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# Week Ahead 23-27th May: Highlights include FOMC minutes, US PCE data, Flash PMIs, RBNZ

## Week Ahead 23-27th May:

- **SAT:** Australia Federal Election.
- **SUN:** Davos World Economic Forum (22nd-26th May).
- **MON:** German Ifo Survey (May); New Zealand Retail Sales (Q1); ISM Semi-Annual Economic Forecast.
- **TUE:** EZ, UK, US Flash PMIs (May).
- **WED:** FOMC Minutes; RBNZ Announcement; German Prelim CPI (May); US Durable Goods (Apr).
- **THU:** BoK Announcement, CBRT Announcement, US GDP 2nd (Q1).
- **FRI:** Chinese Industrial Profits (Apr); US Personal Income, Consumption, PCE (Apr).

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***NOTE: Previews are listed in day-order***

**AUSTRALIA FEDERAL ELECTION (SAT):** Australians will head to the polls on Saturday to vote in the Federal Elections, with the incumbent PM Morrison's ruling Liberal-National Coalition facing an uphill battle to secure a fourth term in power. The opposition centre-left Labor Party (ALP) has led in nearly all surveys before the start of campaigning in April, although the ruling centre-right Coalition has been catching up; the latest IPSOS poll put Labor's lead at just one point vs the six point advantage it had a fortnight ago. PM Morrison is also no stranger to overcoming the odds, and made a 'miraculous' comeback at the last election in 2019, despite exit polls predicting a strong Labor win. According to Roy Morgan Research, ALP is set to win a narrow majority based on either State-by-State swings or a uniform national swing, while desks see no substantial difference between parties in key areas, including tax policy and foreign relations, although there are expectations for a likely change in the hawkish rhetoric on China under a Labor government. Polling will occur from 8am to 6pm local time, and 76 seats are required for a majority in the Lower House. From a market perspective, the most bearish scenario would be a hung parliament. Analysts at Nomura do not expect a material reaction; they say "AUD could rise a fraction (up to 1%) on an LNP victory, and fall by a similar amount on a Labor win, given a perception by some that the LNP is a better manager of the economy. Bond yields could rise by a few basis points on a Labor win, given that budget deficits may be modestly larger under a Labor government. However, the LNP's new plan to allow first-home buyers to access some of their retirement savings to purchase a home could also push up short-end rates if the government is returned."

**DAVOS WORLD ECONOMIC FORUM (SUN-THU):** Global leaders will meet in Davos, Switzerland, for the World Economic Forum's (WEF) Annual Meeting 2022. This year's event is centred around "History at a Turning Point: Government Policies and Business Strategies", where the Ukraine crisis likely to take the spotlight. German Chancellor Scholz, US climate envoy Kerry, NATO Secretary-General Stoltenberg and European Commission president von der Leyen are among the event headliners. The leaders are likely to pledge support for Ukraine whilst telegraphing a shift away from Russian energy to clean energy and will likely reaffirm vows to fight inflation. Major and imminent policy decisions are unlikely to be agreed upon at the gathering.

**NEW ZEALAND RETAIL SALES (MON):** Analysts at Westpac are forecasting NZ retail sales will rise 2.2% in Q1 vs +8.6% in Q4 (which was mostly driven by growth in durable items; hospitality remained weak). "Much of the Q1 rise is related to a lift in new car sales, with households rushing to beat the price change for less energy-efficient vehicles," Westpac says. The data is unlikely to shift the dials much given the quarterly nature of the release and since the release will be on the eve of the RBNZ – most analysts anticipate that the central bank will increase rates by 50bps.

**EZ FLASH PMI (TUE)**: Expectations are for the flash May manufacturing metric to decline to 55.0 from 55.5, services to rise to 57.9 from 57.7, leaving the composite at 55.0 vs the previous 55.8. The April report was characterised by an increase in the services print from 55.6 to 57.7, whilst the manufacturing metric fell to 55.5 from 56.5. S&P Global noted that the "data highlighted the growing emergence of a two-speed economy across the euro area as faster service sector growth starkly contrasted with a slowdown across manufacturers". Looking ahead, Nordea expects "rising prices, monetary tightening, and dwindling household savings to take its toll on both the manufacturing and the service industry. The service sector, however, is likely to stay robust in the coming months, while the cyclical manufacturing industry is set for a large slowdown as tightening of financial conditions and reopening of the economy will skew consumption back towards services and away from goods". From a policy perspective with an end to the ECB's APP as of July 1st and a

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July 21st rate hike firmly baked into the market consensus, the upcoming PMI release is unlikely to have much sway on the June 9th ECB announcement. However, market participants will be cognizant of forthcoming releases to assess the extent of the expected slowdown in the region and whether this narrows the "window of opportunity" for the ECB to move on rates before an expected pause either later this year or early 2023.

