Central Bank Weekly: 20th September 2024

Previewing RBA, SNB, Riksbank and Banxico; Reviewing FOMC, BoE, BoJ, PBoC LPR, Norges Bank, SARB and CBRT

PREVIEWS

RBA ANNOUNCEMENT (TUE): The RBA is likely to keep the Cash Rate Target unchanged at 4.35% at its meeting next week with all 45 economists surveyed by Reuters unanimously forecasting no change in rates, while money markets are pricing in around a 92% probability for no adjustment in rates and just under an 8% chance of a 25bps cut. As a reminder, the central bank refrained from any policy adjustments at the last meeting in August and stuck to a hawkish tone in which it noted that the Board remains resolute in its determination to return inflation to the target and is not ruling anything in or out, while it reiterated that inflation remains above target and is proving persistent. Furthermore, the central bank said policy will need to be sufficiently restrictive until the board is confident that inflation is moving sustainably towards the target range, and it raised its view for GDP, CPI and the Unemployment Rate with its forecasts assuming the cash rate will be 4.3% in December 2024, 3.6% in December 2025, and 3.3% in December 2026. RBA Governor Bullock also provided a hawkish tone at the post-meeting press conference where she stated that the board considered a rate increase and that a cut is not on the near-term agenda, as well as commented that they are ready to raise rates if needed and that the pricing of cuts for the next six months does not align with the board. The minutes from the meeting also noted that it is possible the Cash Rate would have to stay steady for an extended period and members agreed it is unlikely rates would be cut in the short term. The rhetoric from officials since then continued to support the case for a pause as Governor Bullock repeated that it is premature to be thinking about rate cuts and the board does not expect to be in a position to cut rates in the near term with bringing inflation down remaining the central bank's highest priority, while she stated that they need to see results on inflation before lowering rates and that the board is not going to focus on one inflation number. This suggests the central bank is far from cutting rates, especially given that the latest monthly inflation data for July topped estimates and remained above the central bank's 2%-3% target with Weighted CPI YY at 3.5% vs. Exp. 3.4% (Prev. 3.8%).

RIKSBANK ANNOUNCEMENT (WED): The Riksbank is expected to deliver a 25bps cut to 3.25%, with markets fully pricing in the chance of such a move and assigning a 16% probability of a deeper 50bps cut. At the last meeting, the Riksbank cut rates by 25bps (as expected) and shifted dovishly, guiding towards "two or three times this year" (prev. guided "two or three times in H2"); essentially opening the door to a cut at each meeting. The Minutes of that meeting mentioned that a 50bps cut was discussed, but the board felt a 25bps cut was well-balanced. Focus of this meeting will also be on the guidance for the remainder of the year, which SEB believes will be revised to indicate another two rate cuts to 2.75% by the end of the year vs Riksbank's current forecast of 3.14%; it can be noted that Governor Thedeen said that "3 additional cuts are more likely than 2 this year". Further out, the bank thinks the rate path will also indicate two more cuts until May 2025. In terms of recent data, the Core CPIF in August fell in line with the Bank's forecast, but headline CPIF fell far below target, which could stimulate the Riksbank to cut by 50bps. SEB believes the chance of such a move is "significantly" higher than market pricing, but would be at odds with the guidance given in the August meeting; as such, SEB thinks it is more probable that the Riksbank will cut by 50bps in November. The SEK has been in focus at past meetings but has stabilised since the last announcement so is unlikely to take much of the attention at this confab.

SNB ANNOUNCEMENT (THU): Expected to continue its easing cycle via another 25bps cut which will take the Policy Rate to 1.25%. Market pricing assigns a circa 63% chance of such an outcome with a larger cut of 50bps priced at 37%. Further easing is justified by the ongoing moderation of inflation with August's Y/Y CPI printing at 1.1%, shy of the 1.2% forecast by markets and well below the SNB's overall Q3 forecast of 1.5%. The continued faster-than-expected moderation of inflation may well provide the SNB with more confidence on the pricing front and will likely see downward tweaks to their inflation forecasts, though the magnitude of the adjustment remains unclear. Additionally, such confidence could enable the SNB to allow the CHF to weaken a touch, as called for by the Swissmem group who in early-August outlined their fair value EUR/CHF view of 0.98 vs circa. 0.92 at the time and 0.9450 at the time of writing. Furthermore, the impact of currency strength on domestic industry was acknowledged by Chairman Jordan in a speech towards the end of August. As a reminder, this is the last policy meeting for Chairman Jordan who is to be replaced by current Vice-Chairman Schlegel.

