

The Week Ahead: Strong US CPI inflation strengthens the case for higher terminal rate

► **US: February FOMC meeting minutes and PCE inflation in focus**

February's FOMC meeting minutes (due this week) might be slightly stale as incoming data released post-meeting showed strong economic activity in January (page 2). Robust hiring activity, solid retail spending and persistent core inflationary pressures indicate that the probability of a recession in the near term has decreased. However, the risk of prolonged high inflation has increased, which, in turn, could lead to a higher terminal rate than the current FOMC median dot-plot estimate of 5.1%. Fed members' communication since the policy meeting has also been more hawkish, with a number of participants flagging the need to raise rates more than previously envisaged. Two FOMC members, Loretta Mester and James Bullard (both non-voting members), have argued for a 50 bps rate hike at March's meeting, though this looks less likely, in our view. We now expect an additional 25 bps increase at the June meeting, on top of 25 bps each in March and May, which would take the terminal rate to 5.5%. The market is currently pricing in an additional 71 bps increase by July and has also pared back a potential rate cut. On the data side, January's PCE report will be watched for household activity and the Fed's preferred inflation gauge of core PCE deflator. Consensus expects the core PCE deflator to strengthen to 0.4% m-o-m in January (December: 0.3%), although the annual reading is seen decelerating marginally to 4.3% y-o-y (December: 4.4%), given the previous year's high base.

► **Japan: Kazuo Ueda nominated for BoJ Governor role**

Japan's government last week nominated Kazuo Ueda to succeed BoJ governor Haruhiko Kuroda after his term ends in April. It also nominated BoJ Executive Directors Shinichi Uchida and Ryoza Himino for deputy governor roles, replacing Masayoshi Amamiya and Masazumi Wakatabe. Parliament will hold a confirmation hearing on the nominated BoJ governor and deputies on 24 February. Consensus expects Ueda to maintain the BoJ's accommodative monetary policy but expects him to adopt a neutral stance on forward guidance, compared with the current dovish stance. Ueda is seen as a neutral outsider who can gradually steer the BoJ away from extremely accommodative monetary policy. That said, Kuroda will still head March's policy meeting. We expect an on-hold decision next month, although a tweak to the Yield Curve Control (YCC) cannot be ruled out entirely, given inflation strengthening to a multi-decade high of 4.0% in December.

► **Turkey: CBRT likely to cut policy rate to support economy**

We expect the CBRT to cut its benchmark one-week repo rate by 100 bps to 8.0% at its 23 February meeting to support the economy, which was recently hit by the severe earthquake. Even before the earthquake, at January's meeting, the CBRT removed its earlier guidance for a stable rate outlook, likely indicating the possibility of a rate cut before the scheduled general election in May. Meanwhile, the government has announced a TRY100 billion relief package for earthquake rescue efforts and has offered TRY10,000 for affected families.

Economics Team

Thirumalai Nagesh

Economist

+91 787 167 4887

Thirumalainagesh.ext@adcb.com

Sri Virinchi Kadiyala

Economist

+971 (0)2 697 3582

SriVirinchi.Kadiyala@adcb.com

Monica Malik, Ph.D.