**UK FLASH PMI (TUE)**: Expectations are for the flash May services metric to decline to 58.1 from 58.9, manufacturing to slip to 55.2 from 55.8, leaving the composite at 57.4 vs the previous 58.2. The April report saw survey respondents cite subdued consumer demand due to squeezed household finances and rising prices for essential items whilst "business-to-business spending was hit by higher operating expenses, inflation concerns and geopolitical uncertainty". This time around, analysts at Investec expect "business activity in the service sector may have declined a little further as rising prices weighed on discretionary spending volumes". On the manufacturing front, Investec cautions that the past weakening in orders is expected to translate into somewhat more subdued output. From a policy perspective, the release is unlikely to have much of an impact on the June MPC decision to lift rates. However, a downbeat release which emphasises subdued activity as a result of squeezed household incomes could prompt some market participants to further question current pricing which looks for five 25bps hikes by year-end. This comes as policymakers at the BoE continue to stress that they are walking a tightrope between controlling inflation and avoiding a recession.

**FOMC MINUTES (WED):** The Federal Reserve's May policy announcement was in keeping with market expectations. It lifted the Federal Funds Rate target by a 50bps increment to 0.75-1.00%, while the statement continued to suggest the Committee anticipates that "ongoing" rate rises will be appropriate. At the post-meeting press conference, Chair Powell leaned back against calls that the Fed could lift rates in 75bps increments, stating that the Committee was not actively considering hikes of that magnitude, and arguing that 50bps moves at the next "couple" of meetings was likely to be appropriate. The Committee also announced a phased-in start to balance sheet normalisation beginning in June (some were expecting the process to begin in May); the maximum monthly caps will start at USD 30bln and USD 17.5bln for Treasuries and MBS respectively, ramping up to USD 60bln and USD 35bln over three-months. Powell said the effects of balance sheet reduction were uncertain, but there are estimates that it could deliver the equivalent of a 25bps hike over the course of a year, perhaps biasing the neutral rate to the low-end of forecasts. The Fed alluded to the negative GDP print in Q1, saying that although overall economic activity edged down, household spending and business fixed investment remained strong. Chair Powell is also confident that the Fed can engineer a soft economic landing as it lifts rates in the face of a growth slowdown, though he constantly caveated the challenges the central bank would face in that endeavour. Powell was dismissive about the prospects of an outright recession, and he said that there was nothing in the economy that suggests it was close to a recession, though that was not to mean there will not be some slowing of growth. On the notion that the Fed could lift policy above estimates of the neutral rate – something economists say will begin to restrict economic activity from the current accommodative stance – Chair Powell repeated that the Committee would not hesitate to hike above that level (which the Committee sees between 2-3%), but said that this was not a decision to be made now, implying he was in the camp that favoured raising rates to neutral and then assessing the magnitude to which further rate rises were needed. Since the meeting, financial markets have seen episodes of sharp risk-off amid concerns about global inflation and a slowing growth impulse. Some had expected Fed officials to dial-down hawkishness in order to cushion the unwarranted tightening of financial conditions engineered by the sharp risk-off, however, key officials have not gone down this route; hawks like Bullard appear to be in line with the consensus of 50bps rate rises at the June and July meetings, while doves like Evans do not appear to be wavering as risk assets slide, all suggesting that the central bank would stay its course in tightening policy for now. One of the key emerging debates seems to be focussed on what the Fed will do when it gets rates to neutral: will it pause the hikes and assess the situation, or will it revert to shallower 25bps increments rate lifts. Chair Powell this week reiterated the case that the Fed would continue with hikes until inflation was back at target. Given the Fed's challenge in dealing with high inflation, this line from Powell is to be expected – backing away from it now risks undoing the initial work in lowering inflation expectations. However, analysts will be looking to the minutes for any hints on how the Fed could inject dovishness while staying the course regarding normalisation; analysts have speculated that the Fed might be able to project some dovishness by alluding to a lower terminal rate in this cycle, pausing when rates get to neutral; it could even suggest that the need for a larger 75bps increment hike was lower.

