Week Ahead 18-22 July – Highlights: ECB, BoJ, UK/CA /NZ inflation data, UK leadership debates

Week Ahead 18-22nd July

- **SUN:** UK Leadership Debate.
- **MON:** Japanese Marine Day Holiday, NZ CPI, UK Leadership Debate.
- **TUE:** UK Jobs Data.
- **WED:** PBoC, UK CPI, Canada CPI, NZ Trade Balance.
- **THU:** BoJ, ECB, CBRT, SARB, BoI, Japan Trade Balance, US Philly Fed.
- **FRI:** Japan CPI, UK Retail Sales, Flash PMIs, CBR, Canada Retail Sales.

NOTE: Previews are listed in day-order*

UK CONSERVATIVE PARTY LEADERSHIP DEBATE (SUN/MON): On July 17th and 18th ITV and Sky News are to host Conservative Party leadership debates, with the candidates eligible, but not required, to partake (at the time of writing) including Sunak, Truss, Mordaunt, Tugendhat & Badenoch; note, given that another elimination ballot is due on Monday, one of these candidates will not be eligible for the July 18th debate. Subsequent ballots are scheduled for the Tuesday and Wednesday at which point the final two candidates will be put to eligible Conservative party members (circa. 150k) and a new PM determined by September 5th. On this, the latest YouGov polling has Penny Mordaunt as the clear front-runner among grassroot members, emerging as a convincing winner against all other candidates in a head-to-head. Among Tory MPs, Sunak is the current frontrunner having secured over 101 votes and trailed by Mordaunt and Truss with 83 and 64 respectively. Former-Chancellor Sunak has put forward a fiscally prudent card, looking to tackle the cost-of-living crisis while acknowledging the heavy COVID-related expenditure that makes sweeping tax reductions challenging at present. In contrast, Foreign Minister Truss has pledged “Day 1” tax reductions and cutting current levels of public expenditure, while paring down public debt over a longer period of time than under present plans. While Mordaunt’s position is slightly vaguer than peers, her proposals are much closer to those put forward by Truss than Sunak, who is pledging to deliver a “modern economy” and focus on growth and competition with a cost-of-living focus, i.e. by cutting fuel VAT significantly. The TV debates themselves will see leaders asked questions on various topics by a virtual audience, key focal points in shoring up party support will be the cost-of-living crisis, fiscal intentions, ECHR and Brexit – to name a few.

NZ CPI (MON): New Zealand CPI data for Q2 is scheduled next week with the Q/Q reading expected to accelerate to 2.0% from 1.8% and Y/Y consumer inflation anticipated to rise to 7.1% from the previous level of 6.9% in Q1 which was the highest reading in 32 years. The surge in Q1 CPI data was led by rising prices of food, housing and transport which lifted inflation even further away from the RBNZ’s 1%-3% target range and suggests that the central bank will stay on course with its current tightening cycle which has already seen 6 consecutive rate increases. Furthermore, ASB Bank notes that “In the absence of a concerted easing in labour market pressures, current high inflation outcomes run the risk of being increasingly entrenched”, as well as suggesting that restrictive OCR settings are needed and that it expects the RBNZ’s policy rate to peak at 3.5% late this year, although sees cuts thereafter.

UK LABOUR MARKET DATA (TUE): The headline unemployment measure printed at 3.8% in April, which was an above-expected increase from the prior 3.7%. For May, the corresponding PMIs highlighted a “catch up on unfinished work contributed to a robust rise in employment numbers at private sector firms” and thus may pressure the unemployment rate itself. Additionally, the proximity of the Platinum Jubilee Bank Holiday towards the start of June could have supported May employment figures, though much of this would have been on a temporary basis. Anecdotally, the GDP release for May was strong and driven by activity in the services sector predominantly, with growth reported in production and construction as well. As always, average hourly earnings will be scrutinized for any BoE implications, particularly around second-round effects and after Governor Bailey spoke about the possibility for above-25bp moves; last month, the release posted the fastest median growth since 2008. Overall, the employment metrics are interesting, but as always, dated given more timely PMI releases. While the earnings metrics will undoubtedly factor into the BoE’s calculations, they are likely to be overshadowed by the ongoing focus on energy-driven inflation at the August MPR; where the debate will continue to be over 25bp or 50bp. Nonetheless, the ongoing tightness in the labour market has led to desks calling for further upside to the earnings numbers.

