Central Bank Weekly 7th July: Previewing Riksbank, ECB Minutes, BoC, RBNZ, BoK; Reviewing FOMC minutes, RBA

PREVIEWS:

RIKSBANK MINUTES (MON): June’s meeting saw a 25bps hike as expected and guidance for further tightening ahead alongside a step up in the pace of bond sales. All measures which were more or less expected heading in. From this, the minutes will be scrutinised for just how much further tightening is likely, with the statement stating “at least one more hike this year”. Additionally, it will be interesting to see if any member(s) would have preferred another 50bps increment. The increased pace of bond sales to SEK 5bln from 3.5bln was shy of SEB’s 6-7bln forecast, and as such any discussion around alternative magnitudes will be closely monitored. Most interestingly, though not designed for monetary policy purposes, details on the Riksbank announcing it is considering hedging some of its FX reserves are keenly sought. Given that details are currently light, particularly on the monetary/SEK implications; though, desks are viewing it as a balance-sheet-related measure, not a behind-the-scenes way of influencing inflation and/or the SEK.

RBNZ POLICY ANNOUNCEMENT (WED): The RBNZ is likely to keep the Official Cash Rate unchanged at next week’s meeting at the current 5.50% level, with money markets pricing in a 92% probability that the central bank holds rates and just an 8% chance of a 25bps hike. As a reminder, the RBNZ unsurprisingly hiked rates by 25bps at the last meeting in May which was made by a majority of five votes to two and was the first time the Monetary Policy Committee voted on the decision. The announcement was seen as a dovish hike as the central bank maintained its peak rate forecast at 5.50%, and therefore implied that its hiking cycle is done, while it also omitted prior language regarding further rate increases and stated that the OCR is set to remain restrictive for the foreseeable future. The central bank also noted that the level of interest rates is constraining spending and inflation, while inflation is expected to continue declining from the peak and it forecast negative GDP growth for Q2 and Q3. Since that meeting, Governor Orr stated that rates are restrictive and well above neutral, as well as noting that economic growth and inflation are weaker than expected, while Assistant Governor Silk suggested being mindful of over-tightening monetary policy and that they can halt to see how things go. Furthermore, the latest GDP data showed that the economy dipped into a recession with Q2 GDP Q/Q at -0.1% vs. Exp. -0.1% (Prev. -0.6%, Rev. -0.7%) which further reduces the prospects of a rate hike.

BOC POLICY ANNOUNCEMENT (WED): After a five month ‘pause’, the consensus looks for the Bank of Canada to lift interest rates by 25bps for the second straight meeting in July, takings it key rate to 5.00%, according to Reuters. Recent inflation data showed a significant declin in price pressures, with the annual rate diving to 3.4% Y/Y from 4.4%, though some analysts suggested that it might be a result of base effect. The BoC itself does not see inflation returning to its 2% target until early 2025. “The slowdown may not be enough to remove another BoC rate hike from the table given stickier core rates of inflation, while a decent GDP report coupled with a tight job market suggests the economy remains sturdy,” BMO Capital Markets said. Analysts at another Canadian bank, RBC, said that data is pointing to more persistent momentum in consumer spending as well as labour demand, and the question is when are we going to be able to see a material slowdown in labour market conditions as well as the economic outlook; “in our heads, it is really a question of when, not so much whether it is going to happen,” RBC adds. The Reuters poll also finds that analysts are more split on the prospects of a recession, and ahead, analysts think that after the July hike, the BoC will likely keep rates unchanged well into 2024.

