Central Bank Weekly 11th August: Previewing RBNZ, PBoC MLF, Norges Bank, FOMC Minutes, RBA Minutes; Reviewing Banxico and RBI

PREVIEWS

PBOC MLF (TUE): PBoC is likely to keep its 1-year MLF rate unchanged at 2.65% next week despite continued weak data releases from China and the numerous support pledges by the central bank and other agencies. Chinese authorities have recently been out in force vowing several measures to support the economy including the PBoC which stated that RRR cuts, open market operations, MLF and all structural policy tools need to be flexibly used to maintain reasonably ample liquidity in the banking system, while it will guide banks to effectively adjust mortgage interest rates and support banks to reasonably control the cost of liabilities. It also announced guidelines to support the development of private firms and said it will implement differentiated housing credit policies in a "precise manner" and will support the stable and healthy development of the real estate market. However, these have mostly been targeted measures and the PBoC has reiterated it is to implement prudent monetary policy, while it is not expected to lower rates for short-term funding or the medium lending facility so soon after having just cut them in June for the first time in 10 months. The bank will also likely want to refrain from cuts to avoid unwanted pressure on its currency although future action such as a RRR cut is expected during H2 given the continued weak economic releases from China which recently slipped into deflation and showed a wider-than-expected contraction in the nation’s exports and imports.

RBA MINUTES (TUE): RBA will release the minutes from the August 1st meeting next week where it kept rates unchanged at 4.10% vs mixed views heading into the meeting as a majority of economists had called for a 25bps hike but money markets were heavily pricing the likelihood of a pause. Nonetheless, the central bank's language provided little new as it reiterated that some further tightening of monetary policy may be required and that the Board remains resolute in its determination to return inflation to target and will do what is necessary to achieve that. Furthermore, it reaffirmed the Board’s priority is to return inflation to the target within a reasonable timeframe and it sees inflation will be back at the 2%-3% target range in late 2025, while it noted higher interest rates are working to establish a more sustainable balance between supply and demand in the economy and will continue to do so but reiterated that a significant source of uncertainty continues to be the outlook for household consumption.

FOMC MINUTES (WED): With the Fed in a data-dependent policy-setting mode, the FOMC meeting minutes from the July meeting are not expected to contain many surprises. However, traders will be looking for any commentary on how the Fed assesses growth dynamics; given that inflation is slowly inching back down towards target, many expect the Fed to pivot policy, and eventually begin cutting rates to support the economy. Money market currently price in the terminal rate between 5.25-5.50%, though the Fed's June projections have pencilled in a further hike; markets are also expecting rate cuts to start in Q1 2024. Meanwhile, at the July meeting, the Fed raised interest rates by +25bps to 5.25-5.50%, in line with expectations. The statement was similar to June's, mentioning the possibility of further rate increases. It acknowledged that the economy is growing at a "moderate" pace instead of a "modest" one, and emphasised that job gains are strong, and the unemployment rate is low. Regarding inflation, the Fed remains cautious and watchful, not overreacting to a single datapoint. At his press conference, Chair Powell said future interest rate decisions will depend on data and the effects of tightening are not fully felt yet. He mentioned that inflation still has a way to go cool to 2%, but noted improvements in the labour market. However, he highlighted that consumer spending growth has slowed compared to earlier this year. In the Q&A, Powell did not give a clear signal about future rate decisions, again framing it around incoming data, adding that the Fed might raise rates in September if the data supports it. And while he suggested a slower pace of rate increases, lifting them at consecutive meetings was still possible. Powell mentioned that stronger economic growth could lead to higher inflation, requiring a policy response. He discussed the possibility of rate cuts in the future if inflation comes down convincingly. He wants to see inflation decrease sustainably, and wages may play a role in bringing it down.

