Central Bank Weekly 26th January: Previewing FOMC, BoE, Riksbank; Reviewing PBoC, BoJ, BoC, Norges and ECB

PREVIEWS:

FOMC ANNOUNCEMENT (WED): The FOMC is set to keep rates unchanged at 5.25-5.50% at its January meeting, according to all economists surveyed by Reuters. The central bank is expected to begin cutting rates in Q2 in response to cooling inflation, according to 86 of 123 surveyed (55 thought June was more likely, while 31 see a reduction in May). Additionally, the Reuters poll reveals that most economists (72 of the 123) believe the Fed will cut rates by 100bps or fewer this year - that compares to money market pricing, which currently sees five 25bps rate cuts fully priced, with a good chance of a sixth; the Fed's own forecasts see three 25bps rate cuts this year. "We still expect the Committee to maintain a cautious stance in the near-term even amid an increasingly improving profile for consumer prices, as the Fed would like to ascertain that the recent progress in inflation is sustainable," TD Securities said.

BCB ANNOUNCEMENT (WED): The BCB is expected to fire its fifth rate cut of the current easing cycle, reducing rates by 50bps to 11.25%. Analysts continue to see further rate reductions this year, with the weekly central bank poll of private economists seeing the Selic falling to 9.00% this year, before easing a little further to 8.50% in 2025. However, Capital Economics suggests that "with inflation set to remain above target, fiscal risks likely to flare up again and the labour market only loosening gradually, we think interest rates will be lowered more cautiously than most currently expect (it sees the end-2024 Selic rate at 9.50%)."

RIKSBANK PREVIEW (THU): Expected to leave rates unchanged at 4.00% given November’s guidance for rates to remain at this level for 2024 and 2025. A decision which is justified by inflation continuing to moderate alongside ongoing signs of a domestic slowdown; though, Services PMI for December lifted back to the 50.0 mark. Given the inflation prints, it is possible the Riksbank revises its guidance for no 2024 cut, though such an announcement may be judged premature at this meeting. While rates are expected unchanged, the Riksbank may elect to announce an increase to the pace of sales of government bonds as flagged at the last gathering. As a reminder, in November the Riksbank left its rate at 4.00% defying expectations for a hike and stated that they are prepared to raise the policy rate further if inflation prospects deteriorate. Additionally, on purchases, said they are considering increasing the pace of sales of gov’t bonds (currently SEK 5bln/month) potentially in January. An announcement which was regarded as a neutral hold overall. Within the minutes, the most pertinent element was Breman switching focus to inflation/activity from the weak SEK.

BOE ANNOUNCEMENT (THU): Analysts surveyed are unanimous in their view that the MPC will once again stand pat on rates, leaving the Bank Rate at 5.25%. The vote will likely be unanimous, with the three December dissenters (Greene, Haskell, Mann) likely to move to the “unchanged” camp after being wrongfooted by the November inflation report, which saw the all-important services print decline to 6.3% Y/Y from 6.6% – in stark contrast to the MPC’s projection of 6.9%. Since the prior meeting, the annualised rate of headline inflation unexpectedly advanced to 4.0% Y/Y from 3.9%, while the services print ticked higher to 6.4% Y/Y from 6.3%. However, expectations for the broader disinflationary trend to continue remain in place; ING bank is of the view that inflation will dip below 2% in April and sit around the 1.5% area in May/June. Elsewhere, GDP in November expanded 0.3% M/M (vs the 0.36% contraction the prior month). Survey data remains strong with the January composite PMI rising to 52.5 from 52.1 with the services print at 53.8 vs. prev. 53.4. In the labour market, the unemployment rate (subject to data quality concerns) holding steady at 4.2%, while headline earnings growth in the 3m/YY period to November fell to 6.5% from 7.2%. Softness has been observed in the consumer too, with monthly retail sales -3.2% in December (vs prev. 1.4%). Incremental commentary from the MPC has been minimal, cementing expectations of a hold in policy. Beyond the upcoming meeting, markets assign an approximately 80% chance of a June rate cut, with a total of 92bps of easing seen by year-end. Thirty-eight of the 70 economists surveyed by Reuters expect the first cut to come in Q2, with all but four seeing at least one cut before September. For the accompanying MPR, Oxford Economics expects that the MPC will “bring forward the timing of when it expects inflation to return to the 2% target to Q2 2024 from end-2025.” On growth, the consultancy says “the BoE will likely take a less downbeat view of the economy's prospects compared to November, when it forecast that GDP would flatline this year and grow only 0.25% in 2025.”

