

Rate cuts, hikes and pauses: The world's central banks just made very different decisions

By Silvia Amaro

From hawkish pauses to rate hikes and dovish tones, the world's biggest central banks last week struck very different tones on monetary policy.

The European Central Bank on Thursday hiked rates and surprised markets with a worsening inflation outlook, which led investors to price in even more rate increases in the euro zone.

This followed a Federal Reserve meeting where the central bank decided to pause rate hikes. Just days before that, China's central bank lowered its key medium-term lending rates to stimulate the economy. In Japan, where inflation is above target, the central bank has left its ultra-loose policy unchanged.

"Taking all these different approaches together shows that not only seems there to be a new divergence on the right approach for monetary policy but it also illustrates that the global economy is no longer synchronized but rather a collection of very different cycles," Carsten Brzeski, global head of macro at ING Germany, told CNBC via email.

In Europe, inflation has come down in the bloc which uses the euro but remains well above the ECB target. This is also the case in the U.K., where the Bank of England is expected to raise rates Thursday after very strong labor data.

The Fed, which started its hiking cycle before the ECB, decided to take a break in June — but said there would be another two rate increases later this year, meaning its hiking cycle is not yet complete.

The picture is different in Asia, however. China's economic recovery is stalling, with falls in both domestic and external demand leading policymakers to step up support measures in an effort to revive activity.

In Japan — which has battled a deflationary environment for many years — the central bank said it expects inflation to come down later this year and opted not to normalize policy yet.

"Each central bank [tries] to solve for its own economy, which obviously includes considerations for changes in financial conditions imposed from abroad," Erik Nielsen, group chief economics advisor at UniCredit said via email.

Market impact

The euro rose to a 15-year high against the Japanese yen on Friday, according to Reuters, off the

back of the divergent monetary policy decisions. The euro also broke above the \$1.09 threshold as investors digested the ECB's hawkish tone last Thursday.

In bond markets, the yield on the German 2-year bond hit a fresh 3-month high Friday, given expectations that the ECB will continue with its approach in the short term.

"Makes sense we start seeing this divergence. In the past, it was clear there was a lot of room to cover for pretty much all the major central banks, while now, given the different stages the jurisdictions are in the cycle, there will be more nuanced decisions to be made," Konstantin Veit, portfolio manager at PIMCO, told CNBC's Street Signs Europe on Friday.

"This indeed will create opportunities for the investors."

ECB President Christine Lagarde was asked during a press conference to compare her team's decision to increase rates, versus the Federal Reserve's decision to pause.

"We are not thinking about pausing," she said. "Are we done? Have we finished the journey? No, we are not at [the] destination," she said, pointing to at least another potential rate hike in July.

For some economists, it is only a matter of time before the ECB finds itself in a similar position to that of the Fed.

"The Fed is leading the ECB [as] the U.S. economy is leading the eurozone economy by a few quarters. This means that, at the latest after the September meeting, the ECB will also be confronted with the debate on whether or not to pause," Brzeski said.