Central Bank Weekly - 11th October

Previewing ECB, SARB, CBRT; Reviewing RBNZ, BoK, RBI, Minutes from FOMC, ECB and RBA

PREVIEWS

SARB ANNOUNCEMENT (TUE): At the prior meeting in September, the SARB cut rates by 25bps from 8.25% to 8.00%, the first time in four years. Governor Kganyago has maintained that the interest rates cutting cycle in the country will continue to be dictated by "domestic idiosyncrasies" in spite of emerging markets central banks cutting rates. On the decision, Nedbank economist da Silva said the domestic economy fared slightly better in Q2 '24, with easing structural constraints, falling inflation, and rising real incomes supporting production and consumption. He added that "the main boost came from a rebound in domestic demand, which offset a renewed deterioration in the country's net export position." Nonetheless, Da Silva stated "Headline inflation is forecast to remain around the Reserve Bank's 4.5% target over the next 2 years, creating space for further monetary easing". The desk expects the repo rate to decline from 8% currently to 7.75% by end-2024 and 7% by end-2025.

ECB ANNOUNCEMENT (THU): Expectations are for the ECB to lower the deposit rate by 25bps from 3.5% to 3.25%, according to 68/75 surveyed by Reuters. Markets price such an outcome at 98%. In the wake of the September meeting, markets assigned just a 28% chance of an October rate cut and were of the view that the ECB would opt to lower rates at meetings that are accompanied by macro projections, whilst pausing at those that do not contain them (as a reminder, ECB cut in June, paused in July and cut in September). Furthermore, source reporting via Reuters stated that an October rate cut was unlikely as a move before December would require "exceptional negative growth surprises". Fast forward to now and the playbook put forward by the ECB and absorbed by markets has been disregarded. The first wave of repricing for October was driven by the September PMI metrics which saw the EZ-wide manufacturing slip further into contractionary territory, services decline, dragging the composite into contractionary territory; its largest decline in 15 months. Thereafter, inflation metrics for September added to the dovishness with headline HICP slipping below target to 1.8% from 2.2%, albeit super-core inflation only slipped to 2.7% from 2.8% and services inflation stands at a still-lofty 4%. As such, the market raced to price in an October rate cut. ECB speak has largely endorsed such a move with even some of the hawks on the GC open to such a move. That being said, from an alternative viewpoint, ING suggests that a rate cut is not a done deal. The desk cites the fact that soft inflation and growth outturns were already baked into the ECB's forecasts, whilst comments from Germany's Schnabel stated that, whilst the bank cannot ignore headwinds to growth, it cannot do much to solve structural weaknesses. Looking beyond October, a further 25bps cut is near-enough fully priced in for December with four further cuts expected in 2025.

CBRT ANNOUNCEMENT (THU): The Turkish Central Bank is expected to maintain its main Weekly Repo Rate at 50%, with the first rate cut likely to come in December or January, as per a Reuters poll. Six out of ten economists forecast a December cut, while the remaining four see it happening in January. This represents a more hawkish shift compared to the September poll, where most predicted a cut in October or November. The initial rate reduction is anticipated to be 250bps, bringing the rate down to 47.5%. The delay comes after higher-than-expected inflation in September, despite an annual rate drop to 49.4%. Analysts cite persistent inflation risks and a cautious approach from the CBRT. The CBRT Governor, at the start of October, cautioned that the September inflation data from the statistical institute was well above their expectations and "upward risks to inflation are clear." As a reminder, at the prior meeting, 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".

REVIEWS

RBA MINUTES REVIEW: The RBA Minutes from the September meeting provided a more balanced tone. It noted the Board discussed scenarios for both lowering and raising interest rates in the future and that members felt not enough had changed from the previous meetings that the current Cash Rate best-balanced risks to inflation and the labour market. It also stated that future financial conditions might need to be tighter or looser than at present to achieve the board's objectives and that scenarios for lowering, holding and raising rates are all conceivable given the considerable uncertainty about the economic outlook. The minutes also stated that policy could be held restrictive if consumption growth picks up materially or could be tightened if present financial conditions are insufficiently restrictive to return inflation to target, while policy could be eased if the economy proves significantly weaker than expected and it is not necessary for the cash rate to evolve in line with policy rates in other economies. Furthermore, it stated that underlying inflation is still too high and policy will need to remain restrictive until board members are confident inflation is moving sustainably towards the target range, as well as noted that it is not possible to rule in or out future changes in the cash rate target at this time. The rhetoric suggests all options remain on the table with future policy moves to depend on how the economy progresses, although there seems to be a lack of urgency for an immediate policy shift given the central bank's view regarding elevated underlying inflation.

