# Central Bank Weekly 5th July: Previewing Fed Chair Powell testimony, RBNZ, BoJ bond meeting; Reviewing minutes from the FOMC and RBA

## PREVIEWS:

**FED CHAIR POWELL TESTIMONY (TUE, WED):** Fed Chair Powell will give testimony to the Senate Banking Committee on Tuesday, and the House Financial Services Committee on Wednesday. He is expected to reiterate his recent remarks that where he said that the disinflation trend is showing signs of resuming, and that they are getting back on the disinflationary path. Powell noted the progress on inflation. Still, Powell reiterated that officials want more confidence before being comfortable with reducing policy rates. Powell also repeated that if the labour market unexpectedly weakens, the Fed would react. He acknowledged the Fed has the ability to take their time and get it right. Minutes to the FOMC June meeting, which Powell is likely to underscore in his testimonies, noted that most policymakers saw the current stance as restrictive; several said if inflation were to persist at elevated levels or rise further, the Fed funds rate might need to be raised. Participants saw 'modest further progress' toward the committee's 2% inflation objective in recent months, with May's CPI data seen by participants as providing additional evidence of progress toward the inflation goal (NOTE: the meeting came before the May PCE data, but after May CPI). Participants affirmed that additional favourable data were required to give them greater confidence that inflation was moving sustainably towards target. Participants highlighted a variety of factors that were likely to help contribute to continued disinflation in the period ahead, including the continued easing of demand–supply pressures in product and labour markets, lagged effects on wages and prices of past monetary policy tightening, the delayed response of measured shelter prices to rental market developments, and the prospect of additional supply-side improvements. Participants suggested a number of developments in product and labour markets had supported their judgment that price pressures were diminishing. On the labour market specifically, a number of participants said policy should stand ready to respond to unexpected economic weakness, with the vast majority seeing US economic growth as having cooled gradually. Several specifically emphasised further demand weakening could generate a larger unemployment response than in recent past, and observed that many labour market indicators pointed to a reduced degree of tightness in labour market conditions. Some analysts said that the minutes felt somewhat dated, given that when the Fed met in June, the Atlanta Fed's GDPnow model for Q2 was tracking growth at over 3%, but that has since been revised down to 1.5% after recent data releases, while we have had further inflation data that has shown the disinflation process has resumed - something that was alluded to by Fed Chair Powell in remarks at the ECB's Sintra conference this week. Oxford Economics said "the communication is evolving in a manner consistent with our assumption for the central bank to eventually tee up a rate cut in September, assuming the economic data generally follows our script," and adds that "the Fed also needs to plan for the unexpected as the transition of the economy toward a slower, but sustainable, pace of growth can feel uncomfortable." OxEco also highlighted that while the minutes suggest the Fed is a little more confident that inflation has resumed moderating, it has acknowledged risks to its dual mandate has come into better balance, "a hat tip that they’re no longer laser focused on inflation, and the Fed is growing more attentive to the downside risks to the labour market" - that has strengthened OxEco's confidence that the central bank will cut rates in September. "The minutes reiterated the Fed needed more data before cutting interest rates, which rules out July but keeps September on the table, and overall, we’re maintaining our forecast for a rate cut in September and December."

**RBNZ POLICY ANNOUNCEMENT**: The RBNZ will conduct its latest Monetary Policy Review next week where the central bank is likely to maintain the Official Cash Rate at the current level with money markets pricing around a 95% chance for the OCR to be kept at 5.50% and just a 5% probability for a 25bps cut. As a reminder, the RBNZ unsurprisingly kept its OCR unchanged at the last meeting in May in what was seen as a hawkish hold as the central bank raised its OCR forecasts across the projection horizon with the rate track suggesting a push-back in the timing of the first cut to late 2025. The central bank also maintained its hawkish language that monetary policy needs to be restricted and reiterated the view that annual consumer price inflation is expected to return to within the committee's 1%-3% target range by the end of 2024. Furthermore, the minutes revealed that members agreed they remained confident that monetary policy is restricting demand and a further decline in capacity pressure is expected, while the committee agreed that interest rates may have to remain at a restrictive level for longer than anticipated in the February Monetary Policy Statement to ensure the inflation target is met and they had discussed the possibility of increasing the OCR at this meeting. The language from RBNZ Governor Orr during the press conference was also hawkish as he stated that it will take time for domestic inflation to decline and they have limited upside room for inflation surprises, as well as noted that they had a real consideration on raising rates at the meeting. However, his comments the following day were more dovish-leaning as he noted that another rate hike would only be meaningful if they believed inflation was getting away from them and that patience on inflation is not exhausted, while he also stated that they can start to ease before inflation hits 2%. The rhetoric from other officials suggests a lack of urgency to tweak policy as Deputy Governor Hawkesby stated that while near-term inflation risks are to the upside, he is confident medium-term inflation is returning to the target, as well as noted that no single data point will cause a rate hike and cutting interest rates is not part of the near-term discussion. Furthermore, RBNZ Chief Economist Conway said inflation may be more sticky near-term but could fall more quickly medium-term and that there is no predetermined timeline for an OCR decrease. Key data since the last policy meeting has been sparse with New Zealand GDP for Q1 the only notable economic release in which both the QQ (0.2% vs. Exp. 0.1%, Prev. -0.1%) and YY (0.3% vs. Exp. 0.2%, Prev. -0.3%, Rev. -0.2%) figures topped estimates and returned to expansion which provides increased scope for the RBNZ to remain patient.