ECB MINUTES (THU): The ECB Minutes will be closely watched for any signs of a potential September hike, with a July hike wholly expected by markets, as pricing currently infers an 88% chance of a 25bps hike and 12% for a 50bps move. To recap the June meeting, the ECB delivered another 25bps hike to the Deposit Rate, taking it to 3.5%. The decision to raise rates was once again premised on the judgement that inflation “is projected to remain too high for too long”. Going forward, policy decisions will continue to follow a data-dependent approach and be taken on a meeting-by-meeting basis. Perhaps the main takeaway from the initial announcement came via the accompanying macro projections which saw upgrades to headline and core inflation for 2023 through 2025 with the core 2025 print expected above-target at 2.3%. From a growth perspective, 2023 and 2024 forecasts were revised lower by 10bps. Elsewhere, the GC confirmed that it will discontinue reinvestments under the asset purchase programme as of July 2023. At the follow-up press conference, when questioned on whether the GC expects to keep raising rates, Lagarde replied that there was still “more ground to cover” and that the ECB is not done on hikes. Note, Lagarde again refused to comment on where she saw the terminal rate. Since the June meeting, Bloomberg sources suggested the ECB is set for a “tough debate” next month over whether a possible September rate hike is needed. Meanwhile, at the ECB Sintra Forum (26-28th June), GC members largely kept the door open for a September hike, whilst refraining from telegraphing a terminal rate and keeping a data-dependent approach. On that front, EZ CPI for June was mixed vs expectations, with the core Y/Y rate narrowly topping forecasts (6.8% vs 6.7%), although headline and super-core both printed 0.1ppts under expectations.

BOK POLICY ANNOUNCEMENT (THU): The Bank of Korea is likely to maintain its 7-Day Repo Rate at the current level of 3.50% for the 4th consecutive meeting next week as softening inflation and expectations of weak economic growth reduce the urgency for the central bank to resume its hiking cycle. The BoK Board was unanimous in its decision to keep rates unchanged at the last meeting in May, although prospects of a future rate increase cannot be ruled out as six of the seven members saw the need to keep the door open for one more rate hike, while the accompanying statement noted that economic growth is to remain weak for some time and inflation will likely fall considerably before rebounding slightly for the rest of the year. Governor Rhee also stated that core inflation is not easing as much as Board members had expected and uncertainty increased over whether inflation will approach the 2% target before year-end, while a senior official pushed back against the view that monetary tightening is over and warned it is still too early to be relaxed over inflation. Nonetheless, an immediate policy adjustment is seen as unlikely given that inflation continued to soften in June with South Korean CPI YY at 2.7% vs. Exp. 2.9% (Prev. 3.3%), albeit remaining above the central bank’s target.

REVIEWS:

FOMC MINUTES REVIEW: The FOMC meeting minutes from the June meeting revealed that most participants favoured leaving the target rate unchanged, but some supported a rate hike due to a tight labour market and stronger economic activity. Participants suggested a moderation in the pace of tightening and emphasised the need to observe the effects of previous tightening. “Some participants” favoured another 25bps hike, but “most” believed that a pause “would allow them more time to assess the economy’s progress.” The minutes stated that “almost all” “judged that additional increases in the target federal funds rate during 2023 would be appropriate.” Most participants observed that post-meeting communications, including the SEPs (which pencilled in two more hikes this year), would help clarify their assessment regarding the stance of monetary policy. Ahead of the NFP reading on Friday, “some” pointed out that payroll gains had remained robust, but noted that some other measures of employment—such as those based on the BLS’ household survey, the Quarterly Census of Employment and Wages, or the Board staff’s measure of private employment using data from the payroll processing firm ADP—suggested that job growth may have been weaker than indicated by payroll employment. A couple of participants also drew attention to the subdued growth in hours worked. Overall, the minutes contained no major surprises, and the market’s outlook for policy was unchanged in wake of the release.

RBA REVIEW: The RBA kept rates unchanged at 4.10% vs near-evenly split analyst expectations between a 25bps hike and a hold. However, the language remained hawkish as it noted that the Board is still resolute in its determination to return inflation to the 2-3% target band and further tightening may be required to ensure that it achieves its goal within a reasonable timeframe, but this will be dependent on how inflation evolves. Furthermore, the central bank noted that a significant source of uncertainty continues to be the outlook for household consumption and the Board remains alert to the risk that expectations of ongoing high inflation will contribute to larger increases in both prices and wages. Looking forward, Westpac believes that the “case for more rate hikes remains strong”, due to a strong labour market, spurred on by low unemployment rates and high job vacancies. Therefore, this has led Westpac to raise its terminal rate forecast to 4.6%, indicating two further 25bps hikes in August and September and this view is also shared by analysts at Deutsche Bank.