PBOC LPR ANNOUNCEMENT (WED): The PBoC is likely to keep its benchmark lending rates unchanged next week with the 1-Year Loan Prime Rate currently at 3.70% and 5-Year Loan Prime Rate at 4.45%. The expectation for the central bank to maintain the LPRs follows its recent decision to keep the 1-Year Medium-Term Lending Facility rate unchanged, which is seen as a fairly reliable leading signal for the central bank's intentions and given that the PBoC has been reserved in its open market operations whereby it has conducted daily 7-day Reverse Repos liquidity injections at a meagre CNY 3bln to match maturing contracts. Furthermore, PBoC Governor Yi recently noted that policy will continue to be accommodative and considering inflation, real interest rates are "pretty low", which suggests tightening is off the table, while further loosening also seems unlikely as the central bank would prefer to avoid stoking currency depreciation or further reduce the attractiveness of Chinese government bonds with China's 10yr yield already at a gap to its US counterpart amid PBoC-Fed policy divergence. Nonetheless, prospects of a future rate cut cannot be dismissed given support pledges by Chinese authorities including PBoC's Monetary Policy Department Head Zou Lan who noted that China will further guide banks to lower real lending rates and with the central bank also stating it will use monetary policy tools flexibly at the appropriate time, while there are also expectations for China to miss its growth target with PBoC adviser Wang Yiming anticipating economic growth at 4.7% this year vs the official target of 5.5%.

UK CPI (WED): Consumer prices are seen rising 0.7% M/M in June, matching the pace seen in May; the annual rate is seen ticking up to 9.3% Y/Y from 9.1% previously. Rising fuel prices are expected to underpin the headline measures; airline fares are also likely to register upside in the month, both on the back of rising fuel costs and demand conditions amid labour shortages; food prices are likely to have remained elevated given that the UK imports a great deal, and global food costs are being stoked higher by Russia's aggression towards Ukraine. The core measure of CPI is seen rising 0.5% M/M in June, matching the prior pace, while the annual rate is expected to tick up further to 6.0% from 5.9%; lower apparel prices and base effects are likely to constrain any upside, however. Investec's analysts do not see inflation peaking in June. The bank says energy is a key input in determining how persistent inflation will be, and it notes that the UK's energy price cap is set to be adjusted in October; Investec foresees the cap rising 67%. Investec also argues that recent political events add an extra layer of uncertainty as to how long 'core' inflation will persist; "many of the frontrunners to replace PM Johnson, former Chancellor Rishi Sunak aside, have promised sweeping tax cuts as part of their leadership campaign," and "such tax cuts may help stimulate the economy, but also risk creating more entrenched underlying inflation."

CAD CPI (WED): The BoC's monetary policy report this week saw upward revisions to the inflation profile. The central bank now sees consumer prices at 7.2% in 2022 (prev. 5.3%), 4.6% in 2023 (prev. 2.8%), and 2.3% in 2024 (prev. 2.1%). The BoC also lifted rates by more than expected (100bps hike vs expected 75bps) following recent upside surprises in inflation data and a pick-up in Canadian inflation expectations, while the unemployment rate continues lower - all compelling the central bank to lift policy out of stimulative territory - rates at 2.50% now sit at the mid-point of its 2-3% estimate of where the neutral rate lies. "Tougher medicine will be needed to get inflation under control and we look for the policy rate to rise to a restrictive 3.25% by October," RBC said, "the BoC's limited guidance seems to align with that view, saying a front-loaded tightening cycle argues for getting the policy rate 'quickly to the top end or slightly above the neutral range.'"

BOJ POLICY ANNOUNCEMENT (THU): The BoJ is expected to maintain its policy settings at next week's meeting with the central bank likely to keep rates at -0.10% and QQE with Yield Curve Control to flexibly target 10yr JGB yields at around 0%. The BoJ has made it clear that it will sustain its ultra-loose policy, despite the rapid JPY weakening and trend of global central banks tightening policies, with Governor Kuroda noting that the central bank stands ready to ease policy further without hesitation as needed and expects short- and long-term policy rate targets to remain at current or lower levels. Furthermore, Kuroda noted shortly after the last meeting that he does not see a need for further policy easing now nor was he thinking about raising the cap on the BoJ's long-term yield target above 0.25% as this could result in higher yields and weaken the effect of monetary easing. Recent data releases have been disappointing and therefore support the view for the central bank to maintain its easy policy settings in which the Tankan Large Manufacturing and Non-Manufacturing Indices and Outlooks all missed expectations, although mostly improved from the prior quarter and Large All Industry Capex growth more than doubled against forecast. The latest Household Spending data showed a surprise contraction and Industrial Production also unexpectedly contracted, which prompted the government to lower its assessment of output, while National CPI Ex. Fresh Food remained slightly above the BoJ's 2% price target as expected at 2.1%, though this is unlikely to have ramifications for policy as the central bank has acknowledged that price increases were due to rising raw material costs and a weak Yen instead of being driven by a positive economic cycle, and therefore it would still be appropriate to keep its easing policy. The BoJ will also release its latest Outlook Report containing board members' median forecasts for Real GDP and Core CPI with recent source reports noting that the BoJ is expected to increase its FY22 inflation forecast marginally to slightly above 2% from 1.9% and lower its economic growth forecast from the current 2.9% view.

