newsquawk

Central Bank Weekly - 4th April 2025

Previewing FOMC Minutes, RBNZ, RBI; Reviewing RBA, ECB Minutes

PREVIEWS

FOMC MINUTES (WED): At its March meeting, the Fed kept rates unchanged, as expected, and maintained its forecast of two rate reductions in 2025. It removed language from its statement suggesting risks to its goals were balanced, citing increased uncertainty. However, it reiterated that "economic activity has continued to expand at a solid pace," labour market conditions "remain solid,", and inflation "remains somewhat elevated." Although, it did add that “uncertainty around the economic outlook has increased.” Its 2025 and 2026 growth projections were lowered, with higher unemployment, and it lifted its PCE inflation forecasts. It also announced that, starting April, the pace of balance sheet runoff will slow, reducing the monthly Treasury redemption cap to USD 5bln (from the current USD 25bln), though the MBS cap remains unchanged at USD 35bln. Analysts were not very surprised by the announcement, given the use of its reverse repo facility has declined significantly this year. The prior meeting minutes also alluded to a slowdown of the balance sheet runoff was coming, although the March meeting was not explicitly signalled by policymakers. The projections also showed that FOMC members are divided on the number of cuts in 2025; the dot plot continues to show two rate cuts this year, and projections for 2026 and the long-term forecast was left unchanged, but four participants now expect rates to be unchanged in 2025 (vs just one previously), and four members expect only one rate cut. In his press conference, Chair Powell stressed a wait-and-see approach, emphasising uncertainty ahead. He noted rising short-term inflation expectations, but highlighted that long-term expectations remain stable. Powell acknowledged tariffs contribute to higher goods prices but are hard to quantify in terms of inflation. He said the Fed could either cut or hold rates at a "clearly restrictive" level. On the balance sheet, he clarified that the slowdown in runoff was a technical adjustment, not a policy shift. He also clarified that removing the language about balanced risks was not a signal. Since the meeting, markets have been rocked by the US tariff announcements this week, which analysts said has the potential to lower the US growth trajectory while boosting inflation. And reports note that the tariffs imposed by President Trump create a challenging environment for the Fed, complicating efforts to control inflation and prevent a recession. Bloomberg said it might lead to a cautious approach by the central bank as it monitors the economic impact before taking further action. Still, money markets began to discount four 25bps rate reductions this year following the announcement. Morgan Stanley, however, has leaned back on this, with the bank scrapping its call for a June Fed cut after Trump's tariff announcement, as a result of "tariff-induced inflation," and now sees the FOMC on hold until next March. MS said that if tariffs persist, US economic growth may suffer, with downside risks increasing.

RBNZ ANNOUNCEMENT (WED): The RBNZ is expected to cut rates for the fifth straight meeting with a Reuters poll showing all 31 economists surveyed expect the Official Cash Rate to be lowered by 25bps to 3.50%. Money markets are pricing in a 97% chance for such a move and a just a 3% probability for a greater 50bps cut to 3.25%. The meeting will be the first in the post-Orr era after former Governor Orr suddenly resigned in March, three years before his term was set to end, while Deputy Governor Hawkesby was appointed as Acting Governor until a new Governor is appointed which is said to likely to be a six to nine-month process. As a reminder, the RBNZ delivered a third consecutive jumbo 50bps rate cut and its fourth straight rate reduction at the last meeting in February which was widely expected, while the central bank noted rates were reduced further as inflation abated and if economic conditions continued to evolve, there was scope to lower the OCR further in 2025. The RBNZ also stated that the committee has the confidence to continue lowering rates and economic activity remains subdued but noted that a recovery is expected over this year. Furthermore, the central bank cut its rate projections with the June 2025 forecast lowered to 3.45% from 3.83% and the March 2026 forecast was cut to 3.10% from 3.43%. The then Governor stated during the press conference that the OCR path projects 50bps of cuts by mid-year around July, in two 25bps steps, with cuts in April and May about right. Orr also commented the following day that he was feeling more positive about the inflation situation and expects the OCR will be around 3.00% by year-end, as well as noting there would have to be an economic shock to cut by 50bps again. Despite Orr’s departure, the remaining six members of the MPC are unlikely to deviate from the signalled rate path with rhetoric from officials very light since the last meeting, while recent GDP data also showed New Zealand’s economy exited a recession in Q4 which suggests the lack of urgency for another oversized rate cut.

