Central Bank Weekly 5th April: Previewing FOMC minutes, ECB, BoC, RBNZ, BoK; Reviewing RBI, minutes from ECB and RBA

PREVIEWS:

FOMC MINUTES (WED): The Fed held rates at 5.25-5.50% in March, as was widely expected. Its updated economic projections continue to see three rate cuts this year, though it sees fewer rate reductions in 2025 and 2026 than it was forecasting in December. It also raised its view of the neutral rate higher (to 2.6% from 2.5%). On the inflation front, it revised its view for core PCE higher this year, despite seeing fewer rate cuts, and continues to see inflation back at target in 2026. "Our interpretation is that Chair Powell and a narrow majority of the Committee feel strongly about not delaying cuts for too long, and are targeting the June FOMC meeting for the first cut," Goldman Sachs said, "in fact, the somewhat higher inflation forecast lowers the bar slightly for incoming inflation data to meet the FOMC's expectations and keep a June cut on track." Regarding the neutral rate, GS argues that with the median longer-run dot revised upwards, and the median 2026 dot rising by 25bps to 3.125%, the FOMC will likely raise its estimates of both the long-run and short-run neutral rates over time, and that the terminal rate will be meaningfully higher than last cycle. At his post meeting press conference, Fed Chair Powell did not show too much concern regarding the hotter-than-expected January and February inflation readings, noting that the data did not provide the Committee with any incremental confidence that inflation was falling sustainably back towards target, and added that the road to inflation falling to 2% would be bumpy. Powell did not show any concerns about the economy, noting the solid labour market and growth conditions. The FOMC's 2024 growth view was raised (to 2.1% from 1.4% - and above the longer-run growth view of 1.8%), but Powell said that the better growth dynamic was made possible after the recent growth in labour supply, and the resilient employment environment was not an argument against rate cuts. Meanwhile, there were no adjustments to the Fed's balance sheet runoff plans, but Powell said policymakers think it will be appropriate to slow the pace of tapering "fairly soon. Since the meeting, Fed Chair Powell has spoken on a couple of occasions; speaking in wake of the February PCE data, Powell said the report was in line with his expectations, and that was something he wanted to see more of. He added that in order to gain confidence on inflation, the Fed wants to see more good readings, as seen over the last year. He warned that risks are two-sided, where reducing rates too soon could be disruptive, while reducing rates too slowly might mean unneeded damage to the economy and the labour market, though added that the Fed does not need to be in a hurry to cut rates.

BOC ANNOUNCEMENT (WED): Analysts expect the Bank of Canada to begin the rate cutting cycle in June, and therefore, rates are expected to remain unchanged at 5.00% at the April policy meeting. Minutes from the March meeting suggested that the BoC was on the fence regarding the timing of rate cuts; policymakers think it is still too early to cut rates, but if the economy evolves in line with its expectations, then rate cuts may be seen sometime this year; that said, the minutes noted a "diversity of views" among officials about when there would sufficient evidence to start the cutting cycle. Ahead of the March meeting, analysts were of the view that there were greater risks that the first rate cut would come later than forecast rather than sooner than forecast. The Q1 business outlook survey revealed that 27% of firms surveyed expect Canada to be in a recession this year (down from 38% in Q4), and 40% of firms expect inflation to be above 3% for the next two years (down from 54% in Q4).

RBNZ ANNOUNCEMENT (WED): RBNZ is expected to keep the OCR unchanged at 5.50% with money market rates pricing around a 95% probability for the OCR to be maintained at the current level and less than a 5% chance of a 25bps cut, while a recent Reuters poll showed economists were unanimous in their forecasts for no change in rates. As a reminder, the central bank kept its rates unchanged at the last meeting in February and stated the OCR needs to remain at a restrictive level for a sustained period and that the committee remains confident that the current level of the OCR is restricting demand. RBNZ noted core inflation and other measures of inflation expectations have declined and that risks to the inflation outlook have become more balanced but added that headline inflation remains above the 1%-3% target band, limiting the committee's ability to tolerate upside inflation surprises. However, the key takeaway from that meeting proved to be the projections for the OCR which were dovish as the central bank reduced its OCR forecast with the June 2024 view lowered to 5.59% from 5.67% and the March 2025 view lowered to 5.47% from 5.56% suggesting the unlikelihood of a hike. Furthermore, the minutes from the meeting noted that ongoing restrictive monetary policy settings are necessary to guard against the risk of a rise in inflation expectations and the committee agreed interest rates need to remain at a restrictive level for a sustained period of time. The rhetoric from the central bank since then continues to suggest a lack of urgency for the central bank to tweak policy in the near-term as RBNZ Governor Orr stated the economy is evolving as anticipated and inflation is still too high but is declining, while he added policy needs to stay restrictive for some time and expects to begin normalising policy next year. Data also supports the case for no adjustments as above-target inflation narrows the scope for near-term loosening, while further tightening is also seen as unlikely especially as recent GDP data showed a surprise contraction in New Zealand's economy which entered into a technical recession during Q4 with GDP Q/Q at -0.1% vs. Exp. 0.1% (Prev. -0.3%) and Y/Y at -0.3% vs. Exp. 0.1% (Prev. -0.6%).

