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THINK Ahead: Central banks and their distracted boyfriends

Central banks have lost their 'love' for inflation and only have eyes for growth. Faster rate cuts might be coming, especially in Europe, but does that mean they need to fall as far as markets think? James Smith thinks not. Read on! We've got viral trends and dubious memes as we look ahead to next week...

Central banks have lost interest in inflation and only have eyes for economic growth

Source: Shutterstock

Central banks and distracted boyfriends

The internet loves a meme, and none is more famous than the "distracted boyfriend". You know the one I mean: the guy checking out a woman as his outraged girlfriend looks on. And I'm here to tell you why it's the perfect analogy for central bankers right now.

As my potentially award-winning meme above suggests, central banks simply don't seem to care about inflation anymore. That was so last year! Policymakers on both sides of the Atlantic are becoming increasingly focused on one thing and one thing only: stopping recession.

The Fed's Powell has said that he doesn't think the jobs market is inflationary anymore. Not only that, he's made it clear that he doesn't welcome any further weakness in hiring. Fortunately for him, the latest jobs report that's hot off the press suggests that's not happening - yet.

An important moment from an influential hawk

Over in Europe, the ECB's Isabel Schnabel said this week that the Bank can't ignore the headwinds to growth. That felt like an important moment from one of Frankfurt's most influential hawks.

Inflation simply isn't in vogue right now, so next week's US CPI figures probably won't count for nearly as much as they did just a few months ago. James Knightley explains below why they should be relatively benign, anyway.

But here's the thing about trends: they have a habit of making a comeback. As Carsten writes, in this week's generally benign German inflation numbers, there are good reasons to think that inflation could rear its ugly head again further down the line.

The obvious candidate right now would be a sharp rise in oil prices. Nobody knows how the situation in the Middle East will unfold, but Warren Patterson writes that a hit to Iranian crude oil supply could take Brent crude above $90/bbl next year, while a more extreme escalation, and we're really talking hypotheticals here, via disruption in the Strait of Hormuz could take it to $150/bbl or above.

If that were to happen, how might central banks react? History suggests they tend to "look through" oil price spikes, focusing on the hit to growth over the impact on inflation. But recent experience tells us that's no longer necessarily true. A speech from the Bank for International Settlements this week recommends that central banks "lean more forcefully" against supply shocks in the future.

Oil prices may be outside of the control of central banks, but the fear is that inflation can more easily take hold against a backdrop of decarbonisation, reshoring and ageing populations. In the latter case, the post-pandemic era has demonstrated how a wave of early retirements and lower worker participation has the potential to drive up wage growth.

The dog's breakfast of a déficit croissant

Demographics matter for another reason, too: government budgets. France is in the headlines again as it struggles to get to grips with the dog's breakfast that is its *déficit croissant*. It's not the first national fiscal strategy to attract the unwanted attention of financial markets; trust me, I'm a weary UK economist. Crucially, it's unlikely to be the last.