BANXICO ANNOUNCEMENT (THU): Mexico's central bank cut rates by 25bps to 10.75% at the last meeting, where analyst expectations were split between a cut and a hold. The decision was not unanimous however with three out of the five Banxico members (namely Governor Victoria Rodríguez, Galia Borja, and Omar Mejía) supporting the decision, while the remaining two (Irene Espinosa and Jonathan Heath) wanted to hold rates at 11%. The meeting saw 2024 year-end headline inflation forecasts rise from 4.0% to 4.4%, while its core projection was left unchanged at 3.9%. The language within the statement was largely reiterated, with the central bank maintaining its view that "looking ahead, the Board foresees that the inflationary environment may allow for discussing reference rate adjustments." Since then, recent data has seen the August inflation data cool further with core easing to 4.0%, the top end of Banxico's target range. Meanwhile, activity gauges have been soft, leading some to question the economic momentum in Q3. Externally, the Fed delivered a bumper 50bps rate cut this week, which analysts said gives Banxico more scope to continue easing. Accordingly, many would be unsurprised by another 25bps rate cut in September. The latest Banxico private sector analyst poll saw expectations shift with the year-end rate seen at 10.25%, lower than the 10.50% in the prior poll, while the end-2025 rate is seen at 8.25% vs the prior forecast of 8.50%. However, with the recent approval of Mexico's judicial reform, Oxford Economics writes it poses a downside risk to investment and could pause policy rate easing. Nonetheless, the desk sees rates ending at 10.25%, 50bps down from current levels.

REVIEWS

FOMC REVIEW: The FOMC cut rates by 50bps, taking the target for the federal funds rate to 4.75-5.00%, more in fitting with money market pricing before the release rather than the analyst consensus of 25bps. There was one dissenter; Governor Bowman opted to vote for a smaller 25bp rate reduction. Within its projections, the 2024 rate forecast was revised down to 4.4% from 5.1%, which implies a further 50bps of easing from current levels. The projections showed that nine of the 19 policymakers see the policy rate above the median forecast for 2024, nine at the median, and one sees it below that. The statement saw some changes: it noted inflation has made further progress but remains somewhat elevated, and it added it has gained greater confidence inflation is moving sustainably towards 2%, and judges risks to achieving its goals are roughly in balance. However, it left its guidance unchanged, noting that "the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks," but it said that it is strongly committed to "supporting maximum employment" and returning inflation to its 2% objective (previously it only referenced inflation). Further out, the FOMC's median projections see the 2025 rate at

3.4% (prev. 4.1%), and the end-2026 dot at 2.9% (prev. 3.1%), where it also sees the neutral rate (2.9% vs prev. 2.8%). At the post-meeting press conference, Fed Chair Powell emphasised that the central bank is not bound by a set course, and will make decisions on a meeting-by-meeting basis. He said that current actions should not be seen as establishing a new norm. He also clarified that the SEPs represent a range of views and are not definitive plans. Regarding the 50bps rate cut, he mentioned there has been a lot of data, including recent labour market revisions which suggest possible downward adjustments to payroll numbers. Despite this, Powell noted that the Fed remains optimistic about the economy's growth, supported by solid retail sales and Q2 GDP figures. He pointed out that current labour market conditions are strong, with low unemployment, high participation, and moderate wage increases. On inflation, Powell affirmed the Fed's commitment to reaching a 2% target. He dismissed concerns that the Fed is behind the curve, highlighting its measured pace compared to other central banks. Powell also suggested that the neutral rate is likely higher than pre-pandemic levels and that balance sheet reduction will continue as part of normalising policy. In the wake of the meeting, money markets were pricing around 70bps of further easing at the two remaining policy meetings this year, suggesting the market still thinks there is a risk of another upsized rate reduction; the Fed median dot plot forecasts a further 50bps of easing this year. Looking to next year, markets price that rates will bottom out at around 2.8% in late 2025 (note: the Fed forecasts neutral at around 2.9%, and its projections implied around 150bps of rate cuts in 2025); the market continues to price the same volume of rate reductions (around 200bps of further cuts following the 50bps enacted this week). In the wake of the decision, analysts at Goldman Sachs revised its Fed forecast to accelerate the pace of cuts next year, and now expect a longer string of consecutive 25bp cuts from November 2024 through June 2025, for an unchanged terminal rate of 3.25-3.50% (note: markets are pricing terminal at 2.75-3.00%).

