Central Bank Weekly 15th December: Previewing BoJ, PBoC, minutes from the BoC and RBA, CBRT; reviewing FOMC, ECB, BoE, Banxico, BCB, Norges Bank, SNB

PREVIEWS:

BOJ ANNOUNCEMENT (TUE): The BoJ is expected to maintain its policy settings at the December meeting, according to all respondents polled by Reuters between December 8th to 14th. BoJ expectations have been choppy over the past couple of weeks following commentary from Governor Ueda who, among other points, said “handling of monetary policy would get tougher from the end of the year”. These comments fuelled speculation of a potential December move by the BoJ, with the Yen rallying on the expectations. Thereafter, a Reuters source piece said there was no intention by Governor Ueda to signal "anything about the timing of a policy change". More recent sources clarified that the BoJ is said to see little need to end negative rates in December and intends to come to a decision based on data up to the last minute, and officials view the potential cost of waiting for more data as not very high. Sources added that the BoJ lacks proof of sustainable inflation and has not yet seen sufficient evidence of wage growth which would support sustainable inflation. The latest Tokyo CPI, which is seen as a precursor to the nationwide metric released on Thursday (after the BoJ meeting), saw the Core Y/Y miss expectations (2.3% vs exp. 2.4%, prev. 2.7%). Furthermore, following the December FOMC decision (which saw a dovish pivot), a Nikkei article citing a BoJ insider suggested Japan’s negative rate exit scenario has been muddled by the Fed’s outlook -"if possible, I'd look forward to wage increases that surpass this year's". The article added that from the standpoint of consistency, the BoJ would hold off until confirming the results of the spring labour talks, including those at small businesses, and that perspective makes an exit in the latter half of 2024 a convincing scenario as well. "The end of the negative interest rate policy would be the beginning of a tightening cycle," the BoJ insider said. The latest Reuters poll shows that 21% of economists think the BoJ will begin to unwind ultra-loose policy in January 2024, while 84% expect the BoJ will end NIRP in 2024 vs 71% in the November poll and 54% in the October poll. 88% of economists expect the BoJ to end YCC policy and 12% think the BoJ will tweak again. 28 out of 42 economists expect the BoJ to raise the deposit rate to 0% or 0.10% by end-Q2 2024, while two expect rates at 0.25%.

RBA MINUTES (TUE): The RBA will release the minutes from the December 5th meeting next week where the central bank kept the Cash Rate Target unchanged at 4.35%, as expected, and reiterated its forward guidance on whether further tightening is required to ensure inflation returns to the target in a reasonable timeframe will depend upon data and evolving assessment of risks. RBA also repeated that the Board remains resolute in its determination to return inflation to target and will do what is necessary to achieve that outcome, as well as noted there are still significant uncertainties around the outlook and that the limited information received on the domestic economy since the November meeting has been broadly in line with expectations. The language from the central bank was largely reiterations of the commentary from the prior meeting and therefore less hawkish than many were anticipating considering the rhetoric from RBA Governor Bullock in the weeks leading up to the meeting who was more forceful in her warnings that inflation remained a crucial challenge and had stated that more substantial monetary policy tightening is the right response. Nonetheless, participants will be eyeing the minutes on the off chance that there are more meaningful clues on monetary policy.

PBOC LPR (WED): The PBoC is expected to maintain the Loan Prime Rates next week with the 1-Year LPR currently at 3.45% and 5-Year LPR at 4.20%. As a reminder, rate-setters have refrained from making any adjustments to the benchmark lending rates since the last cut to the 1-Year LPR in August which most new loans are based on, while the 5-Year LPR which serves as a reference rate for mortgages was last reduced in June. The expectations for the PBoC to maintain the Loan Prime Rates follow the recent decision to keep the 1-Year MLF rate unchanged at 2.50% as this provides a fairly reliable indicator for the central bank’s intentions for the benchmark LPRs and although there has been speculation in Chinese press regarding scope for a RRR cut to meet liquidity needs at year-end, this has so far failed to materialise. Furthermore, recent comments from PBoC Governor Pan haven’t suggested any urgency for a near-term adjustment in which he noted that China's economy continued to gain momentum in recovery with the economy expected to achieve the GDP growth target for 2023 and they will continue to keep monetary policy accommodative, while the PBoC’s Q3 Monetary Policy Report stated that they will further promote financial institutions to lower the effective lending rate and that prudent monetary policy will be forceful and precise.