**RBNZ RATE DECISION (WED):** The RBNZ is expected to continue its hiking cycle, and most analysts are anticipating it will lift rates by a 50bps increment; OIS fully price in a 25bps hike with around a 90% probability of a the larger 50bps move. The RBNZ has consecutively hiked rates for the last four meetings, and even surprised markets in April with a larger than expected increase of 50bps (exp. 25bps), while it stated at the past meeting that it will remain focused on ensuring current high consumer price inflation does not become embedded into longer-term inflation expectations and monetary tightening was brought forward, but noted it remains comfortable with the outlook on the OCR as outlined in the February MPS. This suggests the central bank's more aggressive move in April was just front loading and its view for the actual destination of rates remains unchanged in which it had previously forecast the OCR at 2.84% in June 2023, and at 3.35% in March 2025. Nonetheless, the central bank is likely to continue the front loading; Westpac expects three more 50bps rate hikes, ASB Bank and Kiwibank look for a 50bps hike at the upcoming meeting with the argument for tighter policy supported by inflation data after New Zealand CPI for Q1 rose at its fastest pace in 32 years.

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**BOK RATE DECISION (THU):** The Bank of Korea is likely to continue its hiking cycle and lift its 7-Day Repo Rate by 25bps to 1.75% in its first meeting under the stewardship of newly-appointed Governor Rhee. As a reminder, the BoK defied consensus for a pause at last month’s meeting and surprised markets by unanimously opting for a 25bps rate rise, with policymakers unwilling to wait for the formal appointment of a Governor to resume their fight against price pressures. This decisiveness to tighten policy is expected to continue during Governor Rhee’s term, as he previously noted that the BoK should continue hike rates unless it poses a problem for growth and stated that household debt needs to slow via ongoing tightening, while he also kept the door open to the possibility of a future 50bp move, which he suggested they will be able to determine if required after seeing the data for July-August. Furthermore, Rhee and Finance Minister Choo recently agreed to boost policy coordination to fight inflation and market instability, while the latest inflation data supports calls for a hike after CPI in April continued to outpace expectations and printed at its fastest increase since 2008, at 4.8% vs exp. 4.4% (prev. 4.1%).

**CBRT ANNOUNCEMENT (THU):** The CBRT is expected to maintain its One-Week Repo Rate at 14.00%. Desks note that the overall visibility and predictability of the central bank are low as recent policy decisions have not been based on conventional economic factors. Nonetheless, inflation remains high – April’s CPI metrics topped expectations, rising to 69.97% Y/Y from 61.14%, whilst PPI printed at an eye-watering 121.82% Y/Y from the prior 114.97%. “The MPC is currently monitoring the ‘cumulative impact of the recent policy decisions’, which suggests to us that it will likely remain on hold in the foreseeable future”, analysts at Credit Suisse said, adding that “authorities will probably continue to implement ad hoc measures as long as they can in order to sustain what we view as this ultimately unsustainable policy stance.” CS expects headline inflation to move towards 60-70% in the coming months and believes that the timing of a switch back to conventional policy hinges on politics as presidential/parliamentary elections will be held no later than mid-2023.

**US PERSONAL INCOME, SPENDING, PCE (FRI):** Analysts often use CPI and PPI data as a proxy for how the PCE report - the Fed's preferred measure of inflation - might look. April's CPI data disappointed expectations; although the annual measures narrowed, the rate of core inflation picked-up, challenging the notion that we are now past peak inflation. Producer prices for April gave credence to that argument, with wholesale prices rising by double-digits for the fifth straight month, a sign that firms were continuing to pass on the costs of higher prices to consumers, or face margin erosion. Citi's analysts, however, argue that we may have better news on the PCE front. PCE doesn't match CPI, they both have different methodologies. But Citi says that legislated cuts in Medicare payments could help the situation, and project core PCE will rise 0.3% M/M, matching the rate seen in the previous two reports. Any slowing of the metric may reignite calls of peak inflation, while any upside surprise could be taken as an indication that the Fed will not waiver from its hawkish rhetoric, and will continue its expeditious trajectory of tightening policy until inflation is back under control.

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