BOE REVIEW: As expected, the MPC opted to keep the Base Rate at 5.0% after delivering a 25bps rate cut at the prior meeting. The decision to maintain policy settings was made via an 8-1 vote (vs. consensus 7-2) with Dhingra the lone dissenter in voting for a rate cut. Within the consensus that backed an unchanged rate, "there was a range of views among these members on the degree to which the unwinding of past global shocks, the normalisation in inflation expectations and the current restrictive policy stance would lead underlying domestic inflationary pressures to continue to unwind". For most members, it was noted that "in the absence of material developments, a gradual approach to removing policy restraint would be warranted". This view was echoed by Governor Bailey who remarked that the MPC must be careful not to cut rates too fast, or by too much. Furthermore, the policy statement reiterated that policy "will need to continue to remain restrictive for sufficiently long". Aside from the rate decision, the MPC also voted unanimously to reduce the stock of Gilts by GBP 100bln between October 2024 and September 2025 (as expected). Note, the BoE refrained from including sales of 1-3 year maturity Gilts. Overall, the tone of the policy statement was one of caution with the MPC very much in data-dependent mode. This prompted a hawkish repricing for the rest of the year with just a 64% chance of a cut seen in November (vs. 100% pre-release) and a total of 40bps of easing seen by year-end (vs. 52bps pre-release). Pantheon Macro sees just one cut for the rest of the year with the MPC likely to prefer November on account of it being an MPR meeting. In the wake of the meeting, Governor Bailey was on the wires and noted he is optimistic that UK interest rates will fall further, though further evidence is required, while he needs to see residual inflation pressures disappear. The Governor added it is imperative that the UK improves its current potential growth of 1.2-1.3%. Regarding QT, Bailey is "very relaxed" that the gov't will take the right decision on the treatment of QT within fiscal rules, and will have no impact on BoE policy.

BOJ REVIEW: BoJ kept its short-term policy rate unchanged at 0.25%, as expected with the decision made by a unanimous vote. BoJ also stated that inflation is likely to be at a level generally consistent with BoJ's price target in the second half of its 3-year projection period through fiscal 2026 and it sees medium and long-term inflation expectations increasing. Furthermore, it sees exchange rate trends as having a greater influence on prices and said Japan's economy is likely to achieve growth above potential but also stated that they must be vigilant to the impact of financial and FX market moves on Japan's economy and prices. Governor Ueda's post-meeting presser was more interesting in which he struck a clear dovish and cautious tone. In this press conference, Ueda put significant weight on overseas economies, particularly the US following the Fed's 50bps rate cut. One of Ueda's most notable comments was that upside price risks have decreased given recent FX moves, and risks of an inflation overshoot have somewhat diminished. Furthermore, Ueda kept referring to markets as unstable. As a reminder, on August 7th Deputy Governor Uchida said the BoJ will not hike rates when markets are unstable. As such, Governor Ueda referring to markets as being unstable in the post-meeting press conference, alongside the decrease in upside price risk, has been taken as a "slowing" of hiking plans.

