

PREVIEW: BoC rate decision, MPR and presser due Wednesday 29th January 2025

- **BoC rate decision, MPR and Macklem text to be released at 14:45GMT/09:45EST**
- **Press conference at 15:30GMT/10:30EST**
- **Focus on commentary around potential impact of Trump tariffs**

SUMMARY: The BoC is expected to cut rates by 25bps, taking the target for the overnight rate to 3.00%, according to the majority of analysts surveyed by Reuters, although some look for rates to be left on hold. Money markets are pricing in a 25bps cut as a near certainty with a slowing economy, high unemployment rate and looming trade tariffs (which would further dampen economic growth) supporting the case for a cut. However, some could argue the cases for a hold include the BoC approaching the neutral rate, inflation already around target, and a weakening CAD. Nonetheless, the BoC are more widely focused on economic growth and the threat of tariffs from the US bolsters the case for a cut with the Canadian economy already slowing. We will also get an updated the Monetary Policy Report and economic forecasts, with participants cognizant of the BoC's estimated economic impacts of tariffs from the US, albeit the tariffs have not yet been officially enacted.

EXPECTATIONS: The Bank of Canada is expected to cut rates by 25bps to 3.00% on Wednesday 29th January, according to 25 out of 31 analysts, with the rest expecting a pause. The poll was conducted between January 10-16th, before the December inflation and BoC Business and Consumer Outlook survey, which ultimately saw soft inflation metrics and a subdued outlook survey. At the prior meeting, alongside a 50bps rate cut, the BoC signalled a slowdown of easing ahead following 175bps of easing, and two back-to-back 50bps rate cuts. This has taken the target for the overnight rate to 3.25%, matching the upper-end of the BoC's own estimate of the neutral rate (2.25-3.25%). We will also see the updated MPR for growth and inflation forecasts, as well as its own estimate of the neutral rate. This time around there will be plenty of focus on the economic forecasts to gauge the BoC's views of potential impact of US President Trump's proposed 25% tariffs for Canada and Mexico. Nonetheless, given the tariff threat is a proposal, it is yet to be confirmed and the BoC may not want to front-run trade policy, but any commentary around trade and the impact of tariffs will be key.

TRUMP TARIFFS: US President Trump has threatened 25% tariffs on Canada and Mexico, in which Canada has announced it will respond with tit-for-tat measures. ING points out that the US is Canada's most important trading partner, taking in 76% of Canada's exports with the value equivalent to around 20% of Canadian GDP. ING says, "The proposed tariffs will undoubtedly hurt the competitiveness of Canadian products with the clear risk that substitution away from Canadian-sourced items leads to an economic downturn." Meanwhile, in regards to a response around retaliatory tariffs on US exports into Canada, ING notes that around 65% of Canadian imports come from the US. This may push up price levels for Canadian consumers and prompt faster inflation, while recent weakness in CAD on a trade weighted basis adds to price pressures through higher imported prices and is a key reason why ING expects just a 25bps cut this week. The desk notes that until there is clarity on what is happening on US-Canada trade policy, the BoC is likely to tread carefully. In terms of reaction, ING highlights that the BoC plays a secondary role for the Loonie, with the focus all on Trump tariffs. The desk writes, "Should Trump scale back the tariff threat, then there is an approximate 2% downside room to cover for USD/CAD. Should tariffs be imposed in the near term, we expect a dovish repricing in BoC expectations to compound with a greater risk premium and take USD/CAD well above 1.45."

RECENT DATA: The December inflation data was softer than expected with the average of the three BoC core measures at 2.3%, within the 1-3% target range, and close to the centre - which will be a welcome sign for the BoC. Although a soft report, analysts highlighted the details suggest a higher-than-expected proportion of the GST break was captured by the data. Overall, cooling inflation and a slowing economy support the case for more easing, although there is tremendous uncertainty with the threat of Tariffs from US President Trump overhanging the economy, to which Canada has vowed to respond with tit-for-tat measures. The labour market has seen the unemployment rate grind higher recently although the December jobs report was more encouraging with the unemployment rate dipping to 6.7% from 6.8%, despite expectations for a further rise to 6.9%. On growth, ING highlighted that activity has been disappointing with Q4 GDP expected to come in at 1.5% after 1% in growth in Q3. Meanwhile, the BoC Outlook Survey saw overall subdued sentiment. Regarding the outlook, 20% of firms expect inflation to be above 3% for next 2 years, up from 15% in Q3, while 15% of firms expect Canada to be in a recession over the next year, down from 16% in Q3. The consumer survey saw 46.5% of Canadians expect a recession, down from 49%, while the consumer 5yr inflation expectations eased marginally to 2.99% from 3.03%. However, it is worth bearing in mind the Outlook Surveys took place between 7-27th November 2024, before the BoC's 50bps rate cut in December, while some respondents wouldn't have known about the Trump Tariff threat on 25th November.

RECENT COMMENTARY: There hasn't been much commentary from officials since the prior BoC meeting, although Deputy Governor Gravelle noted a Trump tariff on exports would have a big negative impact on economic growth. He also warned there would likely be an inflation impact at the same time they have a slowdown in the economy, so that puts a central bank in a very complicated space. Gravelle also spoke on the end of QT, noting for it to end now, the BoC thinks they need settlement balances in a range of CAD 50-70bn, up from last year's CAD 20-60bn estimate. He also said he expects to announce the end of QT in the first half of the year, so any commentary around this from the BoC will also be eyed - although it may be more prominent in the minutes if there was any discussion around it.