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Central Banks Weekly July 22nd - Previewing FOMC NBH; Reviewing PBoC, BoJ, ECB, SARB, CBRT, CBR

22nd July 2022:

NBH ANNOUNCEMENT (TUE): Based on recent commentary the NBH will likely decide to conduct a further hike to their Base Rate which currently stands at 9.75%, at the same level as their One-Week Deposit Rate following a 200bp increase. ING looks for a 1.25% increase given it's the average of the last two meetings 50bp and 200bp moves; however, caveating that with expectations so high, the bar for a disappointment is low and EUR/HUF could revert back to 410 over the summer. At the last update, Deputy Governor Virag said hikes will continue in determined steps, altering from their prior "gradual" language. Adding, that hikes are set to continue until such a time as when CPI is seen peaking; for reference, the last inflation release was prior to the One-Week's 200bp move and had the headline YY lifting to 11.7% (prev. 10.7%, exp. 11.5%). The next inflation print is due on August 9th. Elsewhere, at the meeting, Virag added that they will be acting against FX movements which pose a sustained threat to price stability. A pledge that has been followed by days of concerted action from the NBH on this front, providing over EUR 1.5bln of liquidity to banks since at daily swap tenders.

FOMC ANNOUNCEMENT (WED): The FOMC is largely expected to raise its Fed Funds target range by 75bps to 2.25-2.50%, a territory considered to be 'neutral', to which it will guide smaller hikes ahead as policy becomes restrictive. Some signs/expectations of a cooling growth outlook (as evidenced by survey data and corporate commentary), and a lack of deterioration in inflation gauges post-June CPI (UoM inflation expectations fell), have taken the heat off of a 100bps rate hike that gained traction after the headline Y/Y consumer inflation print in June rose again to a multi-decade high of 9.1% from 8.6%. The consensus for 75bps was emboldened in the wake of comments from Fed hawks, Waller and Bullard, after the CPI, indicating their preference remaining for 75bps despite the speculation for a larger hike. Money markets now imply just a 10% chance of a 100bps move, as opposed to the greater than 70% implied in the immediate aftermath of CPI. With no SEPs at this meeting, traders will look to the statement and Powell's presser for guidance on the rate path/terminal rate, with expectations for smaller hike increments at a 'measured' pace now that the Fed Funds rate is being lifted above neutral (2.5% according to June median Dot Plot). Markets are currently pricing in a year-end Fed Funds rate at 3.25-3.50%, which also now happens to be the market-implied terminal rate with rate cuts priced in Q1 '23. When June FOMC Dots were released they implied a terminal of 3.75-4.00%, so there is a disconnect between markets and the Fed's forecasts as the former prices in risk of a growth/employment slowdown later this year while Fed officials are conducting policy on the knowns: solid job growth and consumer spending that is fueling consecutive increases in inflation. The Fed has said it will remain undeterred in its tightening path until inflation shows signs of returning to target, so to expect anything otherwise at the June FOMC appears unlikely.

BOJ SOO (FRI): The BoJ will release the Summary of Opinions from the July meeting on Friday in which the central bank kept its policy settings unchanged, as expected, with rates at -0.10% and QQE with yield curve control maintained to target 10yr JGB yields at around 0%. The BoJ reiterated it will offer to buy 10yr JGBs at 0.25% every business day unless it is highly likely that no bids will be submitted and repeated its guidance on policy bias that it will take additional easing steps without hesitation as needed with an eye on the pandemic's impact on the economy, as well as keeping forward guidance for short- and long-term rates to remain at present or lower levels. Furthermore, it stated that it must be vigilant to financial and currency market moves and their impact on Japan's economy and prices, while it lowered the Real GDP growth forecast for the current fiscal year to 2.4% from 2.9%, but raised the Real GDP view for the two years after and increased CPI projections through to FY24. The policy announcement lacked any major surprises and the adjustment to the current fiscal year's projection was previously flagged by source reports, while Governor Kuroda made it clear in the post-meeting press conference that there is no intention to raise interest rates under Yield Curve Control and no plan to widen YCC's 0.25% cap range, as well as noting that increasing rates a little bit would not stop JPY weakness and a large hike would be needed to stop JPY weakness which would bring substantial damage to the economy and he does not believe such a policy is rationally feasible.

PBOC LPR REVIEW: The PBOC as expected maintained its 1yr and 5yr Loan Prime Rates (LPRs) at 3.70% and 4.45% respectively. Desks have been framing the move as a cautious approach as the Chinese economy attempts to pick back up, with some suggesting the need for aggressive monetary easing has lessened as June economic data was somewhat constructive. Global Times citing analysts, following the PBoC's hold on LPRs, suggests "there's still room for more easing in the months to come, especially in the case of the five-year LPR, citing an imperative to steady the housing

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market as part of broader efforts to support economic stabilization." The decision comes at a time when China's housing crisis deepens as homeowners threatened to stop paying mortgages on a slew of unfinished housing projects they had purchased.

