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Bank of Canada: not today, and that's all for now

by **Avery Shenfeld** avery.shenfeld@cibc.com

Those frustrated by the Bank of Canada's unwillingness to even talk about cutting rates in today's policy statement should bear in mind what its message is designed to do. When rates are left on hold, and so many Canadians are hoping for easier borrowing costs, the Bank needs to focus its words on why it isn't cutting just yet, not on what it might do down the road. Having too many nods in today's message about the progress on inflation, or to downside risks to growth, would only have raised more questions about its choice to keep the policy rate at 5%. As a result, we should be careful about drawing too many conclusions about rate cuts ahead from the lack of any clear steps in that direction in its official statement. Instead, we can simply conclude that today was judged as too soon to make a move.

- Its statement gave a nod to some signs that wage pressures are easing, but balanced that by saying growth was a bit better than expected, if still weak. On inflation, while it mentioned that the overall pace had slowed, it judged that that underlying inflation pressures still persist, led by shelter, and maintained its message that it's still "concerned" about that persistence, and wants to see more progress. In the statement, it opted to stick to its two preferred core inflation measures, with no mention of the better progress seen in measures like CPIX that strip out mortgage interest costs. But it also highlighted the percentage of items that are rising above 3%, and in the press conference, the Governor indicated that they don't only look at the two official core measures, but also a "whole range of indicators."
- We know from remarks the Governor made elsewhere that he judges high rates as not the best tool to address shelter inflation, and the Bank is certainly aware that rate cuts would ease the mortgage interest component of shelter. Government steps to slow inflows of students could help on the rent side. That suggests that continued moderation in inflation rates for other parts of the CPI basket, and a greater share of components below 3%, could be sufficient to have the Bank easing at some point this year, even if headline inflation is still elevated by shelter. That's consistent with the January MPR forecast for better growth in the second half of the year, which it attributed to easier financial conditions, which would have to be validated by actual rate cuts this summer. The Bank is expecting to see inflation start to dip below 3% during that latter half of the year.
- Wage inflation has been a concern for the Bank, so its decision to mention of some signs of moderation on that front is of some importance. Unfortunately, the data have been inconsistent. Data from the SEPH (payrolls) survey showed a marked deceleration in pay rates in the past six months, but today's productivity report still had overall compensation in the 4 1/2% range year-on-year, lifted by brisk gains for the non-business (i.e. public) sector.
- The Bank kept a steady-as-she-goes message on quantitative tightening. While our rates strategists expect it to announce an end to QT as early as April, the Bank is saving further details on its intentions for a speech by Deputy Governor Tony Gravelle later this month. In the press conference, the Governor explained that the period of pressure we saw on overnight rates, which had them running over the target for a while, didn't relate to the QT process, so its interventions to correct for that aren't designed to be a signpost on the timing for winding up QT.

Re: Economic forecast —It wouldn't be the Bank's style to hint today about a rate cut as far off as June, so we'll stick with our call for a rate cut that month despite the lack of fresh dovish talk today. Clearly, we'll need more progress on inflation, and perhaps on wages, for that outcome, so we'll be watching at the upcoming jobs and CPI data as we fine tune our forecasts.

Re: Markets — There weren't any real fireworks in 2-year bond yields, but the Canadian dollar strengthened after the statement in reflection of the absence of any specifically dovish forward guidance, as well as some broader softness in the USD.

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