newsquawk

Central Bank Weekly - 4th October 2024

Previewing Minutes from FOMC, ECB and RBA, Rate decisions from RBNZ, RBI and BOK; Reviewing Riksbank Minutes

PREVIEWS

RBA MINUTES (TUE): The tone down in hawkishness from the central bank was evident at the prior meeting, whereby at the press conference, RBA Governor Bullock reiterated that rates are to remain on hold for the time being and revealed that they did not explicitly consider a rate hike at the meeting, unlike the prior meeting in August where the board had considered an increase. Markets will likely dissect the minutes for any more on this front. To recap the decision itself, RBA provided no surprises as it kept rates unchanged, as unanimously forecast, and maintained its hawkish rhetoric in which it reiterated that the Board remains resolute in its determination to return inflation to the target and is not ruling anything in or out. RBA also repeated that inflation remains above target and is proving persistent, as well as stated that returning inflation to target is the priority. Furthermore, it said inflation is still some way above the midpoint of the 2–3% target range and the Board will rely upon the data and the evolving assessment of risks to guide its decisions, while its current forecasts do not see inflation returning sustainably to target until 2026. Although the RBA effectively opted for a hawkish hold, this was seen to be slightly less hawkish than the previous meeting as Capital Economics noted the RBA no longer explicitly discussed upside risks to inflation in the main body of the statement and focused on downside risks when discussing risks to the outlook, while it also tweaked its rhetoric on wages in which it stated that “wage pressures have eased somewhat” compared with its previous language that “wage growth is still above the level that can be sustained given trend productivity growth”.

RBNZ ANNOUNCEMENT (WED): The RBNZ is unanimously expected to continue cutting rates at its meeting next week with 17 out of 28 economists surveyed by Reuters forecasting a 50bps cut in the OCR to 4.75% from the current 5.25% level and with the remaining 11 calling for a 25bps cut, while money markets are pricing around a 96% likelihood of a 50bps reduction and just a 4% chance for a 25bps move lower. As a reminder, the RBNZ delivered a 25bps cut at the last meeting in August amid mixed views among analysts regarding a cut or a hold although money markets had priced a greater chance of a cut, while the central bank's OCR projections also suggested a further cut by year-end and for the OCR to decline 101bps by mid-2025. The central bank's rhetoric was also less hawkish at that meeting as although it stated that members noted that monetary policy would need to remain restrictive for some time to ensure that domestic inflationary pressures continue to dissipate, the committee agreed there was scope to temper the extent of monetary policy restraint and observed that the balance of risks has progressively shifted since the May monetary policy statement. Furthermore, it stated that the pace of further easing will thus be conditional on the committee’s confidence that pricing behaviour is continuing to adapt to a low-inflation environment and that a broad range of high-frequency indicators point to a material weakening in domestic economic activity in recent months. During the press conference, RBNZ Governor Orr noted confidence that inflation is back in its target band and that they can commence re-normalising rates, while he revealed that they considered a range of moves including a 50bps cut but the consensus was for a 25bps move which he said was a relatively low-risk start. Governor Orr also commented the following day after the meeting that they are to proceed with caution in adjusting interest rates and that removing restraint is appropriate for now. This suggests the central bank is likely to continue lowering rates, while recent GDP data also supports the case for a reduction after the New Zealand economy contracted in Q2 with GDP QQ at -0.2% vs. Exp. -0.4% (Prev. 0.2%, Rev. 0.1%) and GDP YY at -0.5% vs. Exp. -0.5% (Prev. 0.3%, Rev. 0.5%).

FOMC MINUTES (WED): 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 25bps 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, while 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 end-2026 dot at 2.9% (prev. 3.1%), where it also sees the neutral rate (2.9% vs prev. 2.8%). Since then, we have again heard from Fed Chair Powell; speaking this week, the Fed chief said policymakers were cautious about quick rate cuts, stating that upcoming employment and inflation reports will continue to influence the November decision. Powell said that if the economy behaves as expected, there could be two additional cuts this year, for a total 50bps of reductions, implying that the Fed was likely to scale down the cadence of its rate reductions to 25bps increments, after kicking off the cycle with a bumper 50bps move. The Fed chief said that the labour market's current state may not require further cooling, emphasising the importance of policy lags, and reaffirmed the Fed's approach to maintain economic strength, and again expressed confidence in getting inflation back to its 2% target. He said the labour market provides real-time economic insights, and job creation levels may not sustain the unemployment rate amid rising supply. He acknowledged that the labour market has cooled significantly. Powell mentioned that recent revisions in GDI and personal income have alleviated downside risks, while the savings rate revisions indicate healthy spending levels. He also expressed caution about productivity improvements being sustained. After Powell's remarks, Goldman Sachs said it continues to expect 25bps cuts in November and December, though it was a close call for the choice between 25bps and 50bps in November.

