Central Bank Weekly June 9th: Previewing FOMC, ECB, BoJ; Reviewing BoC, RBA, RBI

PREVIEWS:

FOMC POLICY ANNOUNCEMENT (WED): A Reuters poll revealed that economists generally expect the FOMC to hold rates at 5.00-5.25% next week, with only 8 of the 86 surveyed forecasting a 25bps rate rise. Looking ahead, 32 of the 86 economists surveyed still foresee at least one more rate hike later this year. Goldman Sachs thinks the Fed will pause at the June meeting to assess the impact of previous rate hikes, as well as tighter bank credit, before considering another rate increase, with officials likely seeing a pause as a prudent measure to avoid accidentally overtightening. Goldmans says that economic downside risks have diminished, with resilience seen in hard data like spending and the labour market outweighing weakness in other survey data. The bank recently lowered its outlook on a recession, assigning a 25% probability (from 35%), and argues that progress towards a soft landing is on track, supported by improvements in the jobs market, reduced labour shortages, and cooling wage growth. GS also notes that although core PCE inflation has fallen less than expected, a significant deceleration is anticipated later this year. The bank says Fed officials have less reason to be concerned compared to last summer as inflation psychology normalizes and signs of cooling emerge.

ECB ANNOUNCEMENT (THU): All 62 economists surveyed expect the ECB to come to market with another 25bps hike, taking the deposit rate to 3.5%. Market pricing concurs, with 26bps of hikes priced in for the announcement. To recap events at the previous meeting in May, the ECB stepped down to a 25bps increment from the previous 50bps adjustment with the need to keep on hiking justified by the judgement that the "inflation outlook continues to be too high for too long". The reason for the smaller size rate rise was based on the view that "past rate increases are being transmitted forcefully to euro area financing and monetary conditions”. Since the prior meeting, headline Eurozone CPI has cooled to 6.1% from 7.0%, whilst the “super-core” measure fell to 5.3% from 5.6%. Furthermore, the ECB’s Consumer Expectations survey for April saw the 1yr ahead inflation expectation decline to 4.1% from 5.0% and 3yr view fall to 2.5% from 2.9%. That said, despite the disinflationary impulses, President Lagarde has reiterated that inflation “is too high and is set to remain so for too long”, adding that the ECB will “keep moving forward”. In terms of what happens beyond June, as it stands, markets assign a roughly 75% chance of a further 25bps move in July. However, for now, the ECB will likely continue to stress its “data-dependent approach” and therefore any calls for next month will need to be premised on how the data plays out between now and then. Beyond July, markets will be paying attention to the accompanying macro projections and how medium-term inflation forecasts align with the ECB’s mandate. On which, ING expects the 2025 headline and core inflation forecasts to be held at 2.1% and 2.2% respectively. That said, due to the recent inaccuracy of ECB projections, they will likely be taken with a large pinch of salt in some quarters.

BOJ ANNOUNCEMENT (FRI): The BoJ is expected to keep policy settings unchanged at its meeting next week with the Bank Rate to be kept at -0.10% and QQE with YCC to be maintained at the current parameters. As a reminder, the BoJ kept its policy settings unchanged at the last meeting in April which was the first policy decision under Governor Ueda’s leadership, with the decision on QQE with YCC made unanimously, while it tweaked its forward guidance whereby it dropped the reference to the COVID-19 pandemic and its pledge to keep interest rates at current or lower levels, although the new guidance remained dovish with the BoJ to take additional easing steps without hesitation as needed while striving for market stability. The central bank also announced a broad-perspective review of monetary policy with a planned timeframe of one to one and a half years which supported the notion of a slow exit from ultra-easy policy, but Governor Ueda later clarified during the press conference that they will make changes to monetary policy as needed during the review period and may announce results of the policy review in the interim if required. Since then, rhetoric from the central bank has continued to suggest a lack of urgency to normalise policy as Governor Ueda has repeated that there is still some distance before hitting the inflation target stably and sustainably and the BoJ will patiently sustain easy monetary policy, while he added that the BoJ must avoid tightening prematurely and should stick to its 2% inflation target. Ueda also warned that premature tightening could hurt companies even in good health and may weaken the economy's potential, as well as noting that patiently maintaining easy policy would heighten Japan's potential growth in the long run. The recent data releases have been mixed which support the view of keeping policy settings unchanged with the Revised GDP for Q1 stronger than expected at an annualised growth rate of 2.7% vs. Exp. 1.9% (Prelim. 1.6%), although the latest Industrial Production, Retail Sales and Household Spending figures all disappointed, while inflation metrics were mostly in line with expectations with the headline and core CPI at 3.5% and 3.4%, respectively, but CPI Ex. Fresh Food & Energy YY showed the fastest pace of increase since September 1981 at 4.1%. Nonetheless, this is not expected to spur a policy shift from the central bank as Governor Ueda has noted that they haven't achieved sustainable 2% inflation and inflation is to slow greatly around the middle of FY23.