Chief Economist

+971 (0)2 696 8458

Monica.malik@adcb.com

Contents

I.	Recent Events and Data Releases	2
II.	Economic Calendar	5

I. Recent Events and Data Releases

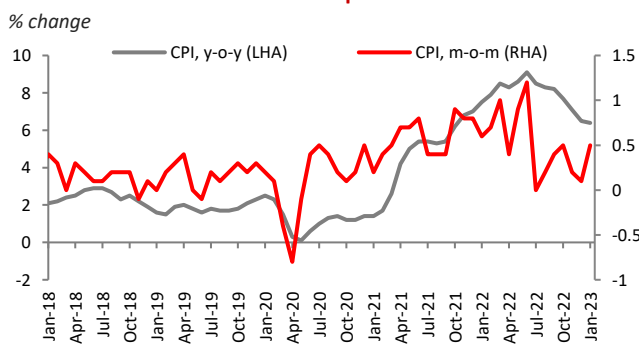
A. G4 Economies

US: Strong activity data supports higher-for-longer rate outlook

January’s CPI report was broadly in line with expectations, with the headline index rising 0.5% m-o-m (December: 0.1%), while core prices remaining steady at 0.4% m-o-m. As a result, headline inflation moved to 6.4% y-o-y (December: 6.5%, Consensus: 6.2%) and core CPI to 5.6% y-o-y (December: 5.7%). Food and energy prices rose sequentially, while price rises in core goods and services remained firm. The market remains focused on core inflation, which Fed Chair Powell stressed as key guidance for the future rate trajectory. The internals showed that the deflation seen in the core goods segment in recent months has ended, with the index edging up by 0.1% m-o-m, while the services index saw a firm price gain of 0.5% m-o-m in January. Details reveal that price rises in apparel, furnishings and medical commodities offset the decline in used car components. On the services side, rental price rises slowed slightly, although we expect some slowdown in this segment in the coming year, in line with private proxy trends. Worryingly, excluding shelter and medical costs, core services saw a broad-based increase, with transportation costs, education and recreation expenditure increasing firmly in January. In addition, the new weighting pattern released for 2023 last week detailed minor changes, including an increase in weightings assigned to ‘owners’ equivalent rent (OER)’, while reducing the weighting attributed to ‘used cars’. As both components are likely to be a source of disinflation in the coming year, they are unlikely to impact CPI’s trajectory significantly. Overall, while January’s CPI print is unlikely to have a material impact on the expected gradual disinflation in CPI over the course of the year, an upside surprise in PPI will likely lead to a firm PCE reading for the month, in our view.

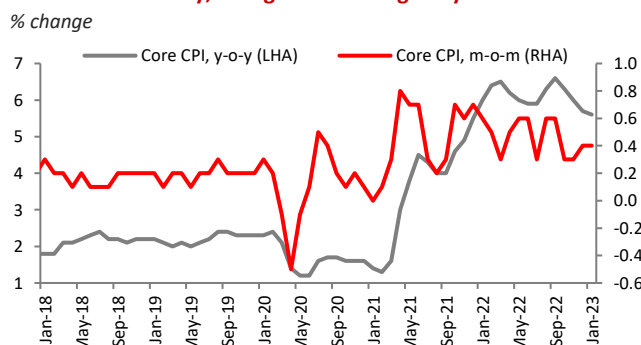
Headline inflation has risen in sequential terms, led by both food and energy

Fig. 1. US: Headline inflation strengthened sequentially with the rise in food and fuel prices



Source: Bureau of Labor statistics, ADCB Economic Research

Fig. 2. US: Core inflation remained steady in monthly terms in January, though eased marginally in annual terms



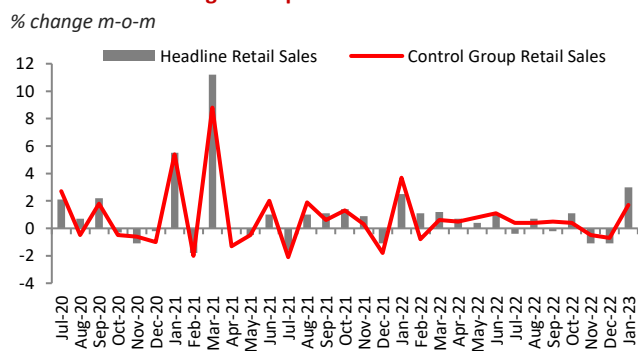
Source: Bureau of Labor statistics, ADCB Economic Research

Macroeconomic data remains supportive, with retail sales surprising to the upside in January (3.0% m-o-m vs consensus of 2.0% m-o-m), adding to the positive news delivered in the jobs report released earlier in the month. Indeed, the improvement in retail sales clearly suggests that the slowdown seen in November and December was an aberration, with a correction in seasonal factors boosting the January retail sales print. The auto sector was a key contributor, even as core retail sales registered a solid pace of expansion in January. Strong economic data and a slower disinflation trajectory lead us to expect three more 25 bps rate hikes from the FOMC during the current tightening cycle. As a