ECB POLICY ANNOUNCEMENT (THU): The ECB will deliver on its heavily flagged 25bp rate hike, a lift-off that will impact all three key rates and lift the main depo rate from -0.50% to -0.25%. Sources and commentary indicate that some of the more hawkish officials (e.g. Holzmann) on the GC want at least the optionality for a 50bp hike at this meeting, as such there could well be dissent on the vote. Note, in wake of the latest hot-US CPI data, market pricing turned significantly more hawkish for numerous central banks; with expectations for the ECB rising to circa. 25% chance of a 50 bp July move. Post-hike focus for the gathering will be, primarily, on three factors: the inflation assessment, guidance for September and the fragmentation tool. Firstly, the ECB's assessment of the inflation situation in June was that their projections indicated it will remain undesirably elevated for some time. Since then, June's EZ Flash inflation metrics have been released and posted another above-exp. increase to 8.6% from 8.1% (exp. 8.4%) for the headline; however, the super-core did incrementally and surprisingly dip to 3.7% from 3.8% - an occurrence that will be closely scrutinized to see if it's a one-off or the beginning of an easing in some price pressures. Nonetheless, the inflation situation remains hot and significantly above the 2.0% goal. As such, and secondly, the ECB's June guidance that if the inflation outlook persists/deteriorates a larger increment (re. hikes) would be appropriate in September; a condition that has, based on hard-data, likely been met. However, the 5yr5yr gauge of long-term EZ inflation expectations recently moved incrementally below the 2.0% target, for the first time since March. An occurrence that, if sustained, could offer some relief, but is unlikely to be sufficient to change the medium-term view and accompanying guidance for a 50bp hike in September; a magnitude that numerous officials have stated they anticipate. Finally, the fragmentation tool has, according to Bloomberg, been named the Transmission Protection Mechanism. Interestingly, the sources piece noted that there is not yet a sense of its certain arrival in July, and this rattled periphery debt in particular. Participants will be focused firstly on whether the tool arrives, and secondly its exact details following an emergency meeting to discuss it which added very little new information. However, subsequent sources indicate that the tool will involve the sale of other securities, in an attempt to prevent a further fanning of inflation. Additionally, PEPP reinvestment activity will reportedly have the periphery nations listed as "recipients" and the likes of Germany and the Netherlands "donors", in a bid to prevent fragmentation. Reminder, the July meeting does not include new forecasts which are scheduled to be updated in September, but will, as always, feature a press conference from President Lagarde; additionally, the timings for the announcement and press conference are now 13:15BST/08:15ET & 13:45BST/08:45ET respectively.

SARB POLICY ANNOUNCEMENT (THU): The South African Reserve Bank is likely to lift its Repo Rate by a 50bps increment in July, taking the rate to 5.25%. The SARB lifted rates by 50bps in May, in line with the market view, with members seemingly supportive of a front-loaded rate hike programme. This is something many other major global central banks have been doing, and accordingly, EMFX like the South African Rand has come under pressure, compelling the SARB to adopt a similar strategy. ING notes that the Repo Rate at the current 4.75% level seems low relative to CPI, which is running at 6.5% Y/Y (NOTE: South Africa's CPI data for June will be released the day before the SARB announcement). ING says the market expects rates will have risen to 6.00% by the end of this year, but the bank itself believes that ZAR weakness could prompt larger hikes.

CBRT POLICY ANNOUNCEMENT (THU): The central bank's most recent monthly survey of business leaders and economists saw CPI expectations revised up, although those surveyed still see the repo rate at the current 14.00% in three-months' time; in 12-months' time, however, the expectation is that rates will have risen to 15.00% (vs 14.00% in the previous month's poll). Credit Suisse has said that "Turkey's recent monetary policy decisions have not been based on conventional economic principles," noting that the central bank cut rates by a cumulative 500bps in late 2021 even as annual inflation was surging. Authorities have tried to protect the value of the currency with the TRY deposit scheme, launched late last year, but this ultimately has clouded visibility and predictability, the bank says. "The inflation outlook remains challenging," it writes, "headline inflation will likely move toward 80% in the coming months and stay elevated through November - the 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." The bank sees rates at 14.00% in 12-months, but argues that this is not to suggest it thinks the current policy stance is sustainable; instead, it is a reflection that the timing of the policy adjustment required is impossible to predict. CS says, "that the timing of a conventional policy adjustment will also crucially hinge, in our view, on political considerations, in particular the presidential/parliamentary elections that will be held no later than in mid-2023."