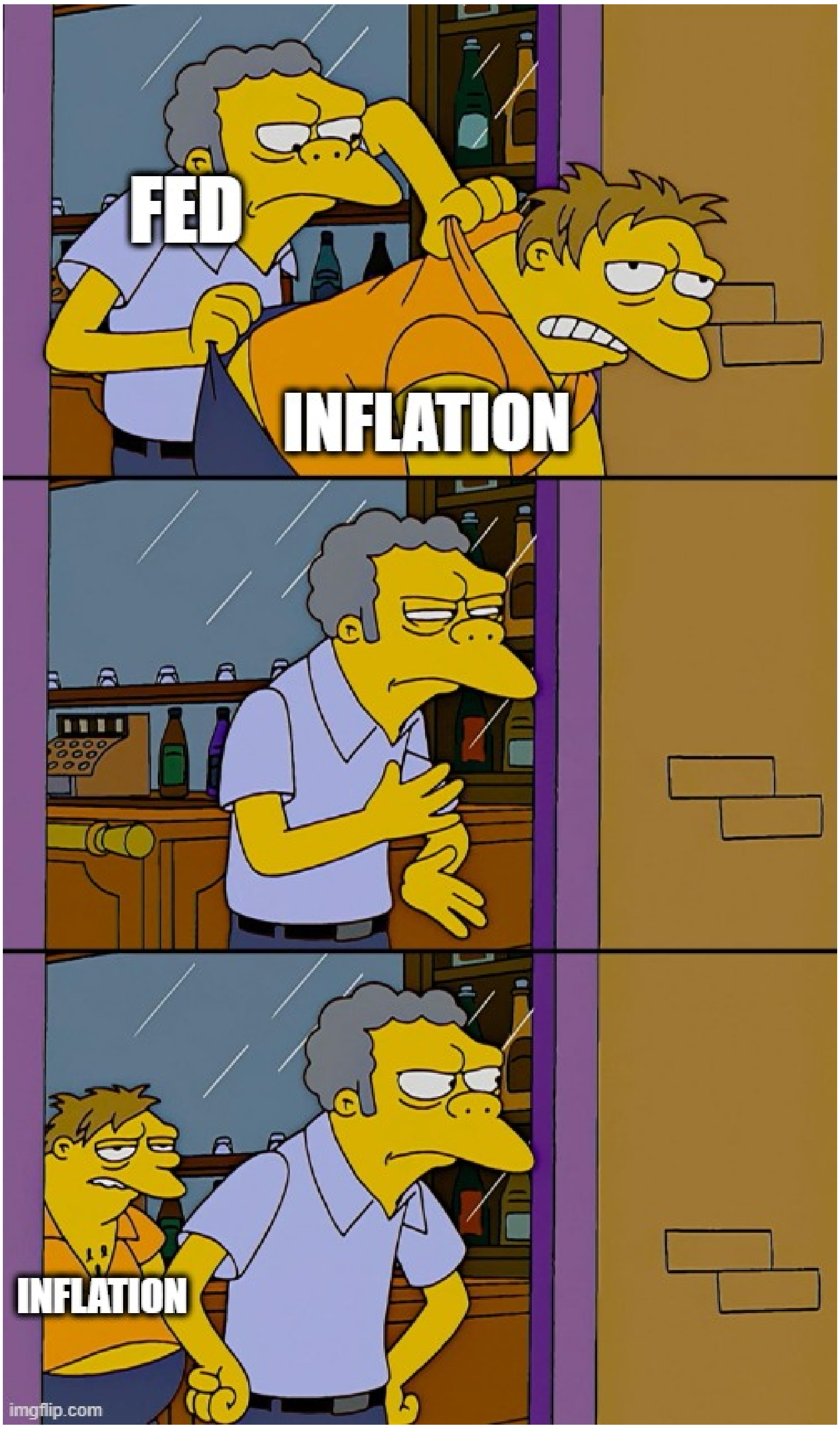
Just look at the US, which is running a deficit above 6% despite a healthy economy. Why? Well, as my colleagues have discussed, it's largely down to elevated spending on social security and healthcare. Those expenditures are only set to increase as the population ages. And it's a challenge that neither party in the forthcoming p[residential election is keen to discuss.

Without action, these sorts of fiscal deficits are set to keep central bank rates higher than we'd become accustomed to in the pre-pandemic years.

My point here is not to play down the concerns central banks have about growth. Far from it, I've argued recently that there's a decent case for moving quickly towards a "neutral" interest rate in a world where policy changes work more slowly than in the past.

