Central Bank Weekly 23rd February: Previewing RBNZ policy announcement; Reviewing PBoC and minutes from FOMC, ECB and RBA

PREVIEWS:

RBNZ ANNOUNCEMENT (WED): The RBNZ will likely keep the Official Cash Rate unchanged at the current level of 5.50% with money markets pricing around a 70% chance for no change in rates and about a 30% probability for a 25bps hike, while a Reuters survey showed 27 out of 28 economists forecast rates to maintained at the current level and just one called for a 25bps hike. Nonetheless, a rate increase cannot be ruled out with the meeting seen as potentially live after the central bank's hawkish signal at the last meeting and ANZ Bank also recently forecasted the RBNZ to deliver back-to-back hikes through to April to lift the OCR to 6.00%. As a reminder, the RBNZ kept rates unchanged as unanimously forecast during the last meeting in November although its language was hawkish as it stated that inflation remains too high and the committee remains wary of ongoing inflationary pressures, as well as noted that if inflationary pressures were to be stronger than anticipated, the OCR would likely need to increase further. In addition, the central bank's OCR projections were lifted to suggest risks of a further hike with the OCR view for March 2024 raised to 5.63% from 5.58% and the view for December 2024 lifted to 5.66% from 5.50%, while it also raised the March 2025 OCR forecast to 5.56% from 5.36%. Furthermore, Governor Orr stated that risk to inflation is still more to the upside and they did discuss raising rates at that meeting but also stated they've been adamant on holding rates and that their projection shows an upward bias to rates but it is not a done deal. The central bank's rhetoric since then has continued to toe the hawkish line with Governor Orr noting that interest rates are restricting spending and that levels of core inflation remain too high, while he also stated a flexible approach to inflation targeting with a medium-term focus remains appropriate and that bringing levels of core inflation back in line with the bank's 1-3% target is an important part of bringing inflation back to the 2% midpoint. Other officials have also provided a similar tone which is hawkish but doesn't suggest an urgency to act as Chief Economist Conway noted recent economic data suggests monetary policy is working with the economy slowing and inflation easing, but they still have a way to go to get inflation back to the target midpoint of 2%, while Deputy Governor Hawkesby commented that New Zealand's financial system remains strong and that the system can cope with high interest rates. The key data releases from New Zealand support the argument for a pause as GDP in Q3 showed a surprise contraction Q/Q at -0.3% (exp. 0.2%) and Y/Y at -0.6% (exp. 0.5%), while CPI in Q4 slowed as expected to 4.7% from 5.6% and the latest inflation forecasts were also reduced with 1-year and 2-year inflation expectations cut to 3.22% and 2.50% from 3.60% and 2.76%, respectively. This would suggest less pressure for the central bank to resume its tightening cycle although chances of a hike cannot be dismissed given that inflation remains above the RBNZ's 1%-3% medium-term target and the latest Labour Cost Index data was also firmer than expected.

REVIEWS:

FOMC MINUTES REVIEW: The minutes were in fitting with recent FOMC commentary, confirming that most policymakers were cognizant of the risks of easing too quickly, though a couple pointed to downside risks from maintaining an overly restrictive stance for too long. Officials also highlighted the uncertainty around how long a restrictive policy stance would be needed. Officials judged that the policy rate was likely at its peak for this cycle, and several emphasised the importance of communicating clearly about its data-dependent approach. On inflation, the minutes noted that while risks to achieving dual-mandate goals were in better balance, officials are 'highly attentive' to inflation risks. Policymakers do not want to lower the funds rate until gaining 'greater confidence' in inflation moving sustainably toward 2%. Some officials also cautioned that progress on inflation could stall. On the balance sheet, the minutes stated that reductions in the overnight RRP usage meant it might soon be appropriate to begin in depth discussions on balance sheet at the next meeting. Elsewhere, staff economic outlook was slightly stronger than December, and staff have placed "some weight" on the chance that further progress on lowering inflation could take longer than expected. Staff also characterized the US Financial system vulnerabilities as notable, adding that risks to the economic forecast were skewed to the downside. In wake of the release, Goldman Sachs pushed back its view on rate cuts, and now sees the central bank starting to lower rates in June (vs its previous call for a May rate reduction). GS now sees four rate cuts this year (it previously projected five - note: the Fed forecasts have pencilled in three cuts in 2024).

ECB MINUTES REVIEW: Given that the meeting itself passed with little in the way of fanfare, the account of the meeting was never going to produce much in the way of fireworks. In terms of the key takeaways, the latest developments in economic activity and inflation were seen as being consistent with the current monetary policy stance.

