newsquawk

Central Bank Weekly June 10th : Previewing FOMC, BoE, BoJ, SNB, BCB; reviewing ECB, RBA, RBI, CBR

10th June 2022:

FOMC ANNOUNCEMENT (WED): Fed officials have heavily guided towards a +50bps rate rise at its June 15th FOMC, a move which is fully priced by money markets; the Committee is also expected to lift rates by the same magnitude at its July 27th confab. If the Fed next week raises rates in line with consensus expectations, focus will fall onto its updated economic projections. Since the Fed has pledged that it will 'expeditiously' be lifting rates towards neutral, traders will take note of the updated Staff Economic Projections for guidance on where the Fed sees the eventual terminal rate of the cycle and the longer-run neutral interest rate. The now-stale March forecasts envisaged rates rising to 1.75-2.00% by the end of this year (money markets are pricing rates at 2.75-3.00% by year-end), before peaking at 2.75-3.00% in 2023 (money markets see 3.25-3.50% by mid-2023); money market pricing, remarks from officials and analysts suggests these so-called 'dots' will be lifted. Meanwhile, the Fed's assessment of the longer-run neutral rate, which was cut in March to 2.4% from 2.5%, may see another revision lower in the June forecasts; when taking out the extremes, the general run of Fed commentary going into the June meeting has put the rate of neutral at around 2.25% among the Governors, though the regional Presidents seem to have a higher assessment than that. "If the two new Fed governors join their colleagues in their estimate of the neutral rate, the central tendency estimate will decline again in June," Moody' s has explained, "at 2.25%, the Fed's estimate would still be higher than the most referenced model for estimating neutral fed funds, which puts it closer to 2%." Finally, updated economic projections, in addition to revising up the foreseen trajectory of rates, it is likely that the profile of inflation will be raised in the near-term, and growth expectations will be lowered, as has been seen in the OECD's recently updated economic projections. At Chair Powell's post meeting press conference, traders will be looking towards any commentary that gives clues on what the Fed will do after it has raised rates by 50bps increments in June and July; while some had envisaged that the central bank would pause and assess the situation, remarks from some officials, like the influential Governor Brainard, suggest that falling back to smaller increments of rate rises are the base case, dependent on the progress of inflation. Chair Powell will also likely emphasise that tackling soaring prices remains the priority of the Committee. Additionally, many market participants are now of the view that the Fed will need to hike rates more aggressively to manage price pressures, and after the hot May CPI data–where the annual rate of inflation rose to 40yr highs, while core measures of inflation continued to rise in the month–Powell will be asked about how prepared the Fed is to raise rates above the neutral level, which would place activity into restrictive territory, potentially triggering a US recession. Fed officials in the passed have suggested that they stand ready to do exactly that if the data requires.

BCB ANNOUNCEMENT (WED): Brazil's May IPCA-15 data showed inflation rising by +0.6% M/M (exp. 0.5%), while the annual rate rose to +12.2% Y/Y (exp. 12.0%, prev. 12.0%). Pantheon Macroeconomics noted that Brazil's inflation dynamics continues to deteriorate. "Upside risks persist due mostly to worsening supply chains, high commodity prices, particularly fuel, and a relatively resilient domestic recovery, following the Omicron wave," but adds "that said, upside pressures in some key components are no longer increasing." PM expects inflation will ease in the months ahead, to around 8.5% Y/Y by the end of 2022 on the back of favourable base effects. "We think that the headline rate will hover around its current level over the next few months, but that a gradual headline inflation downtrend will emerge over Q3," it says, "the COPOM probably will hike by 50bps to bring expectations down, but will recognise that further rate increases will put the economy under severe strain."

BOE ANNOUNCEMENT (THU): Policymakers are expected to continue with the rate hiking cycle by delivering another 25bps rate rise, taking the Bank Rate to 1.25%. The decision to move on rates is expected to be unanimous, however, the split of views regarding the magnitude of the move remains to be seen, given that there were three dissenters at the May meeting. The need to continue raising rates was underscored by the jump in April's CPI metrics, which printed 9.0% from 7.0%. With further increases in inflation likely in the months ahead, and the MPC expects consumer prices to average a little over 10% at its peak in Q4 2022. From a growth perspective, the recent survey data from S&P Global highlighted the difficult economic backdrop in the UK, and the likelihood of a stagflationary environment going forwards, with the services metric slipping to 53.4 in May from 58.9. Accompanying commentary from S&P Global noted "the monthly loss of momentum for business activity expansion was a survey record outside of lockdown periods." That said, policymakers will have found some comfort in the latest government support measures aimed at addressing the cost-of-living crisis, which could boost nominal GDP by around 0.7% in H2 2022. In terms of guidance from the MPC itself, Governor Bailey has flagged concerns that pay growth will feed into inflation and is prepared to raise rates again if needed. Furthermore, Chief Economist Pill has stated that when it comes to lifting interest rates, "further work needs to be done." Note, current market pricing has continued to pick up since the prior meeting and now looks for around

Copyright © 2022 Newsquawk Voice Limited. All rights reserved.
Registered Office One Love Lane, London, EC2V 7JN, United Kingdom · Registered Number 12020774 · Registered in England and Wales.
newsquawk.com · +44 20 3582 2778 · info@newsquawk.com

another seven 25bps hikes by year-end. This continues to remain at odds with guidance from the MPC itself which at the May meeting noted that the implied market path would see inflation firmly below target in three years-time at around 1.3%. Therefore, as the year progresses, desks are still widely of the view that some of this exuberant pricing will need to be taken out of the market.