Retail sales growth rose to 3.0% m-o-m in January

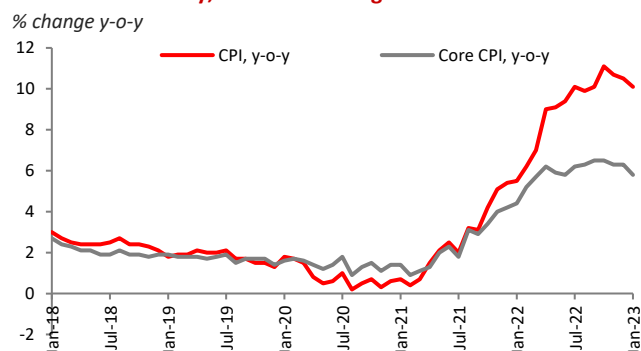
result, we now expect the Fed to increase its FFTR to a peak rate of 5.5% by June 2023. A slower disinflation path would mean the Fed is unlikely to contemplate rate cuts until the end of 2023, in our view.

Fig. 3. US: Retail activity rebounded in January after contracting in the previous two months



Source: US Census Bureau, ADCB Economic Research

Fig. 4. UK: Both headline and core inflation softened further in January, albeit remaining at elevated levels



Source: UK Office for National Statistics, ADCB Economic Research

UK: Softer services inflation pulls down CPI in January

January CPI surprised to the downside, printing at 10.1% y-o-y (December: 10.5%, consensus: 10.3%). Core inflation also softened to 5.8% y-o-y from 6.3% y-o-y. Transportation costs were the main driver of the downward surprise, even though there was a broad-based easing in price pressures across categories. Significantly, there are early signs that supply-side pressures in both goods and services are starting to ease. While most components saw a softening in inflation in January, alcoholic beverages, tobacco and spending on miscellaneous household goods and services were among the key contributors to the upside surprise. The statistical department also revised its weighting patterns for 2023, increasing its weightings to services and energy slightly, while trimming those relating to food and some non-energy goods. By themselves, they are unlikely to materially alter CPI's trajectory this year. Overall, CPI is on a gradual disinflation path but it still remains elevated and much higher than central bank comfort levels. In addition, wage pressures remain strong, much higher than those estimated to be consistent with the inflation target. Overall, we believe the Bank of England remains on track to raise its policy rate by 25 bps at its next policy meeting on 23 March.

BoE likely to shift down to 25 bps hike at March's meeting

B. Emerging Market Economies

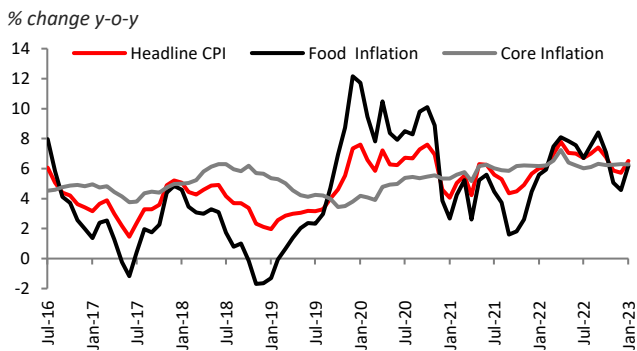
India: Upside surprise to CPI inflation sets stage for another rate hike

January CPI surprised significantly to the upside, strengthening the case for another rate hike at the next policy meeting in April. In January, CPI reversed its disinflation course and surged above the target band to 6.5% y-o-y (December: 5.7%, consensus: 6.0%), led by a sharp pick-up in food segment prices, while core inflation remains sticky at elevated levels. January CPI showed that 'cereals and products' was the key driver of the upside surprise, although more granular data suggests a discrepancy of about 20bp (downside) from the announced sub-category index figures. We await a final resolution to this from the statistical agencies. In contrast, the price declines seen in vegetables continued,

