Central Bank Weekly May 12th: Previewing PBoC and RBA minutes; reviewing BoE, BoJ, Riksbank minutes

PREVIEW

PBOC MLF (MON): Ahead of the Loan Prime Rates (LPRs) announcement next Monday, the PBoC is expected to maintain its 1yr Medium Term Facility Rate (MLF) at 2.75%. Analysts note that ongoing improvements in consumption, partly aided by the Golden Week Holiday, suggest that a recovery is underway, whilst a cut to the MLF would be perceived by the market that the economy is not on the desired path of recovery. Analysts at ING suggest “the challenge from a weaker external sector cannot be addressed by a rate cut. It is possible that the central bank may add more liquidity to the money market via the MLF operation. But that should not lower the market interest rate significantly unless the scale of liquidity injection is large, which is not our expectation.”

RBA MINUTES (TUE): The RBA minutes will largely focus on the reasoning behind the surprise 25bps hike at the May meeting. To recap, the RBA blindsided markets at this month’s meeting when it delivered an unexpected rate increase to resume its policy tightening cycle with its 11th hike in 12 meetings. The language remained hawkish as the Board expects some further tightening of monetary policy will be needed and remains resolute in its determination to return inflation to target whereby it will do what is necessary to achieve that goal. It also stated that the central forecast remains that it will take a couple of years before inflation returns to the top of the target range. The Board noted inflation in Australia has passed its peak, but is still too high at 7% and it will be some time yet before it is back within the target range. Furthermore, RBA Governor Lowe commented in a speech hours after the meeting that the Board had a strong consensus to raise rates and is deadly serious about bringing inflation back down, while the RBA’s quarterly Statement on Monetary Policy stuck with the hawkish tone in which it reiterated that it will do what is necessary to return inflation to target and some further tightening may be required to do that over a reasonable timeframe.

REVIEW

BOE REVIEW: As expected, the MPC delivered a twelth consecutive hike by raising the Bank rate by 25bps to 4.5% via a 7-2 vote split. Once again, Tenreyro and Dhingra voted for an unchanged rate on the basis that they judged prior tightening was yet to make its way into the economy. The MPC also opted to retain guidance that "if there were to be evidence of more persistent pressures, then further tightening in monetary policy would be required". As such, this disappointed some of those in the market with dovish expectations who had been hoping that the MPC would provide a signal that June would see a pause in interest rate hikes. The accompanying MPR projections showed upgrades to the inflation profile with the 2023 projection raised to 5.0% from 4.0%. Crucially, inflation in 2025 is seen materially below the MPC's 2% target at just 1% and therefore indicates that market pricing (upon which the forecasts are based) is too aggressive over the medium-term to be consistent with the BoE's goals. On the growth front, as was expected, 2023-2025 GDP projections were upgraded with the MPC no longer forecasting a UK recession. At the follow-up press conference, Governor Bailey avoided giving markets a "directional steer on rates", stating that policy will be guided by the evidence. Bailey did note however, that the Bank "must stay the course to ensure inflation returns to 2%". Overall, after getting burned by a hot CPI report last month, the MPC is non-committal on further action, however, markets hold a hawkish bias in pricing a June hike at around 60% with the terminal rate seen around 4.87% which suggests markets expect another 25bps and are split over another one thereafter.

BOJ REVIEW: The BoJ's Summary of Opinions from the April meeting adhered to the central bank’s dovish tone as it stated that they must continue with the current easy policy given uncertainty over the global outlook and must support the wage hike momentum through monetary easing. It also noted that the achievement of the price target appears to have come in sight, but they must maintain easy policy for the time being given downside and upside risks, as well as ensure that the tweak to interest rate forward guidance is not interpreted as a sign that the BoJ would allow future rate hikes and should not target a specific monetary policy change when guiding the policy review to ensure it would be neutral and convincing. Furthermore, the central bank stated that Japanese inflation is likely to approach the BoJ's target as wages rise. but it will take time and uncertainty is high, while it added there is a risk that sluggish real wages may push inflation well below 2% and not return to the target level.

RIKSBANK MINUTES REVIEW: Overall, the Minutes cement the case for a final 25bp hike to be delivered in the June gathering. Heading into the release, there was some discrepancy over whether the last move would occur in June or September. The minutes, while noting members expect inflation to continue to moderate, also highlight that all members believe that policy needs to be tightened further - seemingly skewing expectations for the final hike to the June announcement. Rate aside, further emphasis was unsurprisingly placed on the SEK while there was no substantial discussion on QT at the meeting.