BOJ REVIEW: The BoJ policy announcement lacked any major surprises as the Central Bank kept rates at -0.10% as expected and maintained its QQE with YCC policy, while it also reiterated its forward guidance on rates to remain at current or lower levels and kept its pledge to conduct daily fixed-rate operations. The Central Bank also reduced its Real GDP growth forecast for the current fiscal year which was what source reports had previously suggested but raised the GDP view for the two years after, while it also increased CPI projections but reiterated that it will take time for inflation to reach the Central Bank's 2% target. At the presser, Governor Kuroda rammed home dovish guidance - he stressed the importance of maintaining rates low and yield curve control as inflation is still not seen staying above target sustainably, while he also reiterated no intention to widen the 10-year JGB yield tolerance band. The Governor also emphasised that monetary policy does not target FX with currency intervention.

ECB REVIEW: Despite expectations for a 25bps hike across the ECB's three key rates, policymakers opted to "go big" and deliver 50bps worth of tightening, taking the deposit rate to 0% and therefore drawing a line under the Bank's NIRP. Alongside this, the Bank refrained from providing explicit guidance for the September meeting and is instead adopting a meeting-by-meeting approach. The Governing Council was also able to agree on an anti-fragmentation tool named the Transmission Protection Instrument (TPI) aimed at ensuring that the monetary policy stance is transmitted smoothly across all euro area countries. That said, PEPP remains the first line of defence to counter risks to the transmission mechanism related to the pandemic. At the follow-up press conference, as part of the economic assessment, President Lagarde noted that risks to the inflation outlook continue to be to the upside and have intensified. In terms of the decisions taken today, Lagarde said that the Governing Council rallied around the consensus of a 50bps hike and that the ECB is accelerating the normalisation process, but not changing the ultimate point of arrival. With regards to TPI, Lagarde said the decision on the new tool was unanimous. In terms of the details of TPI, Lagarde noted that all nations are eligible, the ECB is capable of "going big" on the instrument, whilst the activation of TPI is at the discretion of the Governing Council. Lagarde later clarified that the four conditions for TPI are as follows: 1. Compliance of EU fiscal framework, 2. Absence of severe macro imbalances, 3. Fiscal sustainability, 4. Sound and sustainable macro policies. Some commentators were quick to suggest that Italy might fail to satisfy such criteria and as such, the IT/GE 10yr spread was unable to narrow from the levels prompted by the recent resignation of Italian PM Draghi. Furthermore, the follow-up press release noted that purchases under TPI could be suspended if it is judged that persistent tensions are due to country fundamentals. Overall, despite delivering a larger than expected hike, EUR/USD erased all of the upside seen on the initial announcement as the potential hurdles for Italy being able to utilise the TPI appear to be high. Furthermore, although the ECB delivered 50bps instead of 25bps, the central bank is likely to see its window of opportunity for raising rates narrow ahead of a difficult winter amid energy supply disruptions. In terms of market pricing, a 50bps move in September is now priced in, with the deposit rate seen rising to 1.25% by year-end vs. 1% pre-announcement. Given the aforementioned headwinds facing the ECB it is unclear whether such a rate path will be realised. Accordingly, ING expects a further 50bps of rate hikes before winter starts with no hikes to follow thereafter.

SARB REVIEW: The South African Reserve Bank lifted its Repo Rate by a larger-than-expected increment of 75bps against expectations for a 50bps hike, marking the fifth consecutive hike. The statement suggested three members backed 75bps, whilst one advocated for 100bps and another for 50bps. Inflation was the main driver of the larger move. The SARB also upped its inflation forecast for 2022 to 6.5% from 5.9%, and warned that the risks to the inflation outlook are assessed to the upside.

CBRT REVIEW: The Turkish Central Bank opted to stand pat at 14.00%, in line with market expectations. The statement was largely a copy of the prior meeting with some minor tweaks. The CBRT stated it will continue to use all available instruments decisively within the framework of the "liraization" strategy until strong indicators point to an permanent fall in inflation and the medium-term 5% target is achieved in pursuit of the primary objective of price stability. The statement reiterated the Committee will continue to take its decisions in a transparent, predictable and data-driven framework. All-in-all, the decision turned out to be a non-event as anticipated. "the July meeting confirms that the CBT will not change its course and maintain reliance on unorthodox instruments in line with its "liraization strategy". With these actions, the CBT aims to "strengthen the effectiveness of the monetary policy transmission mechanism", analysts at ING posit.

CBR REVIEW: The Russian Central Bank opted for a 150bps rate cut to 8.00% vs expectations for a 50bps cut to 9.00%, and signalled that it will consider further rate reductions in H2 this year. This marks the fifth consecutive cut since the CBR easing cycle began in April. The Bank widened its 2022 inflation forecast band to 12-15% from 12.5-14%, whilst the Key Rate forecast was lowered to 10.5-10.8% from 12.5-14.0%. All-in-all, the cooling of inflation and gains in the RUB allowed for a deeper-than-expected cut, with the rate now below levels seen just before Russia invaded Ukraine.

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