Central Bank Weekly - 7th March 2025: Previewing BoC; Reviewing ECB, RBA Minutes and CBRT

PREVIEWS

BOC ANNOUNCEMENT (WED): The Bank of Canada is likely to cut rates by a further 25bps, taking the target for the overnight rate to 2.75%. A 25bps rate cut is currently priced with a c. 70% probability, with a 30% probability for rates to be left unchanged. The BoC's main focus right now is on the impact of tariffs from the US, and although inflation has been ticking up recently (BoC eyed measure at 2.53%, prev. 2.36%), the economic slowdown expected ahead from the impact of tariffs is the clear focus of the BoC. Governor Macklem acknowledged that if US tariffs are long-lasting and broad-based, there will not be a bounce back in the Canadian economy. He noted that the updated BoC model shows Canadian output would fall almost 3% over two years if the US imposed tariffs, all but wiping out growth forecasts for 2025 and 2026. It also shows that exports would fall 8.5% in the year after tariffs took effect. As it stands, Trump has delayed the fentanyl related tariffs by one month until 2nd April on all products that comply with the USMCA trade agreement, but those that are not compliant, are still subject to tariffs. However, from April 2nd, if Trump is not satisfied with progress on reducing the flow of fentanyl into the US, the tariffs will go ahead, alongside the planned reciprocal tariffs that are set to be enforced from the same date. The prior BoC meeting saw the bank cut by 25bps to 3.00% as expected, it also announced the end of QT and removed forward guidance, leaving future decisions open to a pause or cut, depending on the information available to them at the time.

REVIEWS

RBA MINUTES: RBA released the Minutes from its February meeting where the central bank delivered a widely expected 25bps rate cut to lower the Cash Rate to 4.10% which was the central bank's first rate reduction since 2020. However, the release of the Minutes lacked any major fireworks and adhered to the cautious message regarding further rate cuts. The Board judged the case to cut rates was, on balance, the stronger one although it agreed the decision did not commit them to further cuts in the cash rate and members expressed caution about the prospect of further easing. Elsewhere, members placed more weight on the downside risks to the economy and were particularly mindful of the risk of keeping policy too tight for too long, while it was also stated that if inflation proved persistent, rates might stay at 4.1% for an extended period or be raised. Furthermore, the strongest argument for cutting rates was the slowdown in inflation and wages, although the Board also considered three main reasons for keeping rates unchanged with strength in the labour market the strongest reason for holding steady. It was also possible that policy was not as restrictive as thought, or that the economy could pick up quicker than expected, while it also stated that US trade policy could have a material adverse effect on business investment and household consumption.

ECB ANNOUNCEMENT: As expected, the ECB pulled the trigger on a 25bps reduction to the Deposit Rate, taking it to the upper limit of the estimated neutral range. Greater attention fell upon the Governing Council's decision to tweak its policy statement so that it reads "monetary policy is becoming meaningfully less restrictive" (prev. "monetary policy remains restrictive"). Elsewhere, the Bank opted to reiterate its data-dependent and meeting-by-meeting approach, whilst stating that it will not pre-commit to a specific policy path. For the accompanying macro projections, the headline 2025 inflation forecast was raised to 2.3% from 2.1%, 2026 held at 1.9% and 2027 trimmed to 2.0% from 2.1%. On the growth front, policymakers cut their 2025 and 2026 growth views whilst holding 2027 at 1.3%. At the follow-up press conference, President Lagarde remarked that the statement language tweak was not an innocuous change and word changes have meaning. She added that the ECB is now moving towards a more 'evolutionary approach'. With regards to the policy decision, all policymakers, with the exception of Austria's Holzmann (who abstained) backed the announcement. In terms of where the ECB goes from here, Lagarde suggested that the GC could cut again or pause its cutting cycle depending on the data. The fact that Lagarde classified the policy discussion as "lively" and "intense" suggests upcoming decisions will become more contentious. Overall, the ECB's policy path is an incredibly uncertain one with Lagarde suggesting that the Bank needs time to assess recent fiscal announcements from the EU and Germany, whilst also awaiting clarity on the Trump tariff regime. As such, policymakers appear to be buying for time before committing to their next move.

ECB SOURCES: In wake of the meeting, ECB sources hit, with Bloomberg reporting that officials see an April showdown on whether to cut rates again, similar to what Reuters reported. The Reuters sources affirmed there was a wide range of discussions at the ECB due to uncertainty ahead. It stated the chance of a cut in April (the next meeting) is growing and that the current rate of 2.5% is unlikely to be the bottom of the cycle. It also noted that there is a growing chance for a pause before rates continue lower. The key variables included trade policy, and whether the US imposed tariffs on EU, that would raise the chance of more cuts, but an EU retaliation would blur the picture, raising the risk of stagflation. The sources also acknowledged that if Germany were to push through with its proposed military and infrastructure plans, that would raise growth and inflation, making a cut in April less likely. Meanwhile, the sources also noted how the final wording of the ECB's new guidance that rates were "meaningfully less restrictive", was a compromise in the lead-up to the meeting, where some had wanted to maintain prior reference to policy, but others argued for removing that word. Looking ahead, a 25bps cut in April is priced at around 44% with a total of 43bps of loosening seen by year-end vs. circa 45bps pre-ECB.

CBRT ANNOUNCEMENT: The CBRT lowered its policy rate by 250bps to 42.5% as expected. In the accompanying statement, it noted that going forwards, increased coordination of fiscal policy will also contribute to the process of price stability. They justified this cut by emphasising the improvement in underlying inflation trend and domestic demand, and in addition to this, the central bank reiterated their commitment to a meeting-by-meeting basis. Looking forward, BBVA expects another 250bps cut in April, which would be the fourth cut in a row, and the pace of rate cuts to decelerate June onwards, reaching 31.5% policy rate by end 2025.