Central Bank Weekly 30th June: Previewing RBA, FOMC Minutes; Reviewing BoJ SOO, Riksbank

PREVIEWS:

RBA ANNOUNCEMENT (TUE): The RBA will hold its policy meeting next week and analyst forecasts suggest a coin-flip as 16 out of 31 economists surveyed by Reuters expect another 25bps and 15 predict a pause at the current 4.10% level, while money markets are more decisive and are pricing in just a 37% probability for 25bps rate increase and a 63% chance for rates to be kept unchanged. As a reminder, the RBA defied the consensus for a pause in rates at the prior two consecutive meetings and instead opted to continue with its 25bps rate hike increments, while it noted at the June meeting that its actions were in response to the elevated inflationary environment and that data indicated that upside risks to the inflation outlook have increased. The statement remained hawkish and largely reiterated the prior month's rhetoric with the Board remaining resolute in its determination to return inflation to target and some further tightening of monetary policy may be required, while it also repeated that 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. The meeting and subsequent comments by officials initially spurred some hawkish adjustments to rate forecasts, including Goldman Sachs which raised its view for rates to peak at 4.85% in September from a prior view of 4.35% in July, while NAB adjusted its call for rates to peak at 4.60% from 4.35% through back-to-back hikes in July and August. Nonetheless, this hawkish impetus eventually unwound a couple of weeks later after the Minutes from the meeting revealed that the Board considered a rate rise of 25bps or holding steady and that the arguments were finely balanced, while softer-than-expected monthly inflation data from Australia which slowed to 5.60% vs. Exp. 6.10% (Prev. 6.80%) adds to the case for the RBA to stand pat. However, another surprise hike cannot be ruled out as inflation remains a distance from the central bank's 2-3% target range and considering that the central bank has gone against the consensus for a pause at the last two meetings.

FOMC MINUTES (WED): The Federal Reserve held rates steady in June, as expected, but surprised markets by raising its rate projections for 2023 and beyond. The forecasted rates for 2023 were increased by 50bps, indicating two further 25bps rate rises ahead. The more hawkish forecasts were driven by an improved view of GDP growth, higher inflation expectations, and a lower projected unemployment rate. Despite the upward revisions, the long-term "neutral" rate remained unchanged. Fed Chair Powell acknowledged the progress made, but emphasised that the impact of tightening policy was yet to be fully realized. While most policymakers anticipate further rate hikes, they expect subdued growth to persist. Powell noted signs of improvement in the labour market's supply and demand balance, although demand still exceeded the available workforce. Inflation remains above the 2% target, but has moderated; Powell cautioned that reducing inflation may require below-trend growth and labour market adjustments. During his Q&A, he made a reference to the decision not to hike rates as a "skip," hinting at a possible rate increase in July. He emphasised the need for a more moderate pace of tightening. Powell said that a rate cut was unlikely and expressed limited concerns about the banking turmoil's impact. He discussed potential challenges in commercial real estate and projected a fall in the RRP and reserves during the TGA rebuild. Since the meeting, Chair Powell has reiterated that it would be appropriate to lift rates at least a couple of times (in keeping with the Fed's forecasts), stating that incoming data will be the influencing factor; he also has said that a majority of Fed officials support a couple of further rate hikes.

REVIEWS:

BOJ SOO REVIEW: The BoJ Summary of Opinions (SOO) from its June meeting (timelier than the policy Minutes) emphasised the need to maintain current monetary easing policies. The report stressed that sustainable wage growth, not just cost-push inflation, is crucial to meet price targets. Despite a growing willingness among smaller firms to raise wages and increase investment, the BoJ views any policy shift as premature. It plans to continue its ultra-accommodation while being cautious of a potential underestimation of Japan's price rise sustainability and side-effects. The shape of the yield curve is no longer distorted, the SOO said, so no operational changes to Yield Curve Control (YCC) are needed. However, an early review of YCC is advised, despite the continuation of easy monetary policy. The report acknowledged uncertainty about the recovery of inflation after a slowdown, and the possibility of consumer inflation surpassing initial expectations or remaining above 2% in the middle of the fiscal year. As a reminder, the BoJ maintained its ultra-easy policy settings at the June 15th-16th meeting, as widely expected, with the Bank rate kept at -0.10% and QQE with YCC left unchanged at the current parameters to target 10yr JGB yields around 0% within a +/-50bps band. The statement from the meeting provided very little in the way of fresh insight as it maintained the view that core consumer inflation is likely to slow the pace of increase towards the middle of the current fiscal year and noted that inflation expectations are moving sideways after heightening. Furthermore, its language on the economy was mixed in which it noted that activity is picking up and likely to continue recovering moderately, but also stated that uncertainty is very high, which is supportive of the view that the Bank will continue to take a cautious and patient approach. The commentary from Governor Ueda at the post-meeting press conference also pointed to a lack of urgency to tweak policy as he stated that more time is needed to meet the 2% inflation target and warned that responding to an inflation undershoot after a premature rate hike is more difficult than responding to an overshoot, but also noted they are weighing the benefits and side-effects of YCC and will update regarding the progress of the review of past policies on the BoJ website starting from July.

RIKSBANK REVIEW: The Swedish Central Bank hiked its benchmark rate by 25bps and increased bond sales in response to the weak Krona and high inflation. The decision to increase interest rates by 25bps matched general expectations, despite some predicting a 50bps hike due to recent SEK depreciation and high inflation data in May. The decision was made without any reservations, and the policy path now anticipates at least one more hike in 2023. Regarding the balance sheet, the monthly divestment pace was raised from SEK 3.5bln bln to SEK 5bln. The Bank acknowledged the effect of the weak SEK on inflation and announced a possible FX reserves currency hedging program. Analysts at Nordea suggest the decision was fairly in line with expectations – “We keep our forecast that the Riksbank will hike rates by 25bp in September to 4.00%, and stay on hold during the remainder of 2023. However, there is a clear risk that the SEK will continue to weaken, which could trigger rate hikes beyond 4.00%”, the bank says.