Central Banks Weekly Dec. 9th: Previewing FOMC, ECB, BoE, SNB, Norges Bank, Banxico; reviewing BoC, BCB

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FOMC ANNOUNCEMENT (WED): The Fed is expected to lift its Federal Funds Rate target by 50bps to 4.25-4.50%, according to both the analyst consensus, as well as the previous meeting statement and recent commentary from Fed officials. Analysts will also be noting the updated economic projections, which are expected to show a higher terminal rate than assumed in the September projections (4.6%), as has been alluded to by Chair Powell at the November FOMC and in remarks made in December. Money markets are implying that terminal is somewhere in the 4.75-5.00% bracket, although have creeped into the 5.00-5.25% range in wake of some hawkish data prints (like the recent NFP and ISM data, for instance). Powell will likely be quizzed on how long the Fed intends to hold rates at terminal; while he might not get drawn into offering any precise guidance, the chair himself has previously said that rates will have to be held at terminal for “some time” - a line echoed by many other Fed officials too. For context, historically the Fed has typically stayed at terminal for between 3-15 months, with the average being around 6.5 months. It is worth noting that expectations for the December meeting could be subject to some further volatility, given that the November CPI data will be released a day before the FOMC meeting; accordingly, if the CPI data does deviate widely vs expectations, the Fed may choose to again ‘guide’ expectations via its mouthpieces in the WSJ or NYT.

NORGES BANK POLICY ANNOUNCEMENT (THU): Following a downshifted 25bps rate hike at its previous gathering, the central bank guided participants towards further tightening ‘most likely’ taking place in December. While Governor Bach did not provide explicit guidance as to what magnitude to expect, the consensus looks for another 25bps hike, taking its key policy rate to 2.75%. Since the November 3rd policy meeting, the most pertinent releases have been October’s and November’s CPI metrics: the October release was hotter than expected, both for the headline and core measures, while the November rates of inflation unexpectedly cooled, with the core (ex-ATE) figure at 5.75% (prev. 5.9%). However, while a good sign, this compares to (and significantly eclipses) the 4.97% forecast for December within the central bank’s September’s MPR. The December meeting will be accompanied by an updated MPR, which is expected to see a significant upward revision to at least the near-term inflation forecasts. While the inflation backdrop perhaps justified a more hawkish announcement, the view in November that there are signs of the economy slowing down – a prognosis echoed by the Financial Stability Report, Regional Network and Household surveys since. On the latter, while there are some optimistic points within it on inflation and capacity constraints, the overall 6-month ahead index deteriorated. For reference, commentary from the Norges Bank has been very sparse.

SNB POLICY ANNOUNCEMENT (THU): The Swiss central bank is expected to lift rates by 50bps to 1.00%, and will likely reiterate a two-way willingness to intervene in FX as necessary. The downshift to 50bps from September’s 75bps move is justified by inflation printing below both the market and SNB’s forecasts for October and November; though, given recent rhetoric from Chairman Jordan, a larger magnitude cannot be ruled out. At the September meeting, the central bank disappointed market expectations for 100bp, which sparked a pronounced dovish reaction across asset classes. Additionally, it altered its tiering system, essentially flipping the prior exemption to account for rates moving into positive territory. Perhaps the most pertinent aspect of the meeting, rates aside, was the reiteration of language from the Chair that it can buy or sell FX as needed to weaken or even support the CHF. Since then, we have seen Jordan double-down on this language, which hints at further tightening, while stressing a willingness to take all necessary measures to bring inflation back to stable territory and reiterating that nominal CHF appreciation is useful in guarding against inflation. November’s inflation print was in-line with the prior readings and market expectations at 3.0% Y/Y, a figure that is below the SNB’s forecast from September of 3.4% for the Q4-2022 period; and while December’s metrics are not yet available, the numbers for the quarter thus far are comfortably below this forecast. Accordingly, this could perhaps reduce the need for any ‘outsized’ policy action, a view that derives support from the ECB and Fed potentially looking to step down the pace of tightening to 50bps in December, a magnitude the SNB may also enact, although 25bps still should not be ruled out given the aforementioned inflation developments.