BOC MINUTES (WED): At its policy meeting, the BoC left rates unchanged at 5.00%, as expected, but tweaked its statement with both hawkish and dovish tones. On the dovish side, it noted signs that rate hikes were having an impact, stating that "higher interest rates are clearly restraining spending: consumption growth in the last two quarters was close to zero, and business investment has been volatile but essentially flat over the past year." It also referenced the Q3 GDP contraction, easing labour market, and that the economy was no longer in excess demand. The statement dropped a line that said progress toward price stability was slow, and inflationary risks have increased. On the hawkish side, however, it reiterated concerns about the risks to the outlook for inflation, and maintained guidance that it is prepared to raise the policy rate further if needed. Still, with price pressures abating and economic growth slowing, markets remain of the view that the central bank is done with rate hikes, particularly since BoC Governor Macklem's recent remarks that policy may now be restrictive enough. Attention now is turning towards the start of its easing cycle. Money markets are pricing a little over 100bps of easing in 2024, with the first cut fully priced by April. Macklem has said that it was not the time to be talking about rate cuts, and the BoC would likely be cautious over any rising inflation expectations if the consumer starts to expect rate cuts.

CBRT ANNOUCEMENT (THU): The CBRT is expected to raise its One-Week Repo Rate by 250bps according to all 12 economists polled by Reuters. CPI data for November printed sub forecasts but CPI Y/Y and PPI Y/Y both reaccelerated a touch, with the CPI Y/Y at 61.98% (exp. 63.00%, prev. 61.36%), M/M at 3.28% (exp. 3.90%, prev. 3.43%), and PPI Y/Y at 42.25% (prev. 39.39%). To recap the prior meeting, the CBRT hiked its Weekly Repo Rate by 500bps (vs median exp. 250bps hike) to 40% (prev. 35%, exp. 37.5%); expectations ranged from 250-500bps. The central bank stated that the pace of monetary tightening will slow down and the tightening cycle will be completed in a short period of time. The statement clarified that monetary tightness will be maintained as long as needed to ensure sustained price stability. The latest CBRT survey meanwhile suggested the Repo Rate is seen at 36.65% (prev. survey 37.01%), USD/TRY seen at 29.6229 (prev. 29.9961), and 12-month CPI seen at 41.23% (prev. 43.94%).

REVIEWS:

FOMC REVIEW: The announcement was dovish. The Fed left rates unchanged at 5.25-5.50%, as expected, and softened guidance, stating that in determining the extent of "any" additional policy tightening, it will take into account the cumulative tightening of monetary policy, lags, inflation dynamics, economic and financial developments (Chair Powell later said that the word "any" was added to show that the Fed thought it was at or near the peak for rates, though participants did not want to take the possibility of further hikes off the table). The Fed also acknowledged that inflation has eased, but remains elevated, and it maintained language that tighter financial and credit conditions for households and businesses were still likely to weigh on activity, hiring, and inflation. Within its forecasts, it lowered its 2024 rate projection to 4.6% (from 5.1%, exp. 4.9%), 2025 was lowered to 3.6% (from 3.9%, exp. 3.6%), 2026 was kept at 2.9% (exp. 2.9%), and the longer run view was kept at 2.5% (exp. 2.5%). Powell said that inflation had eased without a significant rise in unemployment, but reiterated that inflation was still too high, and the central bank is fully committed to returning inflation to 2%. Policy is well into restrictive territory, and its full effects were likely not yet felt, reiterating that policy will be kept restrictive until the Fed is confident on the path to 2% inflation. The Fed chair talked about how policymakers were still focused on the question of whether rates were high enough, and while it was unlikely to hike further, it did not want to exclude that possibility. Still, Powell said that the Fed was very focussed on not making the mistake of keeping rates too high for too long. Powell said the Fed discussed the timing of rate cuts at the meeting, and there was a general expectation that rate cuts will be a topic of conversation going forward, adding that the Fed will proceed carefully. Wells Fargo's economists said the doves won the day; "the door was left ajar for additional tightening, but the 'dot plot' signals that this was not the base case for most participants," and it adds that "after a period of nearly two years of rapid monetary policy tightening, a pivot to cuts next year seems like the most probable outcome." Money markets are now pricing six full 25bps rate cuts by the end of this year (before the meeting, four were fully priced, with a decent chance of a fifth). The first rate cut is fully priced for March (vs May prior to the Fed's announcement).