REVIEWS:

PBOC LPR REVIEW: The PBoC maintained its Loan Prime Rates, as widely expected, with the 1-year LPR kept at 3.45% which is the rate most new loans are based on, while the 5-year LPR was kept at 4.20% which is the reference for mortgages. The decision to maintain the benchmark lending rates was unsurprising given the central bank's announcement to keep its 1-year MLF rate unchanged at 2.50% the week before despite expectations by a slim majority of forecasters for a cut to the 1-Year MLF rate, as this serves as a fairly reliable leading indicator of the central bank's intentions for the benchmark LPRs. Nonetheless, there are expectations of a potential reduction of the LPRs in the near future especially given after the slew of recent support pledges and measures by Chinese authorities including a 50bps RRR by the PBoC announced on Wednesday which will take effect from February 5th and would release CNY 1tln into the economy.

BOJ REVIEW: The BoJ kept its policy settings unchanged, as expected, with rates at -0.10% and QQE with YCC to flexibly target 10yr JGB yields at around 0%, while it maintained the 1% upper bound reference rate for market operations. The BoJ also stuck to its forward guidance as it reiterated that it will continue with QQE with YCC for as long as needed and won't hesitate to take additional easing steps if needed, as well as noted that inflation expectations are gradually heightening and that inflation will likely gradually accelerate towards the BoJ's target through to the end of the projected period. Furthermore, the BoJ released its latest Outlook Report in which it cut the Fiscal 2023 Real GDP median forecast to 1.8% from 2.0% but raised the Fiscal 2024 Real GDP median view to 1.2% from 1.0%, and it cut its Fiscal 2024 Core CPI median forecast to 2.4% from 2.8% but raised the Fiscal 2025 Core CPI median view to 1.8% from 1.7%. The announcement provided very little to spur price action so the focus then turned to BoJ Governor Ueda's press conference where he stated that the likelihood of achieving 2% inflation is rising gradually and that even if real wages are negative and the outlook is positive, a policy change is possible. Ueda also said they will certainly foresee further rate hikes when exiting negative interest rate policy but noted that accommodative conditions will continue for a while and they will have more data at the April policy meeting compared to March. The comments from Ueda were more hawkish-leaning than usual and therefore triggered a repricing in Japanese asset classes, while the Summary of Opinions from the meeting is scheduled for release next Wednesday which participants will be eyeing to see if this more hawkish tone by Ueda was widespread among the board.

BOC REVIEW: The overall tone was dovish; the boC left rates unchanged at 5.00%, as expected, but it removed statement language that stated that it was prepared to raise rates further if needed. Still, Governor Macklem suggested that the BoC has not ruled out further policy rate hikes, arguing that if new developments push inflation higher, the central bank could still lift rates, although added that this was not its base case. Macklem also noted that if the economy evolves broadly in line with projections, future discussions will be about how long the BoC maintains rates at current levels. Within its updated MPR, the BoC lowered its 2024 inflation forecast to 2.8% from 3.0% in October, while the 2025 forecast was unchanged at 2.2%; the forecasts see inflation returning back to the 2% target in 2025 (the October MPR saw this happening at the end of 2025). Growth forecasts were cut across 2023-2025, while the estimates of the neutral range were unchanged at 2-3%, but it lowered the output gap estimate to -0.25% and -1.25% from -0.75% and 0.25%. Analysts said that the statement language changes and the Governor's remarks open the door to rate cuts this year, though Macklem did not want to commit to any specific dates of when easing might occur (analysts and markets look for either April or June for the first cut). The statement, speech and MPR all made clear however that the central bank remains concerned about upside risks to inflation, and pointed to how shelter services price inflation was still high, and is expected to put upwards pressure on inflation for some time. The Governor and Senior Deputy Governor were quizzed on QT during the Q&A, but said the BoC will take things one decision at a time, and it was not there yet on ending QT. Looking ahead, money markets are assigning a near 50% probability of a rate cut in April with the first 25bp cut priced in by June - this is in fitting with analyst expectations pre-BoC.