SNB ANNOUNCEMENT (THU): Overall, likely to keep the Policy Rate at -0.75% at the June gathering as, on balance, financial conditions do not merit an unguided deviation from current policy at this point in time. However, widening interest differentials, particularly with relation to the EZ as the ECB are set to hike in July and September are of note and imply further currency-driven inflationary pressures ahead. Pressure that Switzerland is already cognisant of with CPI surpassing market expectations for the last three readings to a YTD peak, thus far, of 2.9% YY; a measure that already exceeds the SNB's expected peak of 2.2% for 2022, via March forecasts. As such, the June forecasts will receive upward revisions and attention will be on what they expect the peak to be and when it is forecast to occur – note, while elevated, Swiss inflation is far from the levels exhibited by global peers. From the SNB itself, we have seen somewhat mixed commentary from officials on the inflation situation; with Chairman Jordan acknowledging the increase in global inflation, Board Member Maechler taking a more 'hawkish' line, making clear that they will not hesitate to increase rates if inflation remains outside the target. Most recently, and perhaps pertinently, outgoing Vice-Chairman Zurbrugg spoke on May 31st, when he would have been privy to the embargoed May CPI print (2.9% YY), commenting that inflation is low vs other nations and believes the drivers are temporary; remarks which perhaps serve to dilute some of the notion around the SNB taking near-term action. Note, while the September and December meetings may well be considered 'live' from a rates perspective, and particularly September if the ECB does deliver more than 25bp at that point; the likes of Credit Suisse expect the SNB to drop its "highly valued" classification amid a lessening of sight deposit activity, as any notable currency depreciation would fan inflation further. Finally, although the SNB is unlikely to pre-empt the ECB and hike in June, its most recent rate alterations came via unscheduled announcements, thus, a post-ECB move in July cannot be ruled out but, as mentioned, September/December are the focal points.

BOJ ANNOUNCEMENT (FRI): BoJ is expected to stick to its ultra easy policy with rates to be kept at -0.1% and QQE with yield curve control maintained to flexibly target 10yr JGB yields at around 0%. As a reminder, the BoJ doubled down on its efforts to contain yields at the last meeting by announcing it will conduct special operations on every working day aside from when it is not expected, which went against the outside calls for the BoJ to adjust its tolerance band and the global trend of central banks pivoting towards normalisation, while it also reiterated it will ease policy without hesitation as needed and maintained forward guidance on interest rates. Since that meeting, the BoJ has continuously reinforced its dovish tone with Governor Kuroda stating that Japan is absolutely not in a situation that warrants tightening monetary policy and the biggest priority is to support Japan's economy by continuing powerful monetary easing. Kuroda also noted that the BoJ will be unwavering in its stance of maintaining monetary easing to ensure the recent rise in inflation expectations lead to a sustained price increase, while other officials have echoed the dovish tone including Deputy Governor Wakatabe who said they must maintain powerful monetary easing and sustain an environment where wages can rise, as well as noted that the BoJ shouldn't rule out additional easing steps if risks to the economy materialise and that widening the range around the BoJ's 10yr JGB yield target would be tantamount to a rate increase. Furthermore, the central bank has made it clear that policy is unlikely to be influenced by the recent depreciation in the JPY or the rise in inflation whereby Core CPI rose by its fastest pace since March 2015 at 2.1% vs. Exp. 2.1% (Prev. 0.8%) as Governor Kuroda noted that the FX market is regaining stability and doesn't think rapid Yen weakening was caused by BoJ easing, while he said rising inflation expectations are being driven mostly by energy costs and are lacking sustainability.

