

Global Central Banks Outlook

The Federal Reserve's position of no rate hike until 2024 will be increasingly difficult to reconcile with the data, the European Central Bank will likely look through rising inflation and the Bank of England is likely to slow the pace of purchases this year



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The outlook for central banks

European Central Bank

Higher headline inflation and bond yields combined with a disappointing start of the vaccination roll-out pose a new challenge for the ECB. However, higher inflation on the back of higher energy prices and one-off factors is not the kind of inflation the ECB has been looking for. To put a cap on bond yields, the ECB could be forced to frontload its asset purchases, engaging in a yield curve control of the GDP-weighted eurozone yield curve.

Federal Reserve

The economy has started 2021 strongly and with the vaccine program gaining momentum there is a realistic chance of a full 2Q re-opening. Strong household fundamentals, a housing boom and a vibrant manufacturing sector plus another \$1.9tn fiscal stimulus means 6%+ growth looks achievable while supply constraints makes 3%+ inflation readings likely. The Fed's position of no rate hike until 2024 will be increasingly difficult to reconcile while a QE taper looks likely late this year.

Bank of Japan

As recently as January, BoJ Governor Kuroda was mulling about letting JGB yields fluctuate in wider bands around their zero target rate. Though it doesn't seem as if the BoJ really has any appetite for the latest bond yield volatility which they actively resisted

Bank of England

Inflation is less of an issue in the UK, but recovery prospects mean the BoE appears relaxed about higher yields. We continue to doubt that negative rates will materialise later in 2022, despite policymakers asking banks to adjust systems to keep the option open.

China (PBoC)

The PBoC would not change 7D, 1Y and 5Y policy rates and RRR. It will maintain 7d market rates at 2% to 2.5% by managing daily liquidity. It can't tighten for deleveraging reform as external demand is yet to fully recovered under restrictive travels.

Bank of Canada

The BoC have tapered their weekly asset purchases from C\$5bn to C\$4bn per week, but refocused buying at the longer end of the curve. No further tapering is likely soon given recent Covid lockdowns while the BoC's guidance of a 2023 rate hike looks fair.

Reserve Bank of Australia

The RBA has kept both the cash rate and 3-yr yield target at 0.25%. 3-year yields have fallen steadily since early-Sept, requiring no additional asset purchases. A falling unemployment rate removes pressure for further incremental easing. We see no further easing this year.

Reserve Bank of New Zealand

The RBNZ is considering new tools including funding for lending (FLL), negative cash rate, and purchase of foreign assets. Of these, the FFL is likely to be ready to deploy first, and is more likely to be utilised either now or in the future compared to the other policies.

Riksbank

Inflation is not a major concern for Sweden, implying rate hikes are likely to be 2023 story at the earliest. Before then, a further QE expansion is possible if downside risks materialize, but a negative repo rate remains unlikely.

Swiss National Bank

The SNB is expected to keep rates unchanged at -0.75% and continues to use FX intervention to limit the appreciation of the franc when necessary. Fortunately, reflation is limiting FX pressure, making the SNB's task easier.

Norges Bank

NB remains something of a hawkish outlier, with rate hikes possible as early as 1H22. However like other parts of Europe, inflation prospects are likely to stay relatively benign.

Source: ING

✔ Federal Reserve

The economy has started 2021 strongly with the \$600 stimulus payments boosting consumer spending while manufacturing and the construction sector are firing on all cylinders. With the vaccine programme gaining momentum there is a realistic chance of a full 2Q reopening.

Household balance sheets are strong with high levels of savings and low levels of credit card debt meaning consumers have cash to spend. Significantly, this isn't just for high earners, with extended and uprated unemployment benefits and stimulus cheques clearly benefiting lower income households. With another \$1400 stimulus payment heading their way as part of President Biden's \$1.9tn fiscal package, 6%+ GDP growth looks achievable this year.

However, we anticipate some supply side capacity constraints in the service sector, which when faced with vigorous demand means 3%+ inflation readings are probable. Improved corporate pricing power and a roaring housing market could also make inflation somewhat sticky.

We suspect that the Fed's position of no rate hike until 2024 will be increasingly difficult to reconcile with the data flow while expectations of quantitative easing being tapered this year are likely to grow. We would imagine the Fed would incorporate a "twist" whereby they would lower the \$120bn of monthly purchases but focus them more towards the longer end of the Treasury curve.

✔ Bank of England

The Bank of England appears to be taking a leaf out of the Fed's book when it comes to the 50bp rise in yields we saw last month. Policymakers seem fairly relaxed so far, and in fact we think it's more likely that the pace of purchases is slowly lowered through the remainder of 2021 before the

BoE stops actively expanding its balance sheet at the end of this year. A further QE extension can't be ruled out if conditions warrant it, but it's not our base case. As for negative rates, we think this is a path the Bank is unlikely to cross, despite the operational planning steps being taken to enable the policy's usage from the autumn if needed. Several committee members remain unconvinced of the merits of negative rates, and in any case the economic outlook is unlikely to warrant a move given the improving economic outlook.

European Central Bank

Higher headline inflation and bond yields combined with a disappointing start of the vaccination rollout pose a new challenge for the ECB. The ECB's current rather benign approach to inflation will be put to the test in the coming months as inflation looks set to reach 2% in the summer months, in our view. However, higher inflation on the back of higher energy prices and one-off factors is not the kind of inflation the ECB has been looking for. Consequently, we expect the ECB to look through higher inflation, but only as long as higher bond yields do not undermine what the ECB calls "favourable financing conditions". To put a cap on bond yields, the ECB could be forced to frontload its asset purchases, engaging in a yield curve control of the GDP-weighted eurozone yield curve.

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