BOE POLICY ANNOUNCEMENT (THU): Policymakers on the MPC are expected to step down to a 50bps rate hike pace compared to the 75bps move implemented in November. The decision to “go big” last month was largely based on the disappointment from the market that the MPC “only” went for 50bps in September. This time around, and with 290bps of rate increases under their belts thus far, the MPC is expected to return to a 50bps adjustment, according to 52 of the 54 analysts surveyed by Reuters, and market pricing assigns around a 90% chance of such an outcome. The decision to move on rates is expected to be a unanimous given that headline annualised inflation advanced to 11.1% Y/Y in October, while the core rate remained at an elevated level of 6.5%. However, given dissent at the November meeting – where Swati Dhingra voted for a 50bps hike, and Silvana Tenreyro for 25bps – there is a risk that the decision might not be unanimous. Credit Suisse touts the possibility of a 2-5-2 split, where Tenreyro and Dhingra could vote for 25bps, Haskel and Mann vote for 75bps, and with the remainder opting for 50bps. Capital Economics notes that there is a risk that Tenreyro could opt for an unchanged rate, given remarks she made in a recent speech, where she said that "in the most likely scenario, we had already done enough"; she also published a central scenario where rates peak at 3% (current levels). It is likely that the bulk of the focus will centre around this aspect of the decision, and any adjustment to forward guidance, which currently reads "the majority of the Committee judges that...further increases in Bank Rate may be required for a sustainable return of inflation to target, albeit to a peak lower than priced into financial markets." Beyond next week's meeting, analysts surveyed by Reuters expect the BoE will carry out a further 50bps of rate hikes in Q1, followed by 25bps worth in Q2, taking the terminal rate to 4.25%; market pricing takes a slightly more hawkish view and sees the terminal rate at 4.5%.

ECB POLICY ANNOUNCEMENT (THU): Despite softer-than-anticipated headline inflation in November, Eurozone HICP printed 10.0% Y/Y (exp. 10.4%), and was overshadowed by an unexpected rise in core inflation 6.6% Y/Y (exp. 6.3%, prev. 6.4%). As such, the central bank is expected to pull the trigger on another rate hike, despite the uncertain economic outlook. The 75bps increase at the October meeting was supported by a "very large majority", with some members expressing a preference for 50bps given the potential financial stability and economic activity ramifications of an "overly aggressive pace of tightening." This time around, a downshift to a 50bps increment is expected by 45 of the 62 economists surveyed by Reuters, while market pricing assigns an approximately 87% chance to such a move. Chief economist Lane has laid the groundwork for a potential slowdown in the cadence of rate increases by noting that he would be reasonably confident in saying that "it is likely we are close to peak inflation." Lane added that in December, "we should take into account the scale of what we have already done. So the basis for the decision will be different [compared to September and October]." That said, the Governing Council does not appear to be unanimous in stepping-down to a 50bps pace of tightening; Austria's Robert Holzmann backs another 75bps increase, whilst the influential Isabel Schnabel of Germany said that incoming data thus far suggests to her that scope to slow the rate of adjustments remains limited. ING is of the view that an "earlier and more significant" form of QT could be the compromise required by hawks in order to back a slower pace of rate hikes." Accordingly, the Dutch bank expects the ECB to "announce a gradual reduction of the reinvestments of its bond holdings under the Asset Purchase Programme (APP) at the December meeting, with the aim to stop the reinvestments by end-2023." It adds that the Italian BTP-German Bund yield spread being below 190bps is probably where most would have put it before the ECB embarked upon unwinding its bond portfolio. Looking beyond the December meeting, a further 75bps of tightening is fully priced in for 2023, and that would take the deposit rate to 2.75%, into restrictive territory, with policymakers broadly of the view that rates are "close to neutral."