ECB REVIEW: As expected, the ECB opted to stand pat on rates with the deposit rate, main refi and marginal lending rates held at -0.5%, 0% and 0.25% respectively. On rates, the ECB announced their intention to raise rates by 25bps at the July meeting. Beyond July, policymakers will consider a larger increment in interest rate hikes if the medium-term inflation outlook persists or deteriorates. On the balance sheet, as expected, the Governing Council announced its decision to end net asset purchases under APP as of July 1st. Note, the policy statement offered no fresh guidance on how it could deal with the issue of market fragmentation as it commences its rate hiking cycle. In terms of the inflationary outlook, the ECB stated that inflation will remain "undesirably elevated for some time". This was reflected in the accompanying macro projections which saw the 2022 projection upgraded to 6.8% from 5.1% with 2024 inflation seen above target at 2.1% vs. prev. view of 1.9%. At the accompanying press conference, President Lagarde was pressed further on how the Bank intends to deal with fragmentation, to which, she noted that the Bank can utilise existing tools such as reinvestments from PEPP and, if necessary, can deploy new instruments if required. Later on in the press conference, Lagarde noted that there is no specific level of yield spreads that would be a trigger for an anti-fragmentation policy. When it comes to the decision-making process, Lagarde stated that policymakers were unanimous in their views, adding that no action was taken at today's meeting given the Bank's policy of sequencing. From a more medium-term perspective, the President was questioned on where the Governing Council judges the neutral rate to be, however, she remarked that this issue was deliberately not discussed. Overall, after clearly signposting the outcome of the July meeting and heavily suggesting that 50bps could be necessary in September, money markets have accelerated their interest rate hike bets with end-of-year pricing suggesting the possibility of two 50bps hikes and two 25bps hikes at the remaining four meetings of the year. Later in the session ECB sources suggested some ECB policymakers at

Copyright © 2022 Newsquawk Voice Limited. All rights reserved.

Thursday's meeting wanted a 50bps hike already in July and a large majority of the governing council was against making an announcement on a fragmentation-fighting tool.

RBA REVIEW: RBA hiked rates by 50bps to 0.85% (exp. 25bps increase) and said inflation in Australia has increased significantly, while it is committed to doing what is necessary to ensure that inflation in Australia returns to the target over time. The RBA added that inflation is likely to be higher than was expected a month ago and the Board expects to take further steps in normalising monetary conditions over the months ahead with the size and timing of future interest rate increases to be guided by the incoming data and the assessment of the outlook for inflation and the labour market. Furthermore, it noted the Australian Economy is resilient although one source of uncertainty about the economic outlook is how household spending evolves, given the increasing pressure on Australian households' budgets from higher inflation. “This statement clearly signals that the Bank now recognises that it has a significant challenge to contain inflation”, Westpac says as it cites the line in the statement pointing to higher inflation than earlier expected. “We expect further increases of 25 basis points will be required in November and December in response to another disturbing inflation print for the September quarter. 2022 would end with a cash rate of 2.1% - a policy stance that we would assess as in the contractionary zone… we expect that the 25 basis point increase from the RBA in February [2023] will be the last in this tightening cycle with the terminal rate settling at 2.35%.”, Westpac predicts.

RBI REVIEW: The RBI hiked the Repurchase Rate by 50bps to 4.90% (exp. 40bps hike) via unanimous decision and dropped mention of "staying accommodative". RBI Governor Das noted that inflation has increased above upper tolerance levels and they remain focused on bringing down inflation. Das added they will control inflation without losing sight of growth and that further monetary policy measures are necessary to anchor inflation, as well as noted that upside risk to inflation had intensified and materialised sooner than expected. “All of this sends a clear signal that the tightening cycle has further to run”, CapEco says, as the desk posits that the RBI will be confident enough to front-load hikes with a 50bps move at the next meeting in August, before turning to 25bps increments as inflation peaks. “In all, we remain comfortable with our view that the repo rate will rise to 6.15% by early 2023.”, CapEco said.

CBR REVIEW: Russia’s central bank delivered a larger-than-expected rate cut, lowering its Key Rate to 9.5% from 11% (analysts had expected a reduction to 10%). Capital Economics said that the central bank’s focus was continuing to shift away from inflation (inflation projections were lowered to 14-17% from 18-23%, a function of a stronger currency) and towards supporting economic activity and fighting the strength of the Rouble. A weaker currency could offer more support to the economy, but “fighting the exchange rate will be difficult as imports and demand for FX will remain low,” CapEco says, “but the central bank is likely to continue cutting interest rates and rolling back some of its capital controls – indeed, the government has confirmed that exporters will no longer be required to convert 50% of the FX earnings into Roubles.” Ahead, CapEco thinks that further reductions are likely to be more gradual, noting that the CBR’s statement this month said it would “consider the necessity” of further rate reductions, whereas its previous statement said it “holds open the prospect” for more cuts. “This is a slightly less dovish tone and suggests that the big moves in policy have already happened, and we expect rates to fall to 8% by year-end, and to 5.50% next year.”

Disclaimer

The information contained within this document has been prepared and issued by Newsquawk Voice Limited ("**Newsquawk**") on the basis of publicly available information and other sources believed to be reliable. Whilst all reasonable care is taken to ensure that the facts stated are accurate, neither Newsquawk nor any of its directors, officers or employees shall be in any way held responsible for its content or your use of it. Neither the provision of any content herein nor anything on our website or any other media we use is intended to, and should not be construed as, providing advice and/or enticing an offer or solicitation to invest in, buy or sell securities or other financial instruments.

Copyright © 2022 Newsquawk Voice Limited. All rights reserved.