ECB REVIEW: As expected, the ECB opted to stand pat on rates for a second consecutive meeting with the main policy adjustment coming via the balance sheet. The Governing Council has decided that reinvestments under PEPP will run at current levels during H1 (vs. previous guidance of “at least until the end of 2024), after which, it intends to reduce the PEPP portfolio by EUR 7.5bln per month on average. Elsewhere, the statement reiterated that “policy rates will be set at sufficiently restrictive levels for as long as necessary”. However, the policy statement omitted the prior judgement “inflation is still expected to stay too high for too long”. The accompanying macro projections saw 2023 inflation downgraded to 5.4% from 5.6%, 2024 cut to 2.7% from 3.2% and 2025 held at 1.9%. Note, the forecasts drew criticism in some quarters given the November 23rd cut-off date, which has prompted suggestions that the 2024 core inflation projection of 2.7% is too high given recent economic developments. On the growth front, 2023 and 2024 projections were cut with GDP next year seen at just 0.8% with the 2025 forecast held steady at 1.5%. At the follow-up press conference, when questioned on the Bank’s plans for rate cuts next year, Lagarde stated the decisions will be data dependent, not time dependent, adding that policymakers will not let their guard down. Furthermore, Lagarde was clear in stating that the Governing Council did not discuss rate cuts this week with policy set for a “plateau of hold”. Lagarde also noted that the Bank will need to see more evidence on wage growth given that current data shows that wages are "not declining". When questioned on the balance sheet, the President noted that there were differing views on PEPP whereby some governors wanted different tapering, earlier or later. Overall, market pricing has moved in a hawkish direction with a March hike now seen at circa 60% vs. 80% pre-announcement and 147bps of cuts seen by the end of next year vs. circa 160bps. In wake of the meeting, Bloomberg sources suggested the ECB is largely united on forecasting rate cuts later than what markets are expecting. The sources also added that officials do not expect to revise their stance before March, when the ECB will receive an update on the outlook for growth and inflation.

BOE REVIEW: As expected, the MPC opted to stand pat on rates for a third consecutive meeting via a 6-3 vote with hawkish dissent once again from Greene, Haskel and Mann. The decision to stand pat on rates was based on the judgement that although "some of the news in key data had been to the downside since the MPC's previous decision, economic developments had been relatively limited overall". Overall, the key takeaway from the release, however, was the decision to maintain the phrase that policy will need to be restrictive for an "extended" period of time; some desks has touted an outside chance of a softening of this language. Furthermore, it remains the case that further tightening would be required if there were evidence of more persistent inflation pressures. Indeed, some of the language within the minutes leaned hawkishly by noting that "it was too early to conclude that services price inflation and pay growth were on a firmly downward path." That being said, the inflation path was somewhat lower than projected in November, reflecting softer energy prices. Elsewhere, the MPC judges that the November Fiscal Plan will boost GDP by 0.25% in the coming years. In response to the announcement, pricing has shifted hawkishly from 114bps of cuts priced across 2024 to 107bps, with the first cut pushed back to June from May beforehand, with a May cut priced at 80% implied probability and a March cut falling to less than 30% implied vs 40%. ING concludes that it expects wage growth and services inflation to fall to 4% next year, setting the BoE up for an August rate reduction.

