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Central Bank Weekly February 10th: Reviewing Powell, BoC Minutes, RBA, Riksbank, Banxico

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FED CHAIR POWELL REVIEW: Fed Chair Powell had a message for both the hawks and the doves; in his initial remarks, he reiterated the message from his post-meeting press conference last week, that the disinflationary process had begun, but was at a very early stage and would be bumpy. He was encouraged that the process had started without damaging the labour market. On the January jobs report, Powell said that the labour market was very strong, which he was not expecting, and added that if data were to continue to come in stronger than expected, the Fed would certainly raise rates more, adding that the jobs data showed why the Fed thinks returning inflation to target will be a process that will take a significant period of time. Powell emphasised again that the Fed probably needs to hike rates further as they have still not reached a sufficiently restrictive level. The Fed Chair concluded by stressing that if strength in the labour market continues, or higher inflation reports continue to be seen, the FOMC may need to hike more than what is priced in; his base case is that it will take some time to get inflation down, while the Fed will need to do more rate hikes, and then look to see if it is enough.

BOC MINUTES REVIEW: The BoC meeting minutes noted that the January rate hike was due to labour market tightness and stronger than expected Q3 GDP. Data on jobs and economic activity suggested there was more excess demand in the economy over Q4 than thought, and the risk of inflation getting stuck somewhere above 2% later in the projection horizon was another reason to hike, it said. The Council felt more tightening now could help insure against inflation becoming stuck above 2%, but it wanted to convey that the bar for additional rate hikes was now higher. The Council also debated whether to leave the policy rate unchanged on the grounds it was starting to work and just needed more time, and also debated whether to maintain forward-looking language from the previous statement or signal a pause. Ultimately, it felt that it was important to be clear about the conditionality of any pause, given inflation was still well above target. Elsewhere, it said tighter monetary policy could have a greater-than-expected effect on the housing market, and across the border, the US debt ceiling negotiations could be protracted and pose risks of financial volatility if an agreement were elusive.

RIKSBANK REVIEW: As expected, the Riksbank hiked its benchmark rate by 50bp to 3.00%. However, the details of the announcement were hawkish in nature as the new Policy Path Peak is now 3.33% (prev. 2.84%) and, as explicitly stated by Governor Thedeen, implies either a 25bp move with room to spare, or a 50bp hike in April. Notably, the path does not imply any rate cuts. Rates aside, the Riksbank provided more details than perhaps expected on its asset holding plans, after guiding towards a decrease in-line with maturities this year at the November gathering. A QT remit is scheduled to begin in April and this provides the possibility for it to be used as a complementary tool to rates given a fast pace of bonds, with the Governor remarking February's decision was mainly SEK-motivated. Finally, commentary on the economy was fairly balanced, acknowledging the pressure Sweden is facing, but taking the view that it is better to take action now to reduce the risk of inflation becoming entrenched. Overall, a hawkish-hike from the Riksbank which spurred substantial SEK appreciation.

RBA REVIEW: The RBA hiked rates by 25bps to a fresh decade high of 3.35%, which was widely expected as money markets had priced in over a 90% probability of such a move, so attention turned to the accompanying commentary stating that the Board expects further rate increases and is resolute in its determination to return inflation to target. The RBA also said inflation is expected to decline this year due to both global factors and slower growth in domestic demand, as well as noting uncertainty about the expected slowdown in household spending and how the global economy responds to the large and rapid increase in interest rates around the world. Furthermore, it added that these uncertainties mean there is a range of potential scenarios for the Australian economy and it opted to maintain its forecasts for 2023 GDP growth and CPI at 1.5% and 4.75%, respectively. The signal for further rate increases was the key highlight from the statement as there had been mixed views regarding the central bank's future intentions, with CBA among those that had previously anticipated this to be the last hike in the cycle, while the median view from a Reuters poll going into the meeting was for the central bank to hike again next month before pausing. As such, the hawkish rhetoric prompted CBA to adjust its call in which it now expects the RBA to hike at the next two meetings and a more recent poll showed that economists have raised their terminal rate view to 3.85% from 3.60%.

RBI REVIEW The RBI hiked the Repurchase Rate by 25bps to 6.50% as expected through a 4-2 vote (prev. 5-1) in which MPC member Goyal joined prior dissenter Varma in voting against the rate increase, and both continued to oppose the decision to keep the policy stance of remaining focused on the withdrawal of accommodation, which was

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made via a 4-2 vote (prev. 4-2). The RBI also raised its Standing Deposit Facility Rate and the Marginal Standing Facility Rate by 25bps each, to 6.25% and 6.75%, respectively. The rhetoric from Governor Das remained hawkish in which he noted that further calibrated monetary policy action is warranted and the situation remains fluid and uncertain, while he added that the stickiness of core inflation is a matter of concern and the Bank needs to see a decisive fall in inflation. Furthermore, Das said the MPC will continue to maintain a strong vigil on the inflation outlook and the outlook is clouded by global uncertainties, but noted overall monetary conditions remain accommodative and economic activity in India remains resilient. The commentary does suggest further rate increases are warranted which goes against the median view by economists leading up to the meeting for the central bank to pause thereafter, although it seems that local bond traders are betting against additional hikes with India’s 10yr yield only higher by low single-digit basis points since the meeting.

BANXICO REVIEW: The Mexican central bank delivered a more hawkish rate rise, lifting its key rate by 50bps to 11.00% (exp. +25bps). The language suggested that it could also lift rates by a further 25bps at its March meeting. The updated economic projections saw inflation forecasts lifted over the course of its horizon, though still anticipates that core inflation will converge with the target in Q4 of 2024. Our terminal rate expectation was 11.25% (higher than the consensus estimate) before this meeting even though we had seen some downside risks beforehand. Analysts at SocGen said that following January’s inflation data and Banxico’s hawkish statement, it now sees a substantial upside risk of the terminal rate going beyond 11.25% in Q2 - previously, it had suggested that there were downside risks to that forecast.

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