ECB ANNOUNCEMENT (THU): Analysts are unanimous in expecting the ECB to stand pat on the deposit rate at 4.0% with markets assigning a circa 89% likelihood of such an outcome. Since the prior meeting, headline inflation in March has pulled back to 2.4% from 2.6% with the super-core metric now below 3% for the first time in two years. That being said, services inflation remains uncomfortably high at 4%. With Q1 GDP not released until 30th April, expectations for the bloc's growth prospects have instead been guided by survey data which has seen the EZ March composite PMI climb into expansionary territory for the first time since June last year. The accompanying report noted "expectations for business activity were at their most optimistic since February 2022 during March". Despite the progress on inflation, messaging from the ECB continues to suggest that sufficient confidence on inflation will not be gained until the release of Q1 wage data at the end of May. Accordingly, policymakers continue to guide participants towards a June reduction with even the likes of arch-hawk Holzmann falling into line with such an outcome. With the April decision itself seemingly a given, focus will naturally fall on any tweaks to the policy statement and any hints over forthcoming action. ING suggests that the GC's lightest-touch option for a change in communication would be to alter the existing "confident" but "not sufficiently confident" phraseology. Alternatively, the GC could explicitly declare an outright intention to hike rate at the June meeting (possibly with or without attached conditionality). In terms of market pricing beyond April, June is fully priced for a 25bps reduction with the next cut thereafter fully priced in September and a total of 88bps of loosening seen by year-end.

BOK ANNOUNCEMENT (FRI): The Bank of Korea is likely to maintain its base rate at the current level of 3.5% where rates have been since January last year. As a reminder, the previous meeting in February continued to suggest a lack of urgency for a policy adjustment as the Board voted unanimously to stand pat, while the central bank stated it will maintain a restrictive policy stance for a sufficiently long period and will monitor the inflation slowdown, financial stability and economic growth risks, household debt growth and monetary policy operations in major countries. The BoK kept its 2024 and 2025 GDP growth forecast at 2.1% and 2.3%, respectively, although it acknowledged that uncertainties to the growth outlook are high and it sees 2024 CPI at 2.6% and 2025 CPI at 2.1% but noted that it is premature to be confident inflation will converge on the target level. Furthermore, Governor Rhee revealed that five board members said the current interest rate should be maintained at least for the next three months and one board member said the door for a rate cut should be opened for the next three months, while Rhee still doesn't see much chances of a rate cut in H1 and noted that most members view it is too early to discuss rate cuts. The recent data releases have been mixed and support the case for no policy adjustments as CPI Y/Y in March matched estimates and the prior reading at 3.1% after accelerating from 2.8% the month before but CPI M/M printed softer-than-expected at 0.1% (exp. 0.3%), while Industrial Production was also varied as the latest Y/Y reading for February missed forecasts at 4.8% (exp. 5.8%, Prev. 12.9%) but M/M Industrial Output returned to expansion at 3.1% (exp. 0.5%, Prev. -1.5%).

REVIEWS:

RBA MINUTES REVIEW: RBA Minutes from the March 18th-19th meeting stated that members agreed it is appropriate to leave rates unchanged at the meeting and there was no mention in the minutes that the board considered the option to raise rates. The Board agreed difficult to either rule in or out future changes in the Cash Rate, while the economic outlook was uncertain, but risks seemed broadly balanced. The minutes stated it would take "some time" before the board could be confident inflation returning to target, and upside risks to inflation had not yet materialized, while consumption was very weak. As a reminder, the central bank provided no major surprises at the meeting where it kept the Cash Rate Target at 4.35%, as unanimously forecast, while it reiterated that the Board remains resolute in its determination to return inflation to the target and inflation continues to moderate but remains high. Analysts at Westpac suggest "The minutes of the late-March meeting of the RBA Board recorded that the data had turned out broadly as expected and that this supported keeping the cash rate on hold. Unlike the February minutes, there was no mention of multiple policy options. While the Board endorsed the language of not ruling anything in or out, it seems that policy actions other than keeping rates unchanged were not on the table at this meeting. The current level of the cash rate is assessed as being just right at least for the time being."

ECB MINUTES REVIEW: As is often the case, given the dated nature of the release, the account of the ECB's March meeting passed with little in the way of fanfare. The topline summary was that there had been further progress on all three elements that shape the ECB's reaction function. This warranted increased confidence that inflation was on track to reach the ECB's target in a timely and sustainable manner. However, more data and evidence were needed for the Governing Council to be sufficiently confident of this given that questions remained about the sustainability of the disinflationary process, particularly in services and domestic inflation. It was noted that the Governing Council would have significantly more data and information by the June meeting, especially on wage dynamics. Accordingly, whilst it was noted that the case for considering rate cuts was strengthening, it was judged to be premature to discuss rate cuts at the March meeting. Overall, given the volume of rhetoric heard from the GC since the meeting, little in the way of fresh insight was gained. As such, market pricing for a June cut remains at 100%.

RBI REVIEW RBI kept its Repurchase Rate unchanged at 6.50%, as expected, while it maintained the stance of remaining focused on the withdrawal of accommodation as 5 out of 6 members voted in favour of the rate and policy stance which was similar to the prior meeting. RBI Governor Das stated monetary policy must be actively disinflationary and the MPC will remain resolute in its commitment to aligning inflation to the target, while he also stated that they must ensure the descent of inflation to the target of 4% and the last mile of disinflation is challenging. The central bank maintained its real GDP growth view for FY25 at 7% and also maintained its CPI inflation view for FY25 at 4.5%, as well as noted that it will remain nimble and flexible in liquidity management and will deploy necessary instruments to manage liquidity. The lack of any major surprises or deviation from the prior meeting's voting composition resulted in a muted reaction in INR, while Governor Das also commented that INR has remained rangebound with the relative stability of INR reflecting India's sound macroeconomic fundamentals.