RBNZ ANNOUNCEMENT (WED): The RBNZ is likely to keep rates unchanged at next week’s meeting with money markets pricing a 99% probability that the Official Cash Rate will be maintained at the current level of 5.50%. As a reminder, the RBNZ left the OCR unchanged at the prior meeting to snap a streak of 12 consecutive rate hikes which was widely expected given that the central bank had previously signalled that the hiking cycle was over, while the Committee agreed that the OCR will need to remain at a restrictive level for the foreseeable future and noted the level of interest rates is constraining spending and inflation pressure as anticipated and required. Furthermore, the RBNZ

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acknowledged inflation remains too high but is expected to decline within the target range by H2 2024. The rhetoric from the central bank has been very light since that meeting which only took place over 4 weeks ago, therefore, there hasn't been much to deviate from the current view of no more rate hikes and that the OCR will need to remain at a restrictive level for the foreseeable future. In addition, the data releases have been mixed and support the case for a pause with CPI firmer-than-expected for Q2 at 1.1% vs. Exp. 1.0% (Prev. 1.2%) and YY at 6.0% vs. Exp. 5.9% (Prev. 6.7%) but has slowed from the prior and labour cost index was also softer than estimated, while jobs growth topped forecasts at 1.0% vs. Exp. 0.5% (Prev. 0.8%) but the Unemployment Rate also rose to 3.6% vs. Exp. 3.5% (Prev. 3.4%).

NORGES BANK ANNOUNCEMENT (THU): Expected to stick with the implied guidance from the June MPR and hike by 25bp to 4.00%. A move that is justified by the Norges Bank's preferred inflation measure remaining elevated but printing roughly in-line with their forecast for July. Additionally, the NOK has seen marked appreciation since June, though is now off best, which should serve to push down inflation impulses in the months ahead. Nonetheless, markets continue to ascribe around a 20% chance to a 50bp hike. Note, the decision will be published as usual at 09:00BST but the accompanying press conference takes place as part of an event in Arendal which features questions from both the public and press. As a reminder, this is an interim meeting and as such we do not receive formal inflation or repo path forecasts, which in June implied around an 80% chance of another 25bp hike in September, assuming that magnitude is delivered in August.

REVIEWS

BANXICO REVIEW: The Central Bank of Mexico left rates unchanged as expected at 11.25% in a unanimous decision. The bank also maintained its guidance that "it considers that it will be necessary to maintain the reference rate at its current level for an extended period". Commentary on the economy saw it state activity has shown resilience and register higher-than-anticipated growth (prev. said it has shown resilience in a complex external environment), it maintained its view the labour market remains strong and that the balance of risks to growth is equilibrated. On inflation, it repeated that the balance of risks remains biased to the upside and that the inflationary outlook is still very complex, it also repeated the inflationary outlook will be complicated and uncertain throughout the entire forecast horizon, with upward risks. Banxico made some minor changes to its inflation forecasts. On the headline inflation, the Q3 23 forecast was revised down to 4.7% from 5.0%, but left unchanged throughout the rest of the forecast horizon to Q2 25. While for the core metrics, the Q3 23 forecast was left unchanged at 6.2%, but the Q4 23 to Q2 24 forecasts saw revisions higher by 0.1% for each quarter, to 5.1% in Q423, 4.2% in Q124 and 3.6% in Q224. However, it still sees both headline and core inflation returning more or less to target by the end of 2024. There was nothing in the statement to indicate rate cuts are coming, but analysts are expecting rate cuts in Q4 23, and Banxico officials (namely Heath) have also expressed that rate cuts could occur later this year if the economy unfolds as expected.

RBI REVIEW: As expected, the RBI held rates unchanged at 6.50% in a unanimous decision, making this the third pause in a row. The Bank also maintained its stance for remaining focused on the withdrawal of accommodation, which 5 out of 6 members voted for. Though in a hawkish move, Governor Das asked banks to hold an incremental cash reserve ratio (ICRR) of 10% on the increase in deposits between May 19 and July 28, which will withdraw nearly USD 12.07bln from the banking sector. The decision is temporary and will be reviewed on September 8th. Members gave little by way of additional new commentary, by noting the Indian economy is exuding enhanced strength and that it remains resolute in its commitment to align inflation to the 4% target. However, the Bank did revise its CPI inflation forecast higher to 5.4% (prev. 5.1%). The decision comes after the latest CPI data, which showed inflation edging higher in June to 4.81% vs. exp. 4.58% (prev. 4.25%), driven by a surge in food price inflation. Additionally, next week's inflation data for July is expected to see Indian CPI fly past the RBI's 2-6% target range to 8% YY, due to a surge in food inflation. Though ING attributes the recent surge to abnormal weather conditions and expects prices to normalise in the months ahead. In terms of the next decision, analysts at ING do not see the Bank hiking again, but do note that recent inflationary upticks may "make it harder for them to begin easing rates as soon as we had previously thought", and now forecast cuts to begin in 2024.

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