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Bank of Canada: A Threepeat Quarter Point Cut

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It's said that victory goes to the bold, but the Bank of Canada went with the more cautious approach of yet another quarter point rate cut. That left rates still well above where they will have to head to get the economy and labour markets into better shape, which the Bank say it wants to do as inflation becomes less of a threat. While markets had put small odds on a 50 bp move, the Bank still cited two-sided risks to inflation, while noting that June/July data suggest downside risks to their growth outlook.. For now, we're calling for two more 25 bp moves this year, enroute to a roughly 2 1/2% overnight rate next year, but a disappointment in upcoming jobs data could still compel a bolder pace of easing, as could the need for a significant forecast downgrade in the October MPR. The Governor said they discussed scenarios in which they would cut faster or slower, but also hinted that the summary of deliberations could reveal more on what they discussed.

- The statement announcing the cut, as well the opening remarks in the press conference, were mostly a recitation of publicly-available facts. That contrasted somewhat with some prior meetings, in which the press conference statement gave some insights into what the Governing Council deliberated over in terms of the policy decision. This blander approach might have been influenced by a desire to keep their cards closer to their chest ahead of employment data and a Fed rate decision in upcoming days. By the time they release the summary of deliberations on September 18th, they might be prepared to give more insights into their thinking.
- Mentioning two-sided risks to inflation seems a bit at odds with the Bank's statement that if things evolve as they expect, further rate cuts would be likely. So while there may be still residual concerns about inflation, their base case is clearly one in which economic slack will push it lower, which the Governor underscored in his press conference remarks. The Bank cites shelter inflation as one item on the high side, but part of that is capturing renewals of mortgages at higher interest rates, and rate cuts would provide relief on that front. Rent inflation also seems to be turning the corner, and over the medium term it would be helped by more construction (which lower interest rates could bring) as well as a planned slowing in immigration.
- In the press conference, the Governor downplayed the importance of their estimated neutral rate in their current decisions. So they aren't particularly focussed on getting there in any particular timeframe. He similarly downplayed the influence of the Fed's clear intention to ease this month in terms of their decision today, while noting that the exchange rate is behaving well given that markets are anticipating a series of Fed cuts.

Re: Economic forecast — While moving in larger steps would, in our view, be defensible given that inflation excluding mortgage interest has run below 2% over the past year, the Bank still seems to have a taste for quarter point steps, and for eschewing detailed forward guidance in favour of taking decisions one at a time. We'll stick with our call for a succession of quarter point cuts at each meeting through March 2025, and a trough near 2 1/2% next year, but will be eyeing Friday's labour market data for evidence that they will need to move there faster.

Re: Markets — While there were some odds put on a 50 bp cut, bond yields drifted lower this morning in reaction to weaker than expected US job vacancy data, and the Canadian dollar was slightly firmer.

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