RBI ANNOUNCEMENT (WED): RBI is forecast to continue cutting rates with the Repurchase Rate expected to be cut by 25bps to 6.00% after delivering a similar magnitude cut at the last meeting. However, money markets are pricing around an 82% chance of a greater 50bps cut and an 18% likelihood of a 25bps cut. As a reminder, the central bank unanimously decided to cut rates for the first time in almost five years at the February meeting which was the first policy decision under Governor Malhotra who took over the stewardship at the central bank in December, while the MPC was also unanimous in its decision to maintain a neutral policy stance. The RBI Governor noted at the policy address that average inflation has been lower since the introduction of the framework and that CPI has mostly stayed aligned with the target, barring a few occasions, as well as noted the global economic backdrop remains challenging. Furthermore, the central bank lowered its FY25 Real GDP growth forecast to 6.4% vs 6.6% previously but maintained its FY25 CPI inflation view at 4.8%. The data since then has shown a continued softening of CPI Inflation which slowed to 3.61% vs. Exp. 3.98% (Prev. 4.31%) to print below the central bank’s 4% target and effectively increased the scope for a further rate cut, while GDP for the December quarter accelerated but printed just short of estimates at 6.2% vs. Exp. 6.3% (Prev. 5.4%). Furthermore, recent global trade uncertainty with Trump tariffs and the newly announced US reciprocal tariff of 26% for India also supports the case for the central bank to continue to ease policy, while the appointment of former World Bank economist Poonam Gupta to replace former Deputy Governor Patra is seen by Bloomberg as strengthening the case for the RBI to step up its easing efforts with a potential 50bps cut.

REVIEWS

RBA REVIEW: RBA decided to maintain the Cash Rate at 4.10% which was unanimously expected given that the central bank had just delivered a cut at the last meeting in February and voiced cautiousness regarding future cuts. The language from the central bank provided little clues on future policy adjustments as it noted that the outlook remains uncertain, underlying inflation is moderating and sustainably returning inflation to target is the priority, while it also stated the board's assessment is that monetary policy remains restrictive. RBA also said that monetary policy is well placed to respond to international developments if they were to have material implications for Australian activity and inflation, as well as noted the continued decline in underlying inflation is welcome, but there are nevertheless risks on both sides with the board cautious about the outlook. Furthermore, it stated the board needs to be confident that this progress will continue so that inflation returns to the midpoint of the target band on a sustainable basis but acknowledged inflation could move in either direction. RBA Governor provided little clues on future policy during the post-meeting press conference where she noted the chance that there is more strength in the economy than seems and stated the board will continue to look at the data, while she added the board did not discuss a rate cut and has not made up its mind on a May move. Bullock also stated they are not endorsing the market path on future rate cuts and the board did not open the door to a May rate cut, as well as noted there is more economic data to come and updated forecasts for the May meeting.

ECB MINUTES REVIEW: As expected, given events over the past 24 hours, the account of the ECB's March meeting passed with little in the way of fanfare. In terms of the content, the point was made that the likely shocks on the horizon, including from escalating trade tensions, and uncertainty more generally, risked significantly weighing on growth. Furthermore, it was argued that these factors (escalating trade tensions, uncertainty) could increase the risk of undershooting the inflation target in the medium term. That being said, it was also argued that the combination of US tariffs and retaliation measures could also pose upside risks to inflation, especially in the near term. On net, the decision to lower rates was based on the judgement that the disinflation process remained well on track. Inflation had continued to develop broadly as staff expected, and the latest projections closely aligned with the previous inflation outlook. The GC's decision to change the wording of the monetary policy statement by replacing “monetary policy remains restrictive” with “monetary policy is becoming meaningfully less restrictive”, was widely seen as a reasonable compromise. However, it was considered important that the amended language should not be interpreted as sending a signal in either direction for the April meeting, with both a cut and a pause on the table, depending on incoming data.