RBI ANNOUNCEMENT (WED): Consensus is for the central bank to keep the Repurchase Rate unchanged at 6.50% with 63 out of 76 surveyed by Reuters predicting the RBI would hold the repo rate at the current level and with a majority of economists anticipating the central bank to wait until December before cutting rates, although market participants will be eyeing if there is any shift in the central bank’s tone given the change of external members within the MPC. As a reminder, the RBI kept its key rate unchanged at the last meeting in August for the 9th consecutive meeting, as expected, while it maintained the stance of remaining focused on the withdrawal of accommodation in which 4 out of 6 members voted in favour of the rate decision and policy stance. RBI Governor Das said during the policy address that India's growth remains strong and inflation is broadly on a declining trajectory, while he added that they want inflation to progressively align with the target and noted the food component of inflation remains stubborn but added that going forward, the base effect on inflation will wear out. Furthermore, he said food inflation pressures cannot be ignored and that they cannot and should not become complacent because core inflation is easing, as well as noted that high food inflation adversely affects household inflation expectations and the MPC may look through high food inflation if transitory, but cannot afford to do so if it remains persistent. The dissent at that meeting came from the MPC external members Goyal and Varma who both voted to reduce the policy repo rate by 25bps and to change the stance to neutral, although along with fellow external member Bhide, are finishing their terms on October 4th with Ram Singh, Saugata Bhattacharya and Nagesh Kumar appointed as the new members of the central bank's rate-setting monetary policy committee. Therefore, the upcoming meeting will provide insight into the thinking and stances of the new members who are seen as unlikely to make immediate changes in their inaugural policy decision. Nonetheless, there are outside calls for the central bank to cut at this meeting given the recent rate cuts by major global central banks and the market consensus is for a total of 50bps of cuts in this cycle, although Nomura thinks there will be a more forceful approach in which the investment bank predicted the RBI would reduce rates by a total of 100bps from October to mid-2025.

ECB MINUTES (THU): As expected, the ECB opted to cut the deposit rate by 25bps from 3.75% to 3.5% whilst also lowering the main refi and marginal lending rates by 60bps (as previously announced in March). In the policy statement, the ECB reiterated that it will continue to follow a meeting-by-meeting approach and remain in data-dependent mode. Furthermore, policy rates will be kept sufficiently restrictive for as long as necessary and the ECB will not pre-commit to a specific policy path. In the accompanying macro projections, headline inflation forecasts for 2024-26 were left unchanged; 2026 remained below target at 1.9%. On a core basis, 2024 and 2025 forecasts were upgraded by 10bps on account of stubborn services inflation. From a growth perspective, 2024-2026 projections were lowered by 10bps each “owing to a weaker contribution from domestic demand over the next few quarters”. At the follow-up press conference, Lagarde noted that the decision to cut the DFR by 25bps was “unanimous”. On the inflation path, the President noted that September inflation is likely to see a downtick on account of base effects before rising again in Q4. Despite attempts by journalists to extract information about easing intentions for the October meeting, Lagarde stated she would neither commit to a position or comment on how close the ECB is to R-star. Note, the account of the meeting will likely be deemed as stale by market participants given the shift in market pricing seen September 12th on account of soft survey data and inflation metrics.

BOK ANNOUNCEMENT (FRI): The Bank of Korea will decide on rates next week in what is seen as a live meeting amid sluggish economic activity and softer inflation. As a reminder, the BoK kept its base rate unchanged at 3.50% at the last meeting, as expected, with the decision made unanimously. The central bank said it would examine the proper timing of rate cuts and noted greater confidence that inflation will converge on the target level, while it dropped the phrase 'sufficient period of time' regarding maintaining a restrictive policy stance. BoK Governor Rhee provided a dovish tone after the meeting in which he stated that inflation conditions are appropriate for a cut and revealed that four board members said room for a rate cut should remain open but noted that rising financial stability risks warranted the BoK's decision to hold rates at that meeting. Furthermore, Rhee said the pace and extent of an interest rate cut in South Korea will be smaller than that of the US and that the BoK is communicating with markets using a three-month horizon forward guidance, as well as stated that the BoK sees inflation maintaining the current stable trend for the time being. The rhetoric from the central bank since then has been sparse and Governor Rhee recently responded that he would not comment and would need to discuss with the board members the impact of recent government measures aimed at taming household debt when asked about the possibility of cutting rates at next week’s meeting. Nonetheless, recent key data releases from South Korea support the case for a cut as Final Q2 GDP confirmed a Q/Q contraction of 0.2% and Y/Y growth slowed to 2.3% from the previous quarter of 3.3%, while CPI Y/Y for September softened to 1.6% vs Exp. 1.9% (Prev. 2.0%) which was the slowest pace of increase since February 2021 and below the central bank’s medium-term inflation of 2.0%, providing greater scope for the central bank to move.

REVIEWS

RIKSBANK MINUTES REVIEW: At the Riksbank’s September meeting, the Bank unsurprisingly cut rates by 25bps to 3.25%; with the highlight being that the policy rate may be cut at the two remaining meetings this year, with a possibility of a larger 50bps cut at one of those meetings; the Bank noted that rates are expected to be cut at a faster pace than before. Governor Thedeen at his post-policy press conference noted that the baseline was a 25bps cut at the next two meetings; remarks which were most recently also echoed by Jansson. The Minutes suggested that this was a unanimous decision and all board members supported the path indicating further easing, including the possibility of a 50bps cut. The Minutes also highlighted the downside risks to inflation/growth; putting attention on CPIF Y/Y (as a reminder the most recent print came in at 1.2%, well below the Riksbank target at 1.7%). Delving deeper into the Board’s personal views; Jansson and Theeden stressed the importance of improving growth aspects, with the latter striking a slightly more dovish tone by noting a gradual approach allows the possibility of a 50bps cut. Bunge on the other hand, downplayed the significance of a 50bps cut at a specific meeting, whilst Seim was slightly more hawkish, noting that she is not concerned at this stage that inflation will stay permanently below target. The SEK garnered less focus at this meeting, but some members highlighted the downside risk for the currency due to faster rate cuts. Overall, the Minutes encapsulated the different stances between board members and their opinions on the potential of a larger weighted 50bps cut. Analysts at SEB stick with their view that the Riksbank will opt for a larger 50bps cut in November, followed by 25bps in December, January and March.