BANXICO REVIEW: The Banxico left rates unchanged as expected at 11.25%, however, it was received hawkishly by giving away little signal on future rate cuts as it maintained guidance that rates need to stay at the current level for some time. It maintained its view that inflation risks are biased to the upside, and it raised several of its inflation forecasts, with the 2024 headline and core inflation being lifted, as was the Q4 core inflation view. The decision was unanimous. The statement also acknowledged that headline inflation increased slightly but core inflation continued to decrease and noted the disinflation process is expected to continue, but current forecasts incorporate a more gradual decline in both food merchandise inflation and services inflation. Banxico acknowledged that, for this reason, their forecasts for headline and core inflation have been revised upwards for some quarters. Nonetheless, Banxico is expected to start cutting rates, perhaps in Q1 2024, joining LatAm peers and also after the Dovish Fed twist on Wednesday. However, when Banxico officials have spoken on rate cuts, many have alluded to it being non-consecutive, and only gradual - the minutes on Jan 4th will be eyed for more clues on the timing of rate cuts.

BCB REVIEW: As was widely telegraphed, the BCB voted unanimously to cut the Selic rate by 50bps, taking it to 11.75%, marking the fourth cut since August. Guidance remains that we can expect similar sized cuts in the coming meetings. "The post-meeting statement was dovish, but with a cautious tilt, suggesting that markets should rule out, at least for now, more aggressive cuts," Pantheon Macroeconomics said "lingering domestic and external uncertainties — which 'require caution from emerging market economies' — are forcing policymakers to adopt a prudent approach, despite acknowledging falling inflation and improvements in the global economy." Pantheon still expects both external and domestic conditions to improve in Brazil, and it argues that that should allow policymakers to accelerate the pace of easing to 75bps, noting that the committee's makeup will become more dovish next year.

SNB REVIEW: Largely as expected from the SNB with the key rate maintained at 1.75% and the emphasis on selling foreign currency removed. Most pertinently, the inflation forecasts have seen relatively modest downward adjustments and while this does see CPI within the 0-2% band for 2024 as a whole, inflation is still seen rising in Q2/Q3-2024; though, this is now to just the top of the band, rather than September's guidance for it to eclipse it. Overall, the statement still holds the assessment that "uncertainty remains high" around inflation and as such has not guided us towards the direction of the next move, merely stating they remain ready to adjust policy as necessary. Given this, participants will remain focused on upcoming inflation prints for insight into the development of the rental rate of inflation. From the press conference, Chairman Jordan underscored the FX tweak and more pertinently said that December's discussion did not cover rate reductions and that further ahead the current forecasts do not see any tightening. In short, the SNB is barring a marked upward shock seemingly at the policy peak and the timing for a first rate-cut will likely be driven by the assessment/observation of inflation across Q2/Q3-2024, where it is forecast to rise to 2.0% once again.

NORGES REVIEW: Norges Bank defied consensus by triggering the hike that they flagged in November's meeting as "likely" to occur in December. However, consensus was for unchanged given the development of inflation and growth since then and the optionality at that meeting to leave rates unchanged if "the Committee becomes more assured that underlying inflation is on the decline". December's hike appears to have been spurred by the NOK (marked recent currency depreciation was the sole factor in favour of a hike in the run-up to the announcement). Interestingly, the repo path and statement do not rule out further tightening. With around a 20% chance of a 25bp move by Q2-2025 implied. However, given the recent pivot from the Fed and pronounced market pricing for global easing today's 4.50% rate is likely the peak. The subsequent press conference from Governor Bache added little.

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