

Preview - BoC Policy Announcement

50bps cut expected with risk of a smaller 25bp move

- BoC rate decision, MPR and Governor Macklem text to be released at 14:45 BST / 09:45 EDT; Press conference and Q&A at 15:30 BST / 10:30 EDT
- Focus is on the magnitude of the rate cut.
- Money markets and the majority of analysts expect a 50bps move but some look for a 25bp cut.

SUMMARY: The Bank of Canada is expected to cut rates by 50bps to 3.75% on Wednesday, according to 19/29 analysts surveyed by Reuters, while 10 analysts look for a smaller 25bps rate cut. Alongside the rate decision, the latest Monetary Policy Report will be released as well as a speech from Governor Macklem. Remarks from BoC Governor Macklem on 10th September, a week after the BoC cut by 25bps for the third consecutive time, stated that bigger cuts are possible if the economy and CPI are weaker. The August inflation data was soft, although a strong September jobs report saw money markets price a 25 or 50bps move as a near-coin flip. Thereafter, the September inflation data was notably softer than forecast and 50bps bets ramped up, supported by the latest Business Outlook Survey showing firms expect prices and wage growth to soften further. As things stand, money markets are pricing in c. 48.5bps of easing at the upcoming meeting, implying a 94% probability of a 50bps reduction. The focus of the meeting will largely be on the rate decision, however, the statement and MPR will be eyed for guidance and how the BoC is explaining the recent soft inflation data. We will also look to the MPR for the BoC's economic forecasts.

RATES: According to the Reuters survey, the BoC is expected to cut rates by 50bps, taking its rate to 3.75%. Within the poll, 19/29 analysts surveyed expect this to be the case, with the remaining 10 expecting a 25bps cut to 4.00%. Money markets are largely pricing in a 50bps rate cut with a 94% probability, with just a 6% probability of a 25bps move - therefore there is room for reaction if the BoC were to surprise with a 25bps rate cut, given the pricing for 50. Meanwhile, ING highlights that if the BoC does go ahead with the 50bps decision, it would widen the spread with the Fed funds target rate to 125bps and this may put additional downside pressure on the CAD. Looking ahead, through year-end money markets are fully pricing in 75bps of easing, implying one 50bps rate cut in October and one 25bps rate cut in December, with only a 16% probability priced for back-to-back 50bps moves. Meanwhile, the Reuters poll found that there was no clear consensus on what the BoC will do at the December meeting, 10/29 expect rates to finish the year at 3.50%, nine expect rates to be at 3.75%, while one analyst sees rates at 4.00% from the current 4.25%.

MPR: The monetary policy report will also be eyed to see the updated forecasts from the BoC after the batch of recent data which saw soft inflation figures and a strong jobs report. The prior MPR was released in July, which left 2024 CPI unrevised, but raised its 2025 forecast. There may be revisions lower to the 2024 CPI due to the recent string of soft inflation, but if the BoC becomes more aggressive with its easing it may have an inflationary impact in the future. Growth forecasts for 2024 and 2025 were cut, and since then Q2 GDP has been stronger than the street consensus and above the BoC's forecast in July.

DATA: The most recent inflation data saw a slight tick up in the BoC Core measures to 2.26% from 2.20%, but still remains near the BoC's target. However, the headline measures were notably softer than expected with inflation at 1.6%, beneath the 1.8% forecast. The September jobs report was strong however, with the unemployment rate ticking down to 6.5% from 6.6% while the net jobs added of 47k was largely led by a 125k increase in full-time jobs. Looking ahead, the BoC Business Outlook Survey noted business sentiment remains subdued, while excess capacity is leading to restrained investment and hiring. Firms also expect both wage and price growth to soften. Analysts at RBC note that the recent soft inflation data, coupled with the BOS, has led them to expect a 50bps rate cut at the upcoming meeting.

COMMENTARY: The highlight of recent BoC commentary was from Governor Macklem, who noted that bigger cuts are possible if the economy and CPI are weaker, opening the door to a 50bps rate cut. Also, ahead of the US election, Macklem was cautious on US-Canada trade, noting anything that disturbed their relationship could have a very significant effect on the Canadian economy, adding if they saw a big change in layoffs, that would be a cause for concern. Since the remarks, the inflation data has been softer than expected as mentioned above, while the labour market report was strong. The inflation data supports the argument for a 50bps move but the labour market would likely support the case for a 25bps reduction, while the BoC Business Outlook Survey could support the case for the larger 50bps move, given firms expect both wage and price growth to soften further with inflation already around target levels.

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