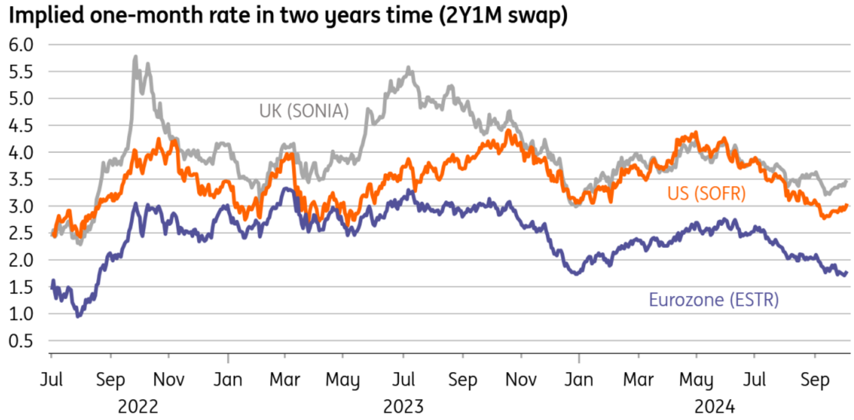
But two things can be true at once: central banks could conceivably cut rates more aggressively now, if the data tells them to, while stopping short of lowering them as far as investors expect. Don't forget that markets are now pricing rates below 3% in the US and below 2% in the eurozone. In the absence of a more severe recession, our base case is that rates are likely to stay higher than that.

Central banks might be bored with inflation right now, but let's just hope they don't end up with this...



Source: Imgflip

Chart of the week: Where markets see rates in two years



Source: Macrobond, ING calculations

THINK Ahead in developed markets

United States (James Knightley)

- **Inflation (Thu):** The market remains split on whether the Federal Reserve will cut the policy rate by 25bp or 50bp at the November FOMC meeting and next week's CPI report should keep both options on the table. After last month's hotter-than-predicted 0.3%MoM print for core inflation, the general sense is that it will revert to a 0.2% reading, which is what we need to see to keep the annual rate tracking towards the 2%YoY target. The annual headline rate should slow to just 2.3% from 2.5% YoY, which will also offer encouragement for those expecting the Fed to continue easing monetary policy towards what the Fed believes is the 3% long-run "neutral" rate. Also, watch out for the University of Michigan consumer sentiment report. There is growing evidence to suggest that households are noticing a cooling in the jobs market, which runs the risk that consumers will become more wary regarding their spending.

United Kingdom (James Smith)

- **August GDP (Fri):** The UK was one of the top performers in Europe during the first half of the year, growing by 1.5% across the first and second quarters. Like most of its neighbours, survey data suggests that the growth rate is unlikely to be sustained, and according to the monthly figures, we've seen two consecutive months of zero growth. We should return to modest growth in August, which would be consistent with a respectable 0.3% growth in Q3 as a whole.

THINK Ahead for Central and Eastern Europe

Hungary (Peter Virovacz)

- **Retail sales (Mon):** After a negative surprise in July, we don't expect August to be much better. This month has traditionally been weak for retail sales due to the holiday season. With anecdotal evidence suggesting that households tended to spend their holidays abroad, this may have had a negative impact on the sector's performance. We are looking for a monthly decline of 0.6%, resulting in retail sales volume growth of 2.1% YoY against a low base.

- **Inflation (Fri):** For the first time since early 2021, headline inflation will be at or below the National Bank of Hungary's inflation target. We see the September 2024 data coming in at 3.0% YoY after another month of flat monthly repricing. Fuel prices did the heavy lifting this time, explaining the full expected 0.4ppt deceleration in the year-on-year print. On the other hand, services inflation remains elevated at 9.4% YoY. As a result, core inflation won't change much, as we see it at 4.7% YoY. In isolation, such a reading would allow the NBH to cut the key rate again. However, with the recent HUF sell-off, this opportunity will be thrown out the window.

Czech Republic (David Havrlant)

- **Industrial output (Mon):** Czech industrial output likely continued its annual decline in August, when adjusted for the number of working days and seasonal effects, which is predominantly down to soft demand from the main European trading partners. Lukewarm support for Czech exports is about to be mirrored in a slightly more pronounced trade deficit in the same month. Still, the unemployment rate likely remained stable in September, as the layoffs in manufacturing were offset by hiring in the service sector.
- **Retail sales (Tue):** Real retail sales probably saw a robust annual expansion in August as consumers benefited from solid nominal and real wage dynamics. The current economic rebound is predominantly driven by strong household spending that has continued throughout the third quarter, reflected in stubborn price growth in the service sector and core inflation flying above the CNB forecast.
- **Inflation (Thu):** We expect consumer price growth to have picked up in September while remaining within the CNB tolerance band. Considering monthly changes, fuel prices are set to drag September's inflation down due to lower oil prices and a stronger Koruna in the same month. We also see lower regulated prices, as large energy distributors reduced end prices of electricity and natural gas at the beginning of September. Whether such a move will be fully recorded by the Statistical office is another question. Food prices represent a wild card that can surprise both upward and downward.