More specifically, there had been further progress on all three elements of the reaction function, which gave grounds to be confident that monetary policy was working. That being said, It was affirmed that further progress needed to be made in the disinflationary process before the Governing Council could be sufficiently confident that inflation was set to hit the ECB’s target in a timely manner and in a sustainable way. Accordingly, members signalled that continuity, caution and patience were still needed, since the disinflationary process remained fragile and letting up too early could undo some of the progress made. More specifically when it came to the prospect of lowering rates, the risk of cutting policy rates too early was still seen as outweighing that of cutting rates too late. Overall, the account provided little in the way of fresh insight with the Governing Council in "wait-and-see" mode as policymakers await further progress in their battle against inflation.

PBOC REVIEW: The PBoC surprisingly maintained its 1yr LPR at 3.45% (expectations were for a 5bps reduction), but the 5yr LPR was cut by 25bps to 3.95% (a larger cut than the expected 10bps reduction), with the latter the rate being the reference for mortgages in China. Analysts framed the move as further support the property sector, a signal of targeted easing, and a dovish policy stance. That said, analysts question the central bank’s willingness to extend mortgages at lower, less profitable rates with potential pressure on net interest margins. Analysts at Oxford Economics suggested that the root of China's property sector issues lies beyond just mortgage affordability, pointing to a broader range of economic and structural challenges. The desk underscores the importance of viewing this rate cut within a larger context of measures aimed at managing a property market correction. OxEco sees the move as a response to the incremental policy easing's limited impact, indicating a deeper concern among Beijing policymakers about the property market's challenges. ING notes the potential pressure on Chinese banks' net interest margins, given the already low levels prior to this policy action, and suggests that while the cut aims to support the property market, it could exacerbate financial challenges for banks. ING anticipates continued accommodative monetary policy in China, with room for further easing, including additional cuts to the LPR and the reserve ratio requirement, especially if global central banks shift toward rate cuts.

RBA MINUTES REVIEW: RBA Minutes from the February 6th Meeting revealed that the board considered the case to hike by 25bps or hold steady in which the case to hold steady was the stronger one and appropriate given balanced risks to the outlook. The minutes also stated the data gave the board more confidence inflation would return to target in a reasonable timeframe although it would "take some time" before the board could be confident enough about inflation and the board agreed it was appropriate not to rule out another rise in rates. Furthermore, it noted that hiking rates would not prevent it from cutting should the economy weaken but also stated that forecasts of inflation to be back at the target in 2025 assumed no further rate hikes. The language from the central bank remained hawkish with the option of a hike clearly on the table although it didn’t suggest an urgency to act as the central bank also acknowledged that data on the labour market and consumption had been weaker than expected and that high inflation, higher tax and interest payments had weighed on consumption.

CBRT REVIEW: The CBRT maintained its Weekly Repo rate at 45%, as expected, and reiterated its forward guidance that the “current level of the policy rate will be maintained until there is a significant and sustained decline in the underlying trend of monthly inflation.” This was the first meeting under new governor Fatih Karaham, though the statement was largely a copy and paste (with some minor tweaks), and signalled continuity in policy after the departure of Hafize Gaye Erkan. The central bank reiterated that its “monetary policy stance will be tightened in case a significant and persistent deterioration in inflation outlook is anticipated.” The statement also said, “The determination in tight monetary stance will continue to contribute to Turkish lira’s real appreciation process, which is a key element of disinflation.” Analysts at ING, on the decision, said “After reaching the terminal rate of 45%, the bank repeated its pledge to maintain a tight monetary policy stance for longer, and kept the door open to further rate hikes, while it has strengthened its messages with some slight changes in the rate-setting statement. At this stage, we continue to expect a first cut in the last quarter of this year and the policy rate to reach 40% at end-2024 with a risk of delay into early next year.”

BOK REVIEW: BoK maintained its base rate at 3.5%, as expected, with the decision made unanimously and it will maintain a restrictive policy stance for a sufficiently long period. BoK said it will monitor the inflation slowdown, financial stability and economic growth risks, household debt growth, monetary policy operations in major countries and developments in geopolitical risks. BoK also stated that consumption and construction investment are to recover at a slower pace, as well as noted that uncertainties to the growth outlook are high. Furthermore, the central bank signalled an unlikelihood for any near-term policy adjustment as Governor Rhee said five board members said the current interest rate should be maintained at least for the next three months and just one board member said the door for a rate cut should be opened for the next three months, while Rhee added that he still doesn't see much chances of a rate cut in H1 and that most members' view it is too early to discuss rate cuts.

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