Central Banks Weekly September 30th: Reviewing Banxico, RBI; previewing RBA, RBNZ, ECB Minutes

30th September 2022:

RBA ANNOUNCEMENT (TUE): RBNZ is expected to deliver its fifth consecutive 50bps rate hike next week to lift the Official Cash Rate to 3.50% with money markets pricing in an 80% probability for such a move and a 20% chance of a larger 75bps increase. The RBNZ delivered a hawkish rate increase at the last meeting where it raised rates for the 7th time in as many meetings since the start of the hiking cycle and it increased its projections for the OCR and inflation with the latter now expected to peak next year at 4.1% vs a prior view of just under 4.0%. Furthermore, the central bank noted that conditions need to continue to tighten and agreed that maintaining the current pace of tightening remains the best means with further increases in the OCR required to meet its remit objectives, while Governor Orr also flagged further rate increases, as getting rates to 4% would buy comfort for the policy committee and although he acknowledged that the tightening cycle is very mature, he added that there is still a little bit more to do in terms of tightening. As such, some analysts have revised their RBNZ rate hikes views with TD Securities lifting its OCR forecast for April to 4.5% from 4.0% and Westpac also raised its view for the terminal rate by 50bps to 4.5%.

RBNZ ANNOUNCEMENT (WED): RBA is expected to hike rates at its meeting next week with 21 out of 29 analysts surveyed by Reuters expecting another 50bps rate hike to lift the Cash Rate Target to 2.85%, although money markets are nearly even in terms of pricing the chances of either a 25bps or 50bps hike. As a reminder, the central bank reiterated at the last meeting that the Board is committed to doing what is necessary to ensure that inflation returns to target and expects to increase rates further in the months ahead, but it is not on a preset path, while members saw the case for a slower pace of rate hikes as becoming stronger as the level of the Cash Rate increases, as well as noting that interest rates had been raised quite quickly and are getting closer to normal settings. Furthermore, RBA Governor Lowe recently stated that at some point, they will not need to hike by 50bps with the central bank getting closer to that point and they are closer to normal on rates, but not there yet. Lowe also noted that rates are still too low right now and that they will consider tightening by 25bps or 50bps at the upcoming meeting which were the options discussed last month. The increased hints about a future slowdown has spurred some expectations for the central bank to switch gears with AMP forecasting a 25bps move for next week and for rates to peak at 2.85%, but acknowledged upside risks given the strength in lagged data and RBA hawkishness, while NAB adjusted its RBA rate hike forecast for October to 50bps from 25bps. The latest data releases also suggest there is scope for the RBA to stick with the current pace as Real GDP YY strengthened in Q2 to 3.6% vs. Exp. 3.5% (Prev. 3.3%) and although jobs data missed slightly, the increase in the employment change was solely driven by full-time work and the unemployment rate remained firmly below 4.0%. In addition, Australia's first ever monthly CPI releases showed inflation remained elevated at 7.0% in July and 6.8% in August which is more than double the higher-end of the 2-3% target and would likely keep the central bank on its current hiking track.

ECB MINUTES (THU): In-fitting with market pricing and against a split consensus amongst analysts, the ECB opted to pull the trigger on a 75bps hike, taking the deposit rate to 0.75%. The statement noted that the GC expects to raise rates further over the next "several" meetings, whilst taking a data-dependent and meeting-by-meeting approach. In terms of other measures, the ECB opted to continue with its current reinvestment policy whilst suspending its two-tier system by setting the multiplier to zero. The accompanying staff forecasts saw 2022, 2023 and 2024 inflation projections revised higher with the 2024 forecast of 2.3% indicating that further policy tightening is required. On the growth front, 2022 GDP was revised a touch higher, however, 2023 was slashed to 0.9% from 2.1% with the downside scenario touting the possibility of negative growth. At the follow-up press conference, President Lagarde noted that the decision on rates was unanimous, albeit there were differing views across the council; any colour around these differing views will be of note for the market, but ultimately deemed as somewhat stale given the fluidity of global inflationary dynamics. With regards to the magnitude of hikes going forward, Lagarde noted that 75bps increments are not the norm, but moves will not necessarily get smaller as the ECB heads towards the terminal rate. Note, source reports after the meeting suggested another 75bps hike could be on the cards for the October meeting, whilst Chief Economist Lane was reportedly more hawkish at the meeting than he had been in a speech a few days before the confab. Despite guidance that the GC will be following a meeting-by-meeting approach, Lagarde stated that hikes will probably take place at more than two meetings, but fewer than five, markets will be looking to see if such a viewpoint was alluded to in the account of the meeting. Finally, source reporting following the meeting revealed that QT is expected to be discussed at a non-policy meeting in Cyprus on Oct. 5th and will likely also be debated at subsequent meetings.