JAPAN CPI (FRI): Japanese nationwide inflation data for June is due next week with National Core CPI (ex-Fresh Food) expected to remain at 2.1%, which would be the third consecutive month just above the BoJ's 2% price goal. Upward inflationary pressures had been largely driven by rising costs of energy and raw materials which were made worse by Japan's rapid currency depreciation and the ongoing war in Ukraine, while food prices excluding volatile fresh food such as meat and fish increased by the fastest pace since 2015 and have led to some concerns regarding consumption considering that wage growth remains sluggish. In terms of the already-released Tokyo CPI data for June, this showed core consumer prices accelerated to a 7-year high of 2.1% from the prior rate of 1.9%, and therefore could be a leading indicator for a rise in nationwide prices. Nonetheless, the inflation figures aren't expected to spur a policy reaction from the BoJ as the central bank had acknowledged that consumer inflation was likely to accelerate and as it wasn't being driven by a positive economic cycle, easy policy remains appropriate.

EZ FLASH PMIS (FRI): July's Flash release follows on from a downbeat June survey where the final reading was deemed to be indicative of quarterly GDP growth of just 0.2% and forward-looking indicators pointed to an output reduction in the months ahead. Overall, the findings suggested that risks are to the downside. While the release will take a back-seat given Thursday's ECB meeting and expected hike, the accompanying commentary from S&P Global will be heavily scrutinised for indications as to whether, as ZEW believes, conditions have seen a marked M/M deterioration, and one that prompted ZEW respondents to cut their 6-month view once again; citing the ECB's announced hikes, China restrictions (which have extended further since the survey was conducted) and the energy situation. Given the referenced ZEW would not have incorporated the most recent China-COVID developments, it will be interesting to see if this prompts further caution/concern from PMI respondents for both the immediate and medium-term outlook.

UK FLASH PMI (FRI): The flash manufacturing PMI for July is seen paring to 52.0 from 52.8 in June; the flash services PMI is seen moderating to 53.2 from 54.3; this should leave the composite PMI at 52.5, falling from 53.7 in June. Although the June data surprised to the upside, the report noted that in the services industry, new order growth fell to a 16-month low as economic uncertainty and rising inflation hit discretionary spending, while the slowdown in manufacturing continued as business optimism dips to lowest levels in over two years. Analysts note that the UK continues to face uncertainty from international (supply chain issues, higher global energy and food costs, slowdown in the global growth engines like China, returning COVID in some areas) and domestic factors (real income squeeze, uncertain political landscape, the prospect of higher borrowing costs ahead), and these themes are expected to be reflected in the data.

UK RETAIL SALES (FRI): The consensus expects retail sales to decline 0.3% M/M in June (prev. -0.5%); the ex-fuel measure is also seen slipping by 0.3% M/M (prev. -0.7%). The data is also subject to some uncertainties given the adjustments needed for the UK public holidays in June; the late May bank holiday was moved into June, while there was an additional holiday for the Queen's Jubilee (which could give a boost to food sales in the month). The British Retail Consortium's June monitor noted that sales volumes were "falling to a rate not seen since the depths of the pandemic, as inflation continues to bite, and households cut back spending." The BRC says discretionary purchases were heavily impacted, and consumers were also trading down to cheaper brands in food and non-food items alike. "Retailers are caught between significant rising costs in their supply chains and protecting their customers from price rises," it said, "the government needs to get creative and find ways to help relieve some of this cost pressure," adding that "government action on transitional relief would make a meaningful difference to retailers' costs and ease pressure on prices for customers."

CBR POLICY ANNOUNCEMENT (FRI): Official commentary has primed us to expect another rate cut from Russia's central bank in July, although the magnitude might not be as great as the 150bps reduction in June, which was motivated by declines in inflation, inflation expectations of household and corporates normalising, along with the RUB currency continuing to strengthen. And these themes may continue to support lower rates. Governor Nabiullina recently reiterated that the central bank will lower rates further as inflation slows, and she sees more scope for rate cuts, dismissing risks of a deflationary spiral. However, analysts note that household inflation expectations picked-up in June, and that could limit the CBR's ability to lower its key rate from the current 9.5%. Potentially offsetting that, the central bank's monthly business climate survey saw improvements, with companies noting that demand had stopped falling in May for the first time since February; although that data was for May it nevertheless highlights some of the themes that Russian officials have been impressing recently, like the improved expectations of businesses, and a less negative view of the current situation. Meanwhile, the RUB currency has largely moved sideways since the June meeting, though many note is at stronger levels against the USD now than it was in Q1 before Russia engaged in a conflict against Ukraine - another factor that could support a smaller increment cut in July.