Central Bank Weekly 19th January: Previewing PBoC, BoJ, BoC, ECB; Reviewing ECB Minutes

PREVIEWS:

PBOC LPR (MON): The PBoC decided to keep its 1-year MLF rate unchanged at 2.50% which was somewhat of a disappointment as a slim majority of forecasters had called for a cut although the size of funds provided under the facility was larger than estimated at CNY 995bln (exp. CNY 900bln), while the central bank also announced a couple of notably large injections through its daily open market operations in the following days after, which suggests a current preference to ensure ample liquidity rather than reduce the cost of funding. As such, the PBoC is expected to maintain its benchmark 1-year and 5-year Loan Prime Rates on Monday at their current levels of 3.45% and 4.20%, respectively, as the 1-year MLF rate serves as a fairly reliable leading indicator of the central bank's intentions for the benchmark LPR which most new loans are based on, while a recent Reuters poll showed 26 out of 27 market watchers surveyed predict no changes to the LPRs. The latest data releases from China also support the case for the central bank to remain patient after the GDP and activity data printed mixed but showed China's economy grew by 5.2% in 2023 to reach the government's official target of around 5%. Nonetheless, Chinese media still think the PBoC could cut rates and RRR during Q1 given the uneven recovery in the Chinese economy, although it is also worth noting that there was widespread speculation of a potential RRR cut during Q4 last which failed to materialise.

BOJ ANNOUNCEMENT (TUE): The BoJ is expected to maintain its policy settings of negative rates at -0.10% and QQE with YCC to flexibly target 10yr JGB yields at around 0% with a 1% upper bound reference rate for market operations, while the central bank will also release its latest Outlook Report containing board members' median forecasts for real GDP and core CPI. As a reminder, the BoJ disappointed outside bets that it could make some sort of policy tweak at the last meeting in December and instead opted to keep policy settings unchanged, as well as reiterated its dovish forward guidance and pledge that it will not hesitate to take additional easing measures if necessary. The upcoming meeting is also unlikely to involve any policy tweaks but participants will be eyeing the central bank's statement for clues regarding future policy and if there are any adjustments to members' projections in the Outlook Report as the BoJ was reportedly considering lowering its price outlook for FY24 to the mid-2% range, although sources have stated that the BoJ is expected to broadly maintain its projections that trend inflation will stay near its 2% target in the coming years and although it is seen cutting its FY24 core inflation forecast, the central bank is likely to make no major changes to its forecast that "core core" inflation will hit 1.9% in both FY24 and FY25. Furthermore, expectations for a rate cut this year by key global central banks such as the Fed and ECB effectively lessens pressure for the BoJ to normalise policy although it is still expected to exit the world's last negative rate policy with most economists forecasting April as the most likely month for the central bank to scrap NIRP.

BOC ANNOUNCEMENT (WED): The BoC is unlikely to move rates from the current 5.00% level at its confab in January. The BoC's latest Business Outlook Survey revealed that Canadian businesses see sales slowing as high interest rates place obstacles to consumer spending, but businesses expect inflation to ease ahead, helping the business outlook indicator to pare back a little to -3.15 from -3.45. "Firms pricing behaviour is slowly returning to normal," the BoC said, "still, wage growth on average is expected to be higher than normal over the next 12 months, often related to cost-of-living adjustments." Money markets are pricing the first BoC rate cuts in H1 of this year. Analysts at Capital Economics expect the BoC to maintain a hawkish tone at the January meeting after CPI-trim and CPI-median core inflation gauges ticked-up in December; "but those measures are arguably overstating inflation pressures," CapEco writes, and "with the economy looking weak, we continue to think that the first rate cut is coming sooner rather than later, albeit in April rather than March as we previously forecast."

CBRT ANNOUNCEMENT (THU): There is no median consensus among analysts at the time of writing, but some desks expect a 250bps hike to the Weekly Repo Rate to push it to 45%, citing the communication given in December implying a move upward in January before ending the hiking cycle. At the prior meeting, the CBRT hiked its rate by 250bps to 42.5% as expected and noted that "The Committee anticipates to complete the tightening cycle as soon as possible. The monetary tightness will be maintained as long as needed to ensure sustained price stability." Analysts at ING share the view that January could be the last CBRT hike – "We expect inflation to remain elevated until mid-2024, with further increases above 70% on seasonal effects in January and unfavourable base effects in May. The second half of next year, on the other hand, will likely see a sharp downtrend – reflecting this year's high base and the further impact of tighter policy, pulling inflation down to 40-45% at year-end. In this environment, following one more hike in January, we expect the CBT to remain on hold until the third quarter of next year", says the bank.