BOE REVIEW: Following last week's 50bps hike from the Bank which disappointed some in the market hoping for a 75bps adjustment, the BoE was once again in the spotlight as investors continued to digest the 'mini-budget' announcement from the government last week. The measures proposed by Truss/Kwarteng last week led to heavy selling pressure in Gilts and upside in yields at the time with this trend resuming on Monday as GBP/USD crashed to a low of circa 1.0350 amid comments from Chancellor Kwarteng who suggested that there was "more to come" with regards to additional tax reductions. Given the tumult in markets, pricing for an intra-meeting hike by the MPC ahead of its November 3rd meeting accelerated, however, at the time of writing, such a policy lever has not been pulled by the Bank. Instead, Governor Bailey released a statement on Monday noting that the BoE "was monitoring developments in financial markets very closely in light of the significant repricing of financial assets and will not hesitate to change rates as much as necessary". Thereafter on Tuesday Chief Economist Pill delivered a speech in which he stated that the MPC will "rely on communication" in the run up to the November meeting and it is best for monetary policy to take "a lower frequency and more considered approach". From a balance sheet perspective, Pill stated that as long as the market is orderly in the repricing of fundamentals, QT can continue, adding that the Bank will not sell Gilts into a dysfunctional market. The following day, the MPC took the decision to carry out temporary purchases of long-dated UK government bonds from 28 September until 14th October with the purpose of restoring orderly market conditions. Thereafter, the first Gilt sale operation will be initiated as of October 31st with the MPC's annual target of an GBP 80bln stock reduction unaffected and unchanged. In the aftermath of the announcement it was noted that one of the motivations behind the decision was from a financial stability standpoint whereby some pension funds began receiving margin calls given the losses seen in bonds held by various funds. With the MPC refraining from further rate hikes at this stage, market pricing suggests that despite concerns in the mortgage space, the MPC will deliver 123bps of tightening by November 3rd, with year-end pricing looking for around 200bps of tightening, which would take the Bank Rate to 4.25%.

BANXICO REVIEW: Banxico hiked rates by 75bps, as expected, to 9.25% (prev. 8.5%), in a unanimous decision in the face of accelerating inflation and deteriorating external conditions, such as persistent supply and demand issues and rising commodity prices. In the accompanying commentary, Banxico said the balance of risks for the trajectory of inflation within the forecast horizon remains biased to the upside, and the Board will thoroughly monitor inflationary pressures as well as all factors that have an incidence on the unforeseen path for inflation and its expectations. As such, Banxico's updated inflation projections were lifted across the board, and it now anticipates year-end inflation at a peak of 8.6% (prev. 8.1%), while "cooling" to 4.0% (prev. 3.2%) by the end of 2023 before returning to target in 2024 with inflation seen at 3.1% by Q3 2024. Looking ahead, Pantheon Macroeconomics expect the Board to increase rates by a final 75bp at the next meeting, assuming the Fed does the same, and then to remain on hold over H1 2023. Pantheon states that "weakening domestic demand, deteriorating global conditions, and a less hawkish Fed, thanks to rapidly falling inflation, should give Banxico room to pause. But the risks to rates remain massively tilted to the upside."

RBI REVIEW: The RBI hiked its Repurchase Rate by 50bps to 5.90%, as expected, via a 5-1 vote and the Standing Deposit Facility was adjusted to 5.65%, while RBI Governor Das said the MPC is to remain focused on the withdrawal of accommodation. The central bank suggested that consumer price-based inflation remains elevated and the inflation trajectory is closed with uncertainties, whilst the persistence of high inflation necessitates a further calibrated withdrawal of monetary accommodation. On FX, Governor Das suggested the INR has fared better than other peers, and the RBI does not have any exchange rate in mind and only curbs volatility. The Governor added that interventions in the FX market are based on the continuous assessment of prevailing and evolving situations. On that note, the INR saw decent strength later amid reports that the RBI is encouraging state-run refiners to reduce USD buying in the spot market; asking to lean on a USD 9bln credit line instead, according to Reuters sources.