Central Banks Weekly Dec. 16th: Previewing PBoC, BoJ, CBRT; reviewing FOMC, ECB, BoE, SNB, Norges, Banxico, CBR

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PBOC PREVIEW: The PBoC is likely to keep its benchmark lending rates unchanged next week with the 1-Year Loan Prime Rate expected to be held at 3.65% which most loans are based on, while there are differing views on the 5-Year Loan Prime Rate which is the reference rate for mortgages and currently sits at 4.30%. The central bank has refrained from any adjustments to both the 1-Year and 5-Year LPRs since it last cut in August and is anticipated to continue maintaining the benchmark lending rate at the current level owing to the slowdown in China's economy and to avoid unwanted pressure on the local currency as most of the major central banks around the world further tighten their monetary policy settings. Recent developments in China also support the case to maintain rates including the shift from zero-COVID policy to a faster reopening which could support an economic recovery, but at the risk of another surge in infections, while a recent RRR cut that took effect earlier in the month and was seen to release around CNY 500bln in long-term liquidity, also suggests there is less urgency for the central bank to adjust lending rates. Furthermore, the PBoC decided to keep the 1-Year MLF rate unchanged within the past week which is a leading signal for the central bank's intentions for its benchmark rates, although Chinese press reports have suggested that the recent RRR cut could push the 5-year Loan Prime Rate lower this month.

BOJ PREVIEW: The BoJ is expected to maintain its monetary policy settings next week with the central bank to keep rates unchanged at -0.10% and continue its QQE with Yield Curve Control to target 10yr JGB yields at around 0%. As a reminder, the BoJ was unanimous in its decision to keep policy settings unchanged at the last meeting in late October where it reiterated its forward guidance that it expects short- and long-term policy interest rates to remain at their present or lower levels and that it will not hesitate to take additional easing measures if necessary. Furthermore, the latest Outlook Report contained a downgrade in Board members' median forecasts of Real GDP for Fiscal 2022 and 2023, but higher estimates for Core CPI throughout the 3-year projection horizon. The language from the central bank has remained dovish as Governor Kuroda noted that they are not at the stage where they can debate an exit and that raising interest rates now would hurt the economy still in the midst of recovering from the pandemic's impact, so is undesirable, while he also reiterated that deepening the negative rate is among the policy options if needed. Conversely, one of the newer board members Tamura recently called for the BoJ to conduct a review of its monetary policy framework and said that whether the BoJ needs to tweak policy will depend on the outcome of the review, although this was an extremely rare opinion within the central bank and triggered plenty of pushback from other Board members that essentially reinforced the view of no policy changes at least for the remainder of Governor Kuroda's term which ends in April next year.

CBRT PREVIEW: After 500bps worth of rate cuts over the last four months, taking its repo rate to 9.00%, analysts predict that Turkey's central bank will stand pat on policy, having reduced its key rate to single digits, as commanded to do so by the nation's President, and having guided towards such an outcome at its previous policy meeting. Data for November showed inflation pressures easing for the first time in 17 months, and having peaked at 85.5% in October, the CBRT is of the view it will fall further to 65.2% by the end of this year (analysts are expecting a reading a little higher, around 69%). Credit Suisse recently said that 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," arguing that "a conventional policy adjustment will likely be delivered if and when ad hoc measures have been exhausted." It has also argued that the timing of this adjustment will hinge on politics, and in particular, the timing of the Presidential and Parliamentary elections, which must take place no later than June 2023.