BANXICO ANNOUNCEMENT (THU): After two successive 75bps rate rises, the Banxico is expected to downshift the rate of interest rate increase in December, as has been suggested by some of its officials this week. But the central bank is still expected to tighten policy, with many expecting a 50bps rate rise, following the 600bps of tightening already implemented this cycle, in order to tame surging consumer inflation. The slowdown will be supported by a slightly easier tone in recent CPI data, which showed consumer prices rising 0.6% M/M (exp. +0.7%), and easing to 7.8% Y/Y (exp. 7.9%) from the prior 8.4%. Traders will be looking for signs from the central bank that it is close to concluding its hiking cycle; Franklin Templeton's analysts expect Mexico's terminal rate to be at 11% in H1 2023, and believes that the central bank will then begin to lower rates.

CBR ANNOUNCEMENT (FRI): Analysts continue to expect Russia's central bank to hold its key rate at 7.5% through the end of this year, according to Reuters' monthly poll. The central bank's own monthly analyst poll notes that the economy has overcome the short-term slump in wake of the partial mobilisation, with the disinflationary impact of that mobilisation having now disappeared. Over the next couple of years, these analysts see GDP growth being capped by a reduced labour force, however, which is likely to have a pro-inflationary effect, with these risks expected to become more apparent in the medium-term. Ahead, the CBR is expected to have lowered rates to 6.75% by the end of 2023, according to the latest Reuters poll.

BOC REVIEW: The Bank of Canada lifted its policy interest rat by 50bps; expectations were split among analysts going into the meeting between a 25bps or 50bps move, although the outcome was more hawkish than the 25bps that money markets were leaning towards. Importantly, the central bank altered its forward guidance on rates, and now says it will consider if future rate rises are necessary to bring supply and demand back into balance and return inflation to target. The change in guidance signals that the BoC could pause for now while it assesses the impact of the tightening already implemented, though leaves the door open for further hikes if the data does not cooperate. On inflation, the BoC said three-month rates of change in core inflation have come down, an early indicator that price pressures may be losing momentum. However, the central bank said inflation as still too high, short-term expectations remain elevated, and the longer that consumers and businesses expect inflation to be above the target, the greater the risk that elevated inflation becomes entrenched. Money markets are pricing in another hike in January, however, albeit a smaller 25bps move. The guidance alteration, according to RBC, “clearly opens the door to a pause as soon as the next meeting in January, and in our view frames that decision as between 0 and 25bps.” Looking ahead, the central bank will be data-dependent when assessing the need for ongoing rate hikes. RBC also highlights that the central bank will likely be watching changes in financial conditions: “a further decline in yields could prompt push-back from the BoC, either through another hike in January or emphasis that rates will have to remain high for an extended period.” RBC is expecting a challenging consumer backdrop and an ongoing pullback in the housing sector, which will see the Canadian economy slip into a recession in H1 2023; that said, with elevated inflation, the central bank might not react as quickly to the recession as it has in recent cycles.

BCB REVIEW: The Copom held the Selic at 13.75%, in line with the consensus expectation. The central bank also reiterated its forward guidance on interest rates, where it will remain vigilant, assessing if the strategy of maintaining rates for a sufficiently long period will be enough to ensure the convergence of inflation, and again emphasised that it will persist until the disinflationary process consolidates and inflation expectations anchor around its targets, while future policy steps can be adjusted, and it will not hesitate to resume the tightening cycle if the disinflationary process does not proceed as expected. The central bank also raised its inflation forecasts over its forecast horizon, but still sees inflation falling back to the 3.0% target (+/- 1.5%) in 2024. SocGen’s analysts said that the statement and forecasts raises the risk that the easing cycle might not begin any time soon. SocGen sees the process of lowering rates beginning in March, assuming that inflation does not begin re-accelerating in the near-term, and the bank sees the Selic ending next year at 11.00% (the consensus looks for 11.75%), though SocGen notes that by implicitly implying a flatter-than-expected easing cycle, the December statement raises upside risks to its end-2023 forecast. Beyond next year, SocGen sees the Selic ending 2024 at 9.0%, which is above the consensus view for 8.5%.