Bank of Canada frontloads easing to support growth

The BoC matched market expectations and delivered a 50bp cut today. Policymakers' focus is now firmly on "sticking the landing", as Governor Macklem pointed out. We cannot exclude another 50bp cut in December, but the latest labour market news suggest 25bp is still slightly more likely. Our call for CAD outperformance versus AUD and NZD is unchanged

Tiff Macklem, governor of the Bank of Canada

A large cut to balance out inflation risks

The Bank of Canada cut rates by 50bp to 3.75% today, matching consensus and market pricing. Governor Tiff Macklem's opening statement to the press conference stressed how the BoC no longer deems price pressures as broad-based, and that now "we need to stick the landing". The focus is on balancing out the upward and downward forces to inflation, and today's supersize is explicitly aimed at strengthening growth to prevent an excessive inflation slowdown.

Sticking the landing is now the priority

The BoC also published new economic projections. End-2024 GDP growth was revised lower from 2.0% to 1.8%, although growth for 2025 was revised slightly higher. There were only small tweaks to the inflation forecasts, with core CPI still expected to stay modestly above 2.0% into the end of next year. Headline inflation is projected to show some upward volatility and can inch back above 2.0% from the current 1.6% before year-end, but is still seen stabilising close to 2% next year.

December looks like an open meeting

We had some doubts the BoC would go ahead with a half-point move today as the labour market printed strong gains in September with the unemployment rate inching lower. However, Macklem looked through those September numbers and stressed during the press conference how the labour market is "soft" and the economy is in "excess supply".

The Bank did not offer any new forward guidance outside of the indication that rates should continue to be lowered if the economy develops in line with expectations. Macklem dodged a question on a 50bp cut in December at the press conference, and the BoC's approach remains a data-dependent, meeting-by-meeting one. That means incoming figures on inflation, labour and growth will all contribute heavily to drive market expectations for December. The next key releases are August's retail sales on Friday and the GDP report (also for August) on 31 October.

> *Expect high sensitivity in BoC pricing to incoming data*

Markets were already partly speculating on a BoC 50bp December cut before this meeting, and the BoC announcement didn't give any reasons to price dovish bets out before key data come in. Our view is that 25bp reductions are slightly more likely given latest jobs market indications and also considering the recent repricing lower in Fed rate expectations, but for now, the risks of 25bp-50bp are finely balanced.

The US election can also have an impact. Should Donald Trump win, the BoC might want to frontload more easing ahead of expectations that US protectionism will slow global demand. Should Kamala Harris secure the presidency, there might be slightly less urgency to cut, all other things being equal.

CAD: Still looking better than other commodity currencies

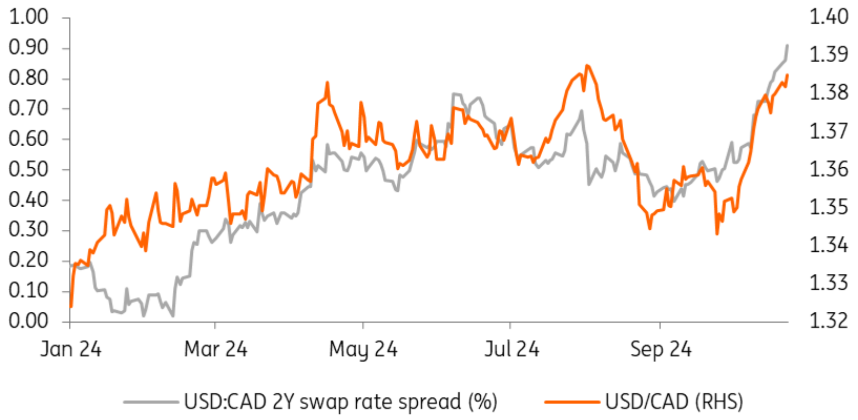
One of our key calls in G10 FX in October has been a stronger CAD versus AUD and NZD as markets build their hedging against a Trump re-election (more in this note). We were taken slightly by surprise by the dovish BoC, but markets had already priced in this 50bp move and the CAD curve has been skewed to the dovish side for some time. CAD was only marginally impacted by the decision.

Soft Canadian data can hit CAD next month, but in the near term we still think the loonie can show some resilience in the crosses due to its relative safe-haven status compared to other high-beta currencies with regards to the Trump risk.

When it comes to USD/CAD, a break above the 1.392 August high can pave the way for a move to 1.40. The US election outcome can have a bigger say than the BoC on the direction of travel for

USD/CAD, especially if Trump wins; for now, the two-year swap rate gap is consistent with USD/CAD trading around 1.39 and soft Canadian data could cause a further widening in favour of USD.

USD:CAD short-term rate gap has widened significantly



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Author

Francesco Pesole
FX Strategist
francesco.pesole@ing.com