Copyright © 2023 Newsquawk Voice Limited. All rights reserved.

Registered Office One Love Lane, London, EC2V 7JN, United Kingdom · Registered Number 12020774 · Registered in England and Wales.

newsquawk.com · +44 20 3582 2778 · info@newsquawk.com

ECB TLTRO REPAYMENT (FRI): The repayment figure for ECB TLTRO III.5-10 will be announced on June 16th at 11:05BST, by which point EZ banks should have repaid around half the outstanding TLTRO funding and Goldman Sachs looks for some EUR 500bln of repayments. Subsequently, the key repayment date GS identifies is March 2024, though when that arrives over 90% of the TLTRO funds will have been repaid. In terms of reaction, the bank does not believe the announcement will result in banking system tensions. Given much of the focus for TLTRO is on Italy, it is worth highlighting that the BTP-Bund yield spread remains steady below 180bps. On June 28th, the TLTRO.III 4 operation will mature and SocGen writes this will represent flows of circa. EUR 480bln with the bulk potentially arising from Italy given domestic data points to borrowing of near EUR 250bln in this tranche. SocGen highlights that whether the maturity has an impact is dependent on a number of factors and as such expects some risk premia to emerge in the Italian repo market; but adds that if this passes by without incident, so should the remainder of 2023.

REVIEWS:

RBA REVIEW: The RBA surprisingly raised the Cash Rate Target by another 25bps to 4.10% (exp. 3.85%), while it reiterated that the Board remains resolute in its determination to return inflation to target and some further tightening of monetary policy may be required. It also repeated that inflation in Australia has passed its peak, but at 7% is still too high and it will be some time yet before it is back within the target range. The Bank stated that this further increase in interest rates is to provide greater confidence that inflation will return to target within a reasonable timeframe, as well as noting that recent data indicates upside risks to the inflation outlook have increased and the Board has responded to this. Following the decision, analysts at Deutsche Bank suggested markets should price in more than just one additional rate hike.

BOC REVIEW: In a surprising move, the Bank of Canada (BoC) decided to hike rates by 25bps to 4.75%, citing the need for a more restrictive monetary policy to address imbalances in supply and demand and achieve sustainable inflation at the 2% target. The BoC expects CPI inflation to ease to around 3% in the summer, but there are concerns that it could remain significantly above the target. The statement highlighted a tight labour market conditions and persistent excess demand in the economy. Services demand is rebounding, and housing market activity has picked up. The BoC removed language indicating its preparedness for further rate hikes, however, emphasising a data-dependent approach, and said it was monitoring core inflation and CPI outlook. Oxford Economics believes that Canada's strong Q1 economic performance was temporary, anticipating a recession in the latter half of 2023 due to the impact of past rate hikes. It argues that if labour markets, wage growth, and inflation do not slow as expected, the BoC could hike rates again in July. This would likely lead to a downward revision of economic forecasts for the latter part of 2023 and 2024. The BoC will assess new job reports and an inflation report before its next rate decision on July 12th.

RBI REVIEW: The RBI kept the key Repo Rate unchanged at 6.50%, as expected, with the decision made unanimously and it also maintained the policy stance of remaining focused on the withdrawal of accommodation through a 5-1 vote. Governor Das said the path ahead is now somewhat clearer and uncertainty on the horizon is comparatively less, while he added that the MPC will remain vigilant on the evolving situation and growth outlook. Das also said they will take further action promptly and headline inflation is still above target and that being within the tolerance band is not enough. The policy announcement was met with a muted reaction across asset classes as it provided no surprises to the market and nothing to shift the current median view for the central bank to stand pat for the rest of the year.

Disclaimer

The information contained within this document has been prepared and issued by Newsquawk Voice Limited (**"Newsquawk"**) on the basis of publicly available information and other sources believed to be reliable. Whilst all reasonable care is taken to ensure that the facts stated are accurate, neither Newsquawk nor any of its directors, officers or employees shall be in any way held responsible for its content or your use of it. Neither the provision of any content herein nor anything on our website or any other media we use is intended to, and should not be construed as, providing advice and/or enticing an offer or solicitation to invest in, buy or sell securities or other financial instruments.

Copyright © 2023 Newsquawk Voice Limited. All rights reserved.

Registered Office One Love Lane, London, EC2V 7JN, United Kingdom · Registered Number 12020774 · Registered in England and Wales.

newsquawk.com · +44 20 3582 2778 · info@newsquawk.com