CBRT REVIEW: The CBRT opted to end its tightening cycle with a 250bps hike as expected, taking the Weekly Repo Rate to 45.00%. The release suggested that the Committee "assesses that the current level of the policy rate will be maintained until there is a significant decline in the underlying trend of monthly inflation…" Furthermore, the CBRT said it will reassess the stance of policy if notable and persistent risks to the inflation outlook emerge. The Committee reiterated its data-dependent stance. All-in-all the release offered little in the way of fireworks and matched expectations of all 25 analysts polled by Reuters who were looking for a 250bps hike, with expectations heading into the meeting more uniform than usual.

NORGES REVIEW: Overall, as expected from the Norges Bank in terms of the policy announcement and guidance for rates to be maintained for some time ahead. Though, the language and framing of the economy does have a hawkish element and thus sparked some modest NOK strength. Specifically, the statement retained the optionality to hike again if necessary (caveated by the optionality to cut earlier than envisaged), highlighted that while underlying inflation has declined further it is still high (known, but the explicit mention is hawkish) and that the overall prospects for the economy do not appear to have materially changed since December (again, not necessarily surprising but still hawkish). Finally, the guidance for rates is now "the policy rate will likely be kept at that level for some time ahead" which compares to the autumn 2024 implied by the repo forecasts. It is difficult to directly compare January's language with December's forecasts and the implied timing they provide; but, the verbal guidance can possibly be interpreted as a touch more hawkish.

ECB REVIEW: As was widely expected, the ECB opted to stand pat on all three of its key rates. The initial policy statement passed with little in the way of fanfare with the Governing Council stating that the declining trend in underlying inflation has continued and that past interest rate increases keep being transmitted forcefully into financing conditions. Furthermore, “Incoming information has broadly confirmed its previous assessment of the medium-term inflation outlook”. At the subsequent press conference, President Lagarde noted that it is “premature” to talk about rate cuts, adding that the ECB will be data-dependent and not fixated on the calendar. With regards to events in the Red Sea, the President noted that the Bank is being careful given that shipping costs have increased and deliveries have been delayed. On wages, which have been a key source of focus when it comes to the timing of the first rate cut, Lagarde suggested that data is 'directionally good' and the Bank is not seeing second-round effects. However, this was followed up by the judgement that the ECB needs to be further along the disinflation process before it can be confident that inflation is moving back towards target sustainably. Overall, the lack of explicit pushback from the President on current market pricing and positive commentary on wages has allowed market pricing to drift in a more dovish direction with an April cut priced at around 84% vs. circa 68% pre-announcement with a total of 134bps of easing priced by year-end vs. 123bps pre-announcement. In wake of the meeting, Reuters sources reported that ECB policymakers are open to start discussing future rate cuts in March if data points to inflation hitting 2% this year, adding a March pivot would pave the way for a rate cut most likely in June, despite markets pricing in over an 80% probability of a rate cut in April.

SARB REVIEW: South African Central Bank, as expected, held its repo rate at 8.25% in a unanimous decision. In the accompanying forecasts, CPI and Core CPI were left unchanged for 2024 at 5.0% and 4.6%, respectively, with 2025 slightly raised to 4.6% (prev. 4.5%) for both metrics. GDP forecasts remained the same, with 2024 seen at 1.2% and 2025 at 1.3%. SARB said that the risks to the medium-term domestic growth outlook are assessed to be balanced, and the return to target in headline inflation has been slow. SARB further added the baseline inflation forecast is of continued gradual moderation and risks are assessed to the upside. Moreover, the Central Bank wants inflation around its 4.5% mid-point before considering cuts, and Governor Kganyaho said as long as there isn't any sustained decline of inflation towards our target, don't expect us to change policy.