Headline inflation strengthens with the pick-up in food prices

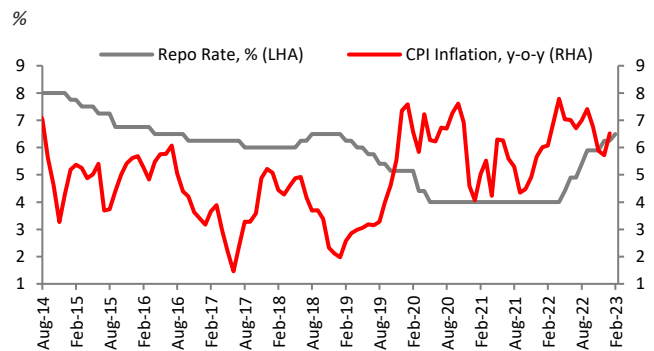
albeit at a softer pace than in previous months. Within the core inflation segments, higher gold prices pushed up prices of personal care and effects, while categories such as clothing and footwear, education and transportation costs saw a decline in inflation. However, as economic activity gains momentum in the coming months, resilient domestic activity and strengthening international commodity prices, including crude oil, could mean any moderation in core inflation would be very gradual.

Fig. 5. India: Food inflation strengthens in January, with the rise in cereal prices



Source: MOSPI, ADCB Economic Research

Fig. 6. India: Real repo stands at 0.0% following the upside surprise in January inflation reading



Source: RBI, MOSPI, ADCB Economic Research

Factoring in the January upside CPI surprise, retail inflation in Q1 2023 (Jan-March) looks set to overshoot the RBI’s 5.7% forecast last week. CPI overshooting the RBI’s target band (4% +/- 2%) strengthens the case for a further increase in policy rates at the RBI’s next meeting. Our base case is for one more 25 bps hike at April’s MPC meeting, taking the repo rate to 6.75%. However, we do see some upside risks if inflation continues to print higher than the RBI’s target band. As we have flagged in previous research, we believe that the hiking cycle is not yet over. Higher-than-expected inflation, relatively resilient growth and continued uncertainty on the external front suggest that the RBI will continue to tighten. Only signs of a durable reduction in core inflation may provide any relief to the relentless policy tightening, in our view.

