.1% in 2024; growth forecasts were also revised up in the near-term as the economy weathered Omicron better than initially feared. However, its 2023 GDP view was cut slightly. The output gap was estimated to be between -0.25% and 0.75% from the previous -0.75% and 0.25%. Its estimate of the neutral rate was also lifted by 25bps to a midpoint of 2.5% from 2.25%. The MPR, statement and press conference told us little new on the balance sheet other than it will shrink over time, with roughly 40% of the bank's holdings of Canadian government bonds due to mature within the next two years. Although a statement was released reiterating that the BoC was not actively considering selling bonds as part of its QT process, it will continue to implement monetary policy via a floor system that will remain in place even after QT is over. During his post-meeting press conference, Governor Macklem noted that if demand responded quickly to higher rates and inflationary pressures moderated, it might be appropriate to pause hikes once rates get closer to neutral. But Macklem also suggested that the bank may need to take rates modestly above neutral for a period of time. Macklem said that we can expect rates to continue to rise towards more neutral settings of between 2-3% while he noted that the 50bps hike shows that monetary policy needs to be normalised quickly. The Governor added that higher rates were needed, and he was confident that the economy can handle them, adding that the bank would act forcefully if needed. Analysts at RBC expect 25bps hikes going forward until the overnight rate hits 2% in October, but it does believe another 50bp increase will be an option on the table in June.

BOK REVIEW: Bank of Korea unexpectedly raised its Base Rate by 25bps to 1.50% with the decision unanimous, while the MPC chief said they couldn't wait for the formal appointment of a Governor to resume the fight against inflation and that the views among BoK board members are seen diverging. BoK said South Korea's growth is to sustain a recovery, but will be lower than previously projected and inflation will run higher than estimated earlier, according to Reuters. Analysts at ING will be closely watching the governor-nominee Rhee Chang-Yong's parliamentary hearing scheduled on 19 April for his views on the economy. The desk believes the BoK will opt for "two more rate hikes in the second half of this year. However, once inflation begins to slow down in the third quarter of 2022, then BoK's focus will shift to financial stability and growth".

CBRT REVIEW: The CBRT maintained its one-week repo rate at 14.00% as expected. The statement reiterated the comprehensive review of the policy framework continues with the aim of encouraging permanent and strengthened liraization in all tools of the CBRT. The Committee repeated it will continue to take its decisions in a transparent, predictable and data-driven framework and expects the disinflation process to start on the back of measures taken and decisively pursues sustainable price and financial stability along with the decline in inflation owing to the base effect and the resolution of the ongoing regional conflict. All-in-all, there were no surprises and the release was mostly a copy-and-paste job from the prior meeting.