FOMC REVIEW: The Fed voted unanimously to lift the Federal Funds Rate target by 50bps to 4.25-4.50%, as expected, and downshifting the pace of hikes. The Committee, however, raised its expectation of where rates will peak, now seeing the terminal level at 5.1% (in the 5.00-5.25% bracket) vs 4.6% (the 4.50-4.75% bracket) it had projected in September. That implies 75bps further tightening in 2023; after that point, the Fed expects to cut rates, and sees the Federal Funds Rate target at 4.1% by the end of 2024. Its updated rate forecasts suggest that the central bank wants to keep rates elevated for longer as it battles with above target inflation (historically, it has remained at terminal for between 3-15 months, and 6.5 months on average). The FOMC statement was little changed, and still guides for "ongoing increases" in interest rates; some had flagged an outside risk of this language being tweaked to something along the lines of "some further" rate increases. Elsewhere, the growth profile was upgraded a little for 2022, but lowered for 2023

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and 2024; the inflation forecasts were raised across the horizon, though it left its long-term PCE view at 2.0%. On the labour market, the central bank revised its unemployment projection a little lower for this year (3.7% vs 3.8%), but nudged it up for 2023 and 2024, where unemployment is seen at 4.6%, before falling to 4.5% in 2025. At his post-meeting press conference, Chair Powell said that the Committee had increased estimates of the terminal rate at each subsequent SEP this year, and he did not rule out further increases in future meetings, depending on incoming data. Further, Powell said that the focus is on moving policy to a sufficiently restrictive stance, though added that he thinks policy is getting to a 'pretty good place' and closer to sufficiently restrictive, but expects that ongoing rate hikes are still appropriate. While the inflation data for October and November showed a welcome reduction in the monthly pace of price pressures, the Fed still has more work to do, and he reiterated that the Committee is strongly committed to bringing inflation back to the 2% goal. He added that risks to inflation are weighted to the upside, and it will take substantially more evidence to have confidence that inflation is on a sustained downward path.

ECB REVIEW: As expected, the ECB stepped back from its 75bps cadence of rate hikes and opted to raise its key three rates by 50bps a piece, taking the Deposit rate to 2.0%. Furthermore, the Governing Council judges that "interest rates will still have to rise significantly at a steady pace to reach levels that are sufficiently restrictive". The statement reiterated that future policy rate decisions will continue to be data-dependent and follow a meeting-by-meeting approach. On the balance sheet, from the beginning of March 2023 onwards, the APP portfolio will decline at an average pace of EUR 15bln per month until the end of Q2 with its subsequent pace to be determined over time. Lagarde later noted that the EUR 15bln figure represents roughly half of redemptions over that period of time. The accompanying macro projections saw 2022 HICP upgraded to 8.4% from 8.1%, 2023 raised to 6.3% from 5.5% with 2024 and 2025 seen at 3.4% and 2.3% respectively and therefore indicative that further tightening will be required to bring inflation back to target over the medium term. On the growth front, 2022 GDP was upgraded to 3.4% from 3.1% and 2023 now seen at just 0.5% (prev. 0.9%) with the upcoming recession likely to be shallow and short-lived. Thereafter, 2024 and 2025 GDP is seen at 1.9% and 1.8% respectively. At the follow-up press conference, Lagarde was defiant in her hawkish stance and even went as far as pre-judging the February meeting by stating that markets should expect a 50bps pace of hikes for a period of time. Lagarde later noted that info predicates 50bps at the next meeting, "possibly the next one as well and possibly thereafter". In terms of the unanimity of the Board, Lagarde stated that there was a very broad majority view that the ECB should show perseverance. However, some wanted to do a bit more and some a bit less. Later, sources showed that over a third of ECB policymakers wanted to opt for a larger 75bps hike. Overall, despite the ECB's negative experience earlier in the year by prejudging the magnitude of rate hikes ahead of time, Lagarde appeared to be willing to play the same card again in an attempt to highlight her hawkish stance and put the inflation genie back in the bottle. Time and a likely tough winter for the Eurozone will tell if this was a brave or misjudged move from the President. As it stands, market pricing puts the terminal rate at around 3%.