We expect another 25 bps hike by the RBI at its April meeting

II. Economic Calendar

Fig. 7. The week ahead

Time*	Country	Event	Period	Prior	Consensus
Expected this week					
	UAE	M3 Money Supply, y-o-y	Dec	15.3%	
	Kuwait	CPI, y-o-y	Jan	3.15%	
	Bahrain	CPI, y-o-y	Jan	3.60%	
Monday, 20 February					
19:00	Eurozone	Consumer Confidence	Feb P	-20.9	-19.0
Tuesday, 21 February					
4:30	Japan	Jibun Bank Japan PMI Mfg	Feb P	48.9	
4:30	Japan	Jibun Bank Japan PMI Services	Feb P	52.3	
11:00	UK	PSNB, ex-Banking Groups	Jan	27.4B	
13:00	Eurozone	S&P Global Eurozone Manufacturing PMI	Feb P	48.8	49.3
13:00	Eurozone	S&P Global Eurozone Composite PMI	Feb P	50.3	50.6
13:30	UK	S&P Global/CIPS UK Manufacturing PMI	Feb P	47.0	47.5
13:30	UK	S&P Global/CIPS UK Services PMI	Feb P	48.7	49.2
18:45	US	S&P Global US Manufacturing PMI	Feb P	46.9	47.4
18:45	US	S&P Global US Services PMI	Feb P	46.8	47.3
18:45	US	S&P Global US Composite PMI	Feb P	46.8	47.5
19:00	US	Existing Home Sales	Jan	4.02M	4.1M
Wednesday, 22 February					
16:00	US	MBA Mortgage Applications	17-Feb	-7.7%	
23:00	US	FOMC Meeting Minutes	1-Feb		
Thursday, 23 February					
13:30	UK	BOE's Catherine Mann speaks			
14:00	Eurozone	CPI, y-o-y	Jan F	8.5%	8.6%
14:00	Eurozone	CPI Core, y-o-y	Jan F	5.2%	5.2%
14:45	UK	BOE's Jon Cunliffe speaks			
15:00	Turkey	One-Week Repo Rate	23-Feb	9.0%	8.0%
17:30	US	GDP Annualized, q-o-q	4Q S	2.9%	2.9%
17:30	US	Personal Consumption	4Q S	2.1%	2.0%
17:30	US	GDP Price Index	4Q S	3.5%	3.5%
17:30	US	Core PCE, q-o-q	4Q S	3.9%	3.9%
17:30	US	Initial Jobless Claims	18-Feb	194K	199K
17:30	US	Continuing Claims	11-Feb	1696K	1701K
19:50	US	Fed's Bostic Discusses Fed's Role in the Banking System			
23:00	US	Fed's Daly to Speak on Leadership			
Friday, 24 February					
3:30	Japan	Natl CPI, y-o-y	Jan	4.0%	4.3%
3:30	Japan	Natl CPI, ex-Fresh Food, y-o-y	Jan	4.0%	4.3%
4:01	UK	GfK Consumer Confidence	Feb	-45.0	-43.0
17:30	US	Personal Income	Jan	0.2%	1.1%
17:30	US	Personal Spending	Jan	-0.2%	1.3%
17:30	US	PCE Deflator, m-o-m	Jan	0.1%	0.5%
17:30	US	PCE Deflator, y-o-y	Jan	5.0%	5.0%
17:30	US	PCE Core Deflator, m-o-m	Jan	0.3%	0.4%
17:30	US	PCE Core Deflator, y-o-y	Jan	4.4%	4.3%
19:00	US	New Home Sales	Jan	616K	620K
19:00	US	U. of Michigan Sentiment	Feb F	66.4	66.4
19:15	US	Fed's Jefferson discusses paper on managing disinflation			
20:30	UK	BOE's Tenreyro speaks			
22:30	US	Fed's Collins gives recorded remarks at US Monetary Policy			
22:30	US	Fed's Waller discusses inflation			