RBNZ REVIEW: The RBNZ delivered a 50bps cut to the OCR which was widely expected by the majority of economists in a recent survey, and as money markets had priced around a 93% likelihood of heading into the announcement. RBNZ said New Zealand is now in a position of excess capacity and low import prices have assisted disinflation, while the Committee assessed annual consumer price inflation within its 1-3% target and noted it was appropriate to cut OCR by 50bps to achieve and maintain low and stable inflation. The Minutes from the meeting noted that the Committee confirmed future changes to the OCR would depend on its evolving assessment of the economy and that they discussed the respective benefits of a 25bps cut versus a 50bps cut in the OCR but decided a 50bps cut at this time is most consistent with the committee's mandate of maintaining low and stable inflation. Furthermore, the central bank stated that the new OCR level of 4.75% is still restrictive and leaves monetary policy well-placed to deal with any near-term surprises, as well as noted that the economic environment provides scope to further ease the level of monetary policy restrictiveness.

FOMC MINUTES REVIEW: Minutes from the FOMC's September confab revealed that while a substantial majority favoured a 50bps rate cut, believing it would align monetary policy with inflation and labour market objectives, some officials had supported a 25bps, and "a few" said they could have supported a decision in favour of the smaller reduction. Nearly all participants expressed increased confidence that inflation was moving towards its 2% target; participants also acknowledged complexities in evaluating labour market trends, but believe further cooling may not be needed to achieve inflation goals. On the balance sheet, the minutes said "several" discussed the importance of communications that QT could continue for some time, even as rates are reduced. Pantheon Macroeconomics said the minutes showed a more cautious outlook compared to Chair Powell's post-meeting press conference. Its economists said the Committee's patience reflects confidence in sustainable inflation at 2% and stable GDP growth, allowing for gradual policy adjustments. Money market implied expectations are now in the camp of a 25bps rate cut at the Fed's November 7th policy meeting, with the probability of another larger 50bps move being priced out after strong labour market data for September. Additionally, in recent remarks, Fed Chair Powell signalled a preference for 50bps of further easing this year across the two remaining meetings. There are even some calls for a November "skip", with Fed's Bostic, who signalled just one more 25bp rate cut in the 2024 dot plot, said that some elements of the recent inflation data validate this view.

RBI REVIEW: RBI kept the Repurchase Rate unchanged at 6.50%, as expected with the decision made through a 5-1 vote (prev. 4-2) and it unanimously voted to switch its stance to neutral from the prior stance of remaining focused on the withdrawal of accommodation, while Governor Das stated that macroeconomic parameters of inflation and growth are well balanced although the moderation in headline inflation is expected to reverse in September and remain elevated in the near term. Das provided an upbeat tone regarding the economy as he noted that domestic growth has sustained momentum with the growth story remaining intact and that prospects of private consumption look bright. However, the language on inflation was somewhat varied in which he commented that core inflation has bottomed out and food inflation pressures could see some easing later in the year but added that there is difficulty in navigating the last mile of disinflation and significant risks to inflation still stare at them. The main takeaway from the meeting was the change in policy stance as the decision to shift to neutral is seen to pave the way for future cuts and would support the ongoing consensus for the rate-cutting cycle to begin at the next policy announcement in December, while the meeting was the first to include the MPC's newly appointed external members Ram Singh, Saugata Bhattacharya and Nagesh Kumar in which the latter was the lone dissenter on rates and voted for a 25bps cut. However, participants will have to wait until later in the month for the minutes from the meeting to get an insight into the individual thinking of the MPC's new external members.

ECB MINUTES REVIEW: Overall, the minutes confirm what has been heard in the central bank's post-meeting communications and he various sourced reports; policymakers are not yet ready to declare victory over inflation (emphasised most recently by Vice President de Guindos), but focus is increasingly falling on the downbeat growth outlook. The minutes noted that PMI data were indicating potential headwinds to the near-term growth outlook, which may imply a downward revision to the outlook. As such, the accounts stress that optionality should be retained regarding the speed of policy adjustments. Elsewhere, the accounts said "there are scenarios in which it might be necessary to suspend the cutting cycle for a while," citing factors which could lead to upward surprises in core inflation. In summary, the account is as usual somewhat stale particularly as the next ECB policy announcement is just one week away; nonetheless, it does serve to underscore the board's desire to keep as much policy flexibility as possible and adds further evidence to the growing importance of growth indicators when assessing future ECB policy.

BOK REVIEW: The Bank of Korea cut its base rate by 25bps to 3.25%, as expected, with the decision not unanimous as board member Chang Yong-Sung dissented and the central bank also voted to lower policy interest rate in special loan programmes. BoK said it will carefully determine the pace of further cuts to the base rate and will thoroughly assess trade-offs among inflation, growth, and financial stability, as well as noted that South Korea's economy is to continue moderate growth. Governor Rhee revealed after the meeting that five board members said keeping the policy rate at 3.25% is appropriate for the next three months and one board member was open to a further cut in the three months ahead, while Rhee added that the policy decision could be viewed as a hawkish cut. Furthermore, he said they will look at property prices, Q3 growth figures and the pace of household debt growth for the rate review in November, while he added that they will look at financial stability risks for any further rate reduction decisions and that the pace of rate cuts will be slower in South Korea compared with the US.