BOE REVIEW: As expected, the MPC opted to step down the pace of its rate hiking cycle to 50bps from 75bps, taking the Base Rate to 3.5%. The decision to move on rates was not a unanimous one with dovish dissent from Dhingra and Tenreyro who voted for no change. They framed their decisions on the viewpoint that the current setting of the Bank Rate was more than sufficient to bring inflation back to target, before falling below target in the medium term. At the hawkish end of the spectrum, external member Mann backed a 75bps hike on the basis that it would reinforce the tightening cycle and lean against an inflation psychology that was embedding in wage settlements and inflation expectations. Elsewhere, the statement noted that further increases in the Bank Rate may be required; according to a "majority" of the Committee. Additionally, the statement did not repeat the November line that rates are unlikely to reach the peak implied by the market. ING notes that this adjustment was not too surprising given that market rates have fallen markedly since the political drama and LDI (Liability Driven Investing) pensions issues in October. The MPC is of the view that CPI inflation has reached a peak, but is expected to remain high in the coming months. Overall, ING concludes that their best guess is the MPC will deliver another 50bps hike in February before pausing its rate hike cycle at a peak rate of 4%. Capital Economics holds a more hawkish view and looks for 50bps increases in both February and March.

SNB PREVIEW: Overall, very much as expected from the SNB. A 50bp hike was delivered to 1.00% with the only 'major' tweak being the replacing of "further" with "additional" in the forward guidance line; though, it remains to be seen what, if any, bearing this alteration has. For reference, Chairman Jordan did not elaborate on this much in the presser. Rates aside, FX language was reiterated and the Exemption Threshold altered to account for the 50bp move. As such, the reaction was limited but the Franc did experience some modest pressure, perhaps spurred on a 'buy the rumour, sell the fact' narrative given the as-expected move and the inflation forecasts now showing Switzerland at a peak, limiting the need for further tightening. Within the subsequent press conference, the main but perhaps unsurprising point was Chairman Jordan explicitly confirming that the SNB has sold foreign FX in recent months; additionally, he reiterated a willingness to undertake two-way intervention.

NORGES BANK: Overall, very much as expected from the Norges Bank. Which delivered the flagged (by Governor Bache in the last press conference) 25bp hike, alongside acknowledging that inflation remains elevated, the labour market is slightly tighter and the economic slowdown might be longer lasting than forecast in September - in-fitting with what data has shown since. In terms of policy ahead, the Repo Path was subject to very minor downside alterations and implies around 35bp of tightening before a peak around March 2023; i.e. a 25bp move in Q1 2023 and then some optionality for another move, if inflation remains stubbornly elevated as the forecasts for CPI-ATE imply. Following the announcement, EUR/NOK saw fleeting downside though this was limited in both duration and magnitude.

BANXICO REVIEW: Mexico's central bank lifted rates by 50bps, as expected, to 10.50%, matching the move from the Fed on Wednesday. The decision was not unanimous, however, with Gerardo Esquivel opting for a smaller 25bps rate rise - he has previously spoken of deviating from the Fed. The Bank continued to signal that further rate hikes will be needed, although specifically said at its next "meeting" rather than "meetings" it has previously used; at the next meeting it will assess if the reference rate needs to be further adjusted. Its inflation forecasts were revised marginally higher, but left unchanged for 2023, though core CPI saw revisions higher from Q4 this year to Q1 2024. It still expects inflation to return to its 3% target by the end of 2024. Analysts at Pantheon Macroeconomics expect Banxico to deliver a 25bp hike in February, albeit they say it is unnecessary, and add that they cannot rule out another 25bp hike in March.

CBR REVIEW: Russia's central bank held its key rate at 7.50%, in line with what the market was expecting. It said that the medium-term balance of risks remains pro-inflationary, while short-term inflation risks have also increased. Analysts at Capital Economics said that this suggests that the central bank's easing cycle is unlikely to resume any time soon. CapEco says the CBR would need to see inflation expectations fall back, and the CBR would need to be confident that the pro-inflationary risks in the future have faded. "We doubt this will be the case until mid-2023 and expect one more 50bps interest rate cut to 7.00% next year," it wrote.