Daiwa Securities

Daiwa's View

Pace of rate hikes in US and Europe to slow in December

- Concerns about wage-price spiral did not deepen in Europe
- BOJ is unlikely to adopt a surprising path for exit from YCC

Fixed Income Research Section
FICC Research Dept.

Chief Strategist
Eiichiro Tani, CFA
(81) 3 5555-8780
eiichiro.tani@daiwa.co.jp

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Pace of rate hikes in US and Europe to slow in December

Concerns about wage-price spiral did not deepen in Europe

◆ Pace of rate hikes at ECB and Fed to slow in December

At the wage hike negotiations that had been the focus of attention at the IG Metall union, the largest labor union in Germany, it was agreed last week that wages at the union in the Baden-Wuerttemberg state would be increased by 5.2% in 2023 and 3.3% in 2024. This includes temporary "inflation compensation" of €1,500. While the wage hikes are reasonable, they are not enough to cover the decline in real wages. Therefore, we think this will lower concerns about a wage-price spiral.

Since the October Governing Council meeting, the ECB has been communicating the message that the timing for suspending rate hikes is not that far off. This has led to the view that a consensus has formed that the ECB, together with the Fed, will slow rate hikes to 50bp in December. Moreover, the slowdown in the pace of rate hikes implies that interest rates are largely approaching "appropriate levels." The Fed's 4-4.5% and the ECB's 1.5-2% are not exactly appropriate levels, but the authorities probably think that interest rates are close to appropriate levels. While central banks are not backing down from their stance of raising rates for now, they are likely to implement slight adjustments as needed from next year onwards.

BOJ is unlikely to adopt a surprising path for exit from YCC

◆ Moody's* does not expect a surprise path regarding the BOJ's exit

According to media reports on 17 November, last week, a credit officer at US credit rating agency Moody's* in charge of Japanese sovereign bonds stated in an email that he expected any changes to the BOJ's monetary policy settings to be gradual and articulated well in advance. Generally speaking, credit rating officers have many opportunities to interview issuers, and issuers tend to tell the truth to avoid receiving undeserved ratings. In that respect, his response that he expects any changes to be articulated well in advance is worthy of special attention. This seems to have slightly strengthened the rationale for assuming that, if the BOJ were to make changes to the YCC, it is very likely that it would signal that in advance, rather than implementing a surprising rate hike or abruptly withdrawing from the YCC policy.

(*) indicates unregistered domestic rating; please see the disclaimer at the end.

That said, it almost speaks for itself that the BOJ will exclude any surprising paths during normalization of the YCC, given (1) that the Bank of Japan Act has set one of the Bank's objectives as "to ensure smooth settlement of funds among banks and other financial institutions, thereby contributing to the maintenance of stability of the financial system" and (2) past developments in which the Fed withdrew from the YCC. In either case, investors have little need to panic due to concerns about abrupt removal of the YCC and/or an abrupt change in the level of fixed-rate purchase operations. Therefore, all they have to do is to monitor signals from the BOJ carefully, and sell in fixed-rate purchase operations when the signal goes out from the BOJ.

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