*UAE time

Source: Bloomberg, ADCB Economic Research

Fig. 8. Last week's data

Time*	Country	Event	Period	Prior	Consensus	Actual
GCC Economies						
	Qatar	CPI, y-o-y	Jan	5.9%		4.2%
	Oman	CPI, y-o-y	Jan	2.0%		1.9%
Monday, 13 February						
16:00	India	CPI, y-o-y	Jan	5.7%	6.0%	6.5%
Tuesday, 14 February						
3:50	Japan	GDP Annualized SA, q-o-q	4Q P	-0.8%	2.0%	0.6%
3:50	Japan	GDP SA, q-o-q	4Q P	-0.2%	0.5%	0.2%
11:00	UK	Average Weekly Earnings, 3M/y-o-y	Dec	6.4%	6.2%	5.9%
11:00	UK	Weekly Earnings, ex-Bonus, 3M/y-o-y	Dec	6.4%	6.5%	6.7%
11:00	UK	ILO Unemployment Rate, 3M	Dec	3.7%	3.7%	3.7%
14:00	Eurozone	GDP SA, q-o-q	4Q P	0.1%	0.1%	0.1%
14:00	Eurozone	GDP SA, y-o-y	4Q P	1.9%	1.9%	1.9%
15:00	US	NFIB Small Business Optimism	Jan	89.8	91.0	90.3
17:30	US	CPI, m-o-m	Jan	-0.1%	0.5%	0.5%
17:30	US	CPI, ex-Food and Energy, m-o-m	Jan	0.3%	0.4%	0.4%
17:30	US	CPI, y-o-y	Jan	6.5%	6.2%	6.4%
17:30	US	CPI, ex-Food and Energy, y-o-y	Jan	5.7%	5.5%	5.6%
Wednesday, 15 February						
5:20	China	1-Yr Medium-Term Lending Facility Rate	15-Feb	2.75%	2.75%	2.75%
8:30	Japan	Tertiary Industry Index, m-o-m	Dec	-0.2%	0.1%	-0.4%
10:00	Saudi Arabia	CPI, y-o-y	Jan	3.3%		3.4%
11:00	UK	CPI, m-o-m	Jan	0.4%	-0.4%	-0.6%
11:00	UK	CPI, y-o-y	Jan	10.5%	10.3%	10.1%
11:00	UK	CPI Core, y-o-y	Jan	6.3%	6.2%	5.8%
17:30	US	Empire Manufacturing	Feb	-32.9	-18.0	-5.8%
17:30	US	Retail Sales Advance, m-o-m	Jan	-1.1%	2.0%	3.0%
17:30	US	Retail Sales Control Group	Jan	-0.7%	1.0%	1.7%
18:15	US	Industrial Production, m-o-m	Jan	-0.7%	0.5%	0.0%
Thursday, 16 February						
3:50	Japan	Trade Balance	Jan	-1451.8B	-3976.7B	-3496.6B
3:50	Japan	Core Machine Orders, m-o-m	Dec	-8.3%	2.8%	1.6%
17:30	US	Building Permits	Jan	1337K	1350K	1339K
17:30	US	Housing Starts	Jan	1382K	1356K	1309K
17:30	US	Initial Jobless Claims	11-Feb	196K	200K	194K
17:30	US	Continuing Claims	4-Feb	1688K	1695K	1696K
17:30	US	Philadelphia Fed Business Outlook	Feb	-8.9	-7.5	-24.3
17:30	US	PPI Final Demand, m-o-m	Jan	-0.5%	0.4%	0.7%
17:30	US	PPI Final Demand, y-o-y	Jan	6.2%	5.4%	6.0%
Friday, 17 February						
11:00	UK	Retail Sales Inc Auto Fuel, m-o-m	Jan	-1.2%	-0.3%	0.5%
11:00	UK	Retail Sales Inc Auto Fuel, y-o-y	Jan	-6.1%	-5.6%	-5.1%
17:30	US	Import Price Index, m-o-m	Jan	-0.1%	-0.1%	-0.2%
19:00	US	Leading Index	Jan	-0.8%	-0.3%	-0.3%

*UAE time

Source: Bloomberg, ADCB Economic Research

This report is intended for general information purposes only. It should not be construed as an offer, recommendation or solicitation to purchase or dispose of any securities or to enter in any transaction or adopt any hedging, trading or investment strategy. Neither this report nor anything contained herein shall form the basis of any contract or commitment whatsoever. Distribution of this report does not oblige Abu Dhabi Commercial Bank PJSC (“ADCB”) to enter into any transaction.

The content of this report should not be considered legal, regulatory, credit, tax or accounting advice. Anyone proposing to rely on or use the information contained in the report should independently verify and check the accuracy, completeness, reliability and suitability of the information and should obtain independent and specific advice from appropriate professionals or experts regarding information contained in this report.

Information contained herein is based on various sources, including but not limited to public information, annual reports and statistical data that ADCB considers accurate and reliable. However, ADCB makes no representation or warranty as to the accuracy or completeness of any statement made in or in connection with this report and accepts no responsibility whatsoever for any loss or damage caused by any act or omission taken as a result of the information contained in this report.

Charts, graphs and related data or information provided in this report are intended to serve for illustrative purposes only. The information contained in this report is prepared as of a particular date and time and will not reflect subsequent changes in the market or changes in any other factors relevant to their determination. All statements as to future matters are not guaranteed to be accurate. ADCB expressly disclaims any obligation to update or revise any forward looking statements to reflect new information, events or circumstances after the date of this publication or to reflect the occurrence of unanticipated events.

This report is being furnished to you solely for your information and neither it nor any part of it may be used, forwarded, disclosed, distributed or delivered to anyone else. You may not copy, reproduce, display, modify or create derivative works from any data or information contained in this report.

...