Key events in developed markets next week

Country	Time	Data/event	ING	Prev.
		Monday 7 October		
Germany	0700	Aug Industrial Orders (MoM%)	-1.0	2.9
France	0845	Sep FX Reserve Assets (EUR bn)	-	254.1
Eurozone	0845	ECB Lane Speech	-	-
		Tuesday 8 October		
US	1330	Aug Trade Balance (USD bn)	-72	-78.8
	1330	Aug Imports (USD bn)	-	345.4
	1330	Aug Exports (USD bn)	-	266.6
Germany	0700	Aug Industrial Output (MoM%/YoY%)	1.5/-3.3	-2.4/-5.3
France	0745	Aug Trade Balance (EUR bn)	-	-5.9
Canada	1330	Aug Trade Balance (CAD bn)	-	0.68
Netherlands	0530	Sep CPI (MoM%)	-	0.3
		Wednesday 9 October		
US	1900	FOMC Meeting Minutes	-	-
Germany	0700	Aug Trade Balance (EUR bn)	18.2	16.8
	0700	Aug Imports (MoM%)	-2.0	1.7
	0700	Aug Exports (MoM%)	-3.0	5.4
		Thursday 10 October		
US	1330	Sep Core CPI (MoM%/YoY%)	0,2/3,2	0.3/3.2
	1330	Sep CPI (MoM%/YoY%)	0,1/2,3	0.2/2.5
Norway	0700	Sep CPI (MoM%/YoY%)	-/-	-0.9/2.6
		Friday 11 October		
US	1330	Sep PPI (MoM%)	0.1	0.2
	1500	Oct Michigan Sentiment Flash	72	70.1
UK	0700	Aug GDP (MoM%)	0.2	0.0
Canada	1330	Sep Unemployment Rate	-	6.6

Source: Refinitiv, ING

Key events in EMEA next week

Country	Time	Data/event	ING	Prev.
		Monday 7 October		
Czech Rep	0800	Aug Trade Balance (CZK bn)	-4.4	-4.1
	0800	Aug Industrial Output (MoM%/YoY%, CASA)	0.3/-1.3	-0.9/-1.1
Hungary	0730	Aug Retail Sales (YoY%)	2.1	2.5
	0730	Aug Trade Balance (EUR mn)	200	167
		Tuesday 8 October		
Czech Rep	0800	Sep Unemployment Rate	-	3.8
	0800	Aug Real Retail Sales (MoM%/YoY%)	0.2/4.6	4.5
Hungary	0730	Sep Budget Balance (HUF bn)	-58.8	-414.4
		Wednesday 9 October		
Hungary	1300	Monetary Policy Meeting Minutes	-	-
		Thursday 10 October		
Turkey	0800	Aug Unemployment Rate	-	8.8
	0800	Aug Industrial Production (YoY%)	-	-3.9
Czech Rep	0800	Sep CPI (MoM%/YoY%)	-0.6/2.4	0.3/2.2
Hungary	0730	Sep CPI (MoM%/YoY%)	0.0/3.0	0.0/3.4
	0730	Sep Core CPI (YoY%)	4.7	4.6
Serbia	1100	Interest Rate Decision	5.75	5.75
		Friday 11 October		
Russia	1700	Sep CPI (MoM%/YoY%)	0.3/8.4	0.2/9.1
Turkey	0800	Aug Current Account Balance (USD bn)	4.5	0.566
Romania	0700	Sep CPI (MoM%/YoY%)	0.0/4.3	0.2/5.1
Serbia	1100	Sep CPI (MoM%/YoY%)	0.3/4.3	0.4/4.3
Kazakhstan	0800	Oct Base Interest Rate	14.25	14.25
	1400	Sep Industrial Production (YoY%)	-	3

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