**BOJ BOND MEETING**: At the last BoJ meeting, Governor Ueda said they had decided to put off a detailed plan of JGB tapering until the July 30th - 31st meeting to have a considered discussion with markets. The BoJ will hold its bond meeting between July 9th and 10th - a confab that will be significant as the central bank begins discussions on its bond-tapering plans. This meeting follows a survey conducted by the BoJ among Japanese government bond market participants, including banks, brokerage houses, and life insurers, to gather insights on expectations regarding the range and pace of tapering. The BoJ, when contacted by Reuters, “confirmed it is contacting all the participants of the upcoming meetings to collect their views on the amount, pace and framework for the planned reductions”. Note, Reuters earlier reported that some bond market participants who met with the BoJ in June called on the bank to trim bond purchases in several stages to enhance market liquidity, according to minutes of the meeting cited by Reuters. The meeting was reportedly held between June 4-5th, before the June policy announcement.

## REVIEWS:

**RBA MINUTES REVIEW**: The RBA Minutes from the June meeting stated the Board judged the case for holding rates steady was stronger than the case for hiking, adding they needed to be vigilant to upside risks in inflation and data suggested upside risk for May CPI (which came in hotter than expected). The release suggested Economic uncertainty meant it was difficult to rule in or out future changes in policy, and recent data was not sufficient to change the outlook for inflation returning to target by 2026. The Board judged it is still possible to bring inflation to target while keeping employment gains. The minutes also noted that a rate hike might be needed if the board judged policy was not "sufficiently restrictive", while noting inflation expectations are still anchored, but market premia had drifted higher. The minutes stated that a material rise in inflation expectations could require significantly higher rates. As a reminder, the June 17th-18th meeting saw the RBA keep the Cash Rate unchanged at 4.35% as unanimously forecast by a recent Reuters poll, while it also refrained from any major surprises in its statement as it reiterated that the Board remains resolute in its determination to return inflation to the target. The RBA reiterated that inflation remains above target and is proving persistent, while inflation is easing but has been doing so more slowly than previously expected and remains high. Furthermore, it stated that the path of interest rates that will best ensure that inflation returns to target in a reasonable timeframe remains uncertain and the Board is not ruling anything in or out. It is also worth noting that more recent data from Australia showed firmer-than-expected Australian Weighted CPI YY for May at 4.00% vs. Exp. 3.80% (Prev. 3.60%) which spurred the likes of Deutsche Bank and Morgan Stanley to call for a 25bps hike at the next RBA meeting in August, while money markets are pricing around a 33% chance of a hike and 67% probability of a hold at that meeting.

**FOMC MINUTES REVIEW:** Minutes to the FOMC June meeting noted that most policymakers saw the current stance as restrictive; several said if inflation were to persist at elevated levels or rise further, the Fed funds rate might need to be raised. Participants saw 'modest further progress' toward the committee's 2% inflation objective in recent months, with May's CPI data seen by participants as providing additional evidence of progress toward the inflation goal (NOTE: the meeting came before the May PCE data, but after May CPI). Participants affirmed that additional favourable data were required to give them greater confidence that inflation was moving sustainably towards target. Participants highlighted a variety of factors that were likely to help contribute to continued disinflation in the period ahead, including the continued easing of demand–supply pressures in product and labour markets, lagged effects on wages and prices of past monetary policy tightening, the delayed response of measured shelter prices to rental market developments, and the prospect of additional supply-side improvements. Participants suggested a number of developments in product and labour markets had supported their judgment that price pressures were diminishing. On the labour market specifically, a number of participants said policy should stand ready to respond to unexpected economic weakness, with the vast majority seeing US economic growth as having cooled gradually. Several specifically emphasised further demand weakening could generate a larger unemployment response than in recent past, and observed that many labour market indicators pointed to a reduced degree of tightness in labour market conditions. Some analysts said that the minutes felt somewhat dated, given that when the Fed met in June, the Atlanta Fed's GDPnow model for Q2 was tracking growth at over 3%, but that has since been revised down to 1.5% after recent data releases, while we have had further inflation data that has shown the disinflation process has resumed - something that was alluded to by Fed Chair Powell in remarks at the ECB's Sintra conference this week. Oxford Economics said "the communication is evolving in a manner consistent with our assumption for the central bank to eventually tee up a rate cut in September, assuming the economic data generally follows our script," and adds that "the Fed also needs to plan for the unexpected as the transition of the economy toward a slower, but sustainable, pace of growth can feel uncomfortable." OxEco also highlighted that while the minutes suggest the Fed is a little more confident that inflation has resumed moderating, it has acknowledged risks to its dual mandate has come into better balance, "a hat tip that they're no longer laser focused on inflation, and the Fed is growing more attentive to the downside risks to the labour market" - that has strengthened OxEco's confidence that the central bank will cut rates in September. "The minutes reiterated the Fed needed more data before cutting interest rates, which rules out July but keeps September on the table, and overall, we're maintaining our forecast for a rate cut in September and December."