PBOC LPR REVIEW: The PBoC opted to maintain its Loan Prime Rates (LPRs) at 3.35% for the 1-year and 3.85% for the 5-year despite expectations for both rates to be trimmed following the recent batch of dire Chinese data, including sub-par inflation, imports, retail sales, industrial production, and house prices – all pointing to sluggish demand from China. The unchanged rates also come despite the FOMC cutting its policy rate by 50bps on Wednesday. Heading into the LPR release, 27 out of 39 respondents polled by Reuters expected a rate cut. Analysts at ANZ suggest a rate cut will likely be included in a larger package, which is being reviewed by policymakers. ANZ added that the "Current economic data and expectations all support a rate cut. And, lowering existing mortgage loan rates also requires further reductions in the 5-year LPR, which may lead to a one-time and significant decline in the LPR in the fourth quarter." Reuters earlier this week reported that analysts and policy advisers expect China to ramp up measures to at least help the economy meet the 2024 growth target, which is proving to be increasingly challenging.

NORGES BANK REVIEW: In short, a hawkish hold. As expected, the policy rate was maintained at 4.50%. While the rate projections were adjusted and the timing of the first cut brought forward from Q2-2025 the adjustment was of a smaller magnitude than widely expected heading into the announcement. The new path/commentary implies a first cut in Q1-2025, a quarter earlier than the June MPR's view but more hawkish than expected heading into the release. Pre-release, the general view was that the path would price in around a 50% chance of the first cut happening in Q4-2024 (i.e. December), however, the forecast for that period was subject to only a very minor adjustment. Ahead, the November decision will likely be a reiteration of this one, barring any material economic development with particular emphasis on the NOK; as such, December's MPR will be scrutinised for any indication as to which Q1 meeting the Norges Bank expects the first cut to occur on. Following the meeting, the likes of SEB have pushed back their call for a first cut in Dec'24 to Mar'25.

BCB REVIEW: The Copom raised its Selic rate by 25bps points to 10.75%, its first hike in over two years. The unanimous decision was driven by stronger economic activity and inflation risks and comes amid a robust labour market and rising wages, prompting concerns over potential inflationary pressures. Pantheon Macroeconomics noted that the statement did not provide explicit forward guidance, but keeps the door open to further hikes, by highlighting upward risks to inflation from the tight labour market, and resilient services inflation while acknowledging potential relief from a global slowdown. Pantheon anticipates rates will remain on hold at the next meeting in November, with possible cuts by year-end, depending on inflation dynamics and external factors. Overall, PM expects disinflation to resume, alongside a cooling labour market, despite a more hawkish stance than previously anticipated. Meanwhile, economists generally expect two additional rate increases by year-end, according to Refinitiv, with projections for inflation reaching 4.3% in 2024 and 3.7% in 2025, both above the 3% target.

CBRT REVIEW: The Turkish Central Bank left its Weekly Repo Rate at 50% as widely expected by analysts heading into the meeting. The CBRT however dropped its tightening bias, in which it noted "monetary policy tools will be used effectively", omitting the prior line that "monetary policy stance will be tightened". Analysts at BBVA suggested that "The bank smoothed its tone by changing the statement." The desk believes Turkey's headline inflation rate will cool to 43% by the end-2024, "which could create room for the CBRT to consider starting a gradual easing cycle". However, BBVA warns that high inflation expectations and uncertainties from wages could require a cautious stance, as such BBVA shifted its first rate cut expectation to December from November, with a 250bps move. Meanwhile, CapEco maintained its call for the first rate cut in early 2025.

SARB REVIEW: South Africa's Reserve Bank cut its repo rate by 25bps to 8.00%, as expected, in a unanimous decision, although MPC members did consider an unchanged stance, and also a larger 50bps cut, potentially indicating there may be some division ahead. The decision was backed up by remarks from Governor Kganyago, who noted risks to the growth outlook were balanced, alongside an expectation that the recent moderation in inflation is likely to be sustained. In addition, Capital Economics points out that there is still clearly some reluctance on the MPC to declare the inflation fight over; Governor Kganyago remarked that "you've got to be cautious; adventurism is not part of our monetary policy toolkit." As such, Cap Eco thinks that the hawkish tone may, once again, be overcooked given the low inflation and sluggish growth backdrop that is likely to continue in the near term. Its economists see the repo rate lowered further at upcoming meetings, and think it will end 2025 at 6.25%, below the consensus.