NORGES ANNOUCEMENT (THU): There are currently no analyst polls for Norges Bank's confab next week, but the central bank's communication, transparency, and recent data indicate a hold on current rates. To recap the prior meeting, Norges Bank defied consensus by triggering the hike to its Key Policy Rate to 4.50% from 4.25% (exp. a hold at 4.25%) but the forecast indicated that the policy rate will lie around 4.5% until autumn 2024 before gradually moving down. 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, whilst the statement flagged a data-dependent approach and noted that "If cost inflation remains elevated or the krone turns out to be weaker than projected, price inflation may remain higher for longer than currently projected. In that case, the Committee is prepared to raise the policy rate again", but also noted, "If there is a more pronounced slowdown in the Norwegian economy or inflation declines more rapidly, the policy rate may be lowered earlier than currently envisaged." In terms of recent data, Core Y/Y for December printed at 5.5% (exp. 5.6%, prev. 5.8%) whilst headline Y/Y printed at 4.8%, matching the expectations and prior. The core Y/Y figure cooling from the prior by more than expected likely confirms that the Norges Bank's tightening cycle has concluded. But the fact that inflation remains markedly above the 2.0% target, even for the headline rate which printed at 4.8% Y/Y, means it is far too soon for rate-setters to begin discussing easing. Analysts at Rabobank suggest that the headline print also means policymakers are likely to maintain a hawkish tone at the upcoming meeting. "Currently the market is priced for rates around 35 bps lower on a 6-month view. We see this as overdone and look for the NOK to find some support as the market adjusts to a more cautious Norges Bank. We expect EUR/NOK to edge lower to 11.20 on a 3-month view", says Rabobank.

ECB ANNOUNCEMENT (THU): Expectations are for the ECB to stand pat on all three of its key rates after having held the deposit rate at its current peak of 4% since October. In terms of recent economic developments, headline EZ HICP rose to 2.9% in December (vs. prev. 2.4%) amid unfavourable energy base effects from Germany. Note, the uptick is set to be a temporary one and therefore the disinflationary process is still judged to remain in place. Core inflation has continued to decline with December showing a downtick for the super-core metric to 3.4% from 3.6%. On the growth front, the prelim Q4 EZ release is not due until 30th January. However, the FY 2023 GDP release from Germany noted a prelim 0.3% Q/Q contraction for the Eurozone's largest economy. Survey data saw the December EZ-wide composite PMI hold steady at 47.6, services tick higher to 48.8 from 48.7 and manufacturing nudged up to 44.4 from 44.2. Despite the slowing trend for inflation and subdued growth, January is seen as too soon for the ECB to commence its rate cutting cycle with policymakers attempting to dampen market expectations for an aggressive path of reductions. On which, President Lagarde has noted that too optimistic markets do not help the ECB in its inflation fight. Adding that, it is likely that the ECB will cut rates by the summer. Elsewhere, Chief Economist Lane has suggested the ECB will have key data by June to decide on rates and that changing rates too fast can be harmful. Looking beyond the current meeting, the recent dovish repricing has seen markets assign a circa 85% chance of a cut in April with a total of 135bps of cuts seen by year-end vs. circa 160bps in the aftermath of the ECB's December meeting. Surveyed economists are slightly more hawkish-leaning with the median looking for a rate cut in June and a total of 100bps of cuts this year.

REVIEWS:

ECB MINUTES REVIEW: The account of the ECB's December meeting in which it opted to stand pat on rates and bring forward the reduction of reinvestments under PEPP passed without much fanfare as the contents revealed little in the way of new information. In terms of the highlights, the decision to stand pat on rates was based on the judgement that "headline inflation was set to return to target only by the second half of 2025". More specifically on the inflation outlook, caution was warranted as inflation would probably pick up in the near term. Furthermore, it was too early to be confident that the task had been accomplished. For the accompanying macro projections, it was noted that given the cut-off date for the forecasts, the outlook for economic activity in the staff projections seemed too optimistic and the strength of disinflation was likely to be underestimated. On the balance sheet (as alluded to by President Lagarde in the press conference), some members favoured an earlier end to full reinvestments than had been proposed, suggesting that tapering could start earlier and be more gradual, other members argued that full reinvestments should continue until the end of 2024. Overall, the accounts provide little useful in terms of signalling with markets more focused on economic data and ECB rhetoric. On the latter, President Lagarde has cautioned markets ahead of next week's meeting that too optimistic markets do not help the ECB in its inflation fight. In terms of the timing of the ECB's first rate cut, the President stated that it is likely that the ECB will cut rates by the summer.