BoC Leaves Rate Unchanged With No Hint Of A Near-Term Hike

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Overnight lending rate, %:
Actual: 1.0%
Scotia: 1.0%
Consensus: 1.0%
Prior: 1.0%

- The BoC left its policy rate unchanged at 1% as expected and retained 'cautious' guidance that in my opinion offers no obvious hint on the bias of near-term rate hikes into the new year. The statement was fairly short and broadly balanced in such fashion as to tilt neither in a more hawkish nor dovish direction. Because markets were expecting a slightly more hawkish tilt and didn't get it, CAD depreciated by a full cent versus the USD and the front-end became dearer post-statement as expected. In fact, the GoC 2 year yield dropped by over 4bps and is now outperforming the US front-end plus much of the rest of the curve. Overall, the BoC remains in data dependent mode, unconvinced to change its bias by the broad tone of recent data relative to its October MPR forecasts and more mindful of ongoing uncertainties like NAFTA negotiations than backward looking data in any event. Scotia's BoC forecast remains for a policy hold until April.
- In fact, I continue to think the BoC's focus is more upon the risk of hiking in response to (mixed) backward looking data that over-hypes future inflation risk only to then get a 'dear john' letter from the Trump administration that would make it look rather foolish for having tightened policy in the face of a rising risk to one-third of the economy that is driven by exports. There is obviously a limit to the point to which monetary policy can be put on hold by never ending uncertainties, but I simply don't buy that the data is screaming out that this limit is being breached now or that the BoC's inflation target range of 1–3% is at risk of being materially overshot in the projection horizon. Governor Poloz is well aware of years of model-based forecasts for a return to 2% inflation that haven't worked out and I think his bias is to wait for much clearer evidence the projections will be right this time and being patient in the meantime.
- One key is that the statement takes a broadly neutral stance on the evolution of data relative to its expectations and forecasts. The BoC stated "Recent Canadian data are in line with October's outlook…" That pretty clearly—and rightly in my opinion—says that the BoC is looking at more than just the latest and greatest jobs report. Please see the morning note for a run down on the other high frequency data since the October statement.
- Other data references traded off against each other by noting "very strong" jobs and "some improvement" to wage growth while driving "robust" consumption but acknowledging that exports "declined by more than expected" in Q3 while expecting the resumption of export growth.
- There are, however, two data observations that struck me as somewhat odd which might imply that if future data doesn't reinforce a possible data filter bias then references to them may be at risk of revision. One is that the BoC says that "measures of core inflation have edged up in recent months" which would have been a fairer depiction in the September or even the October report but less so now that the average of the core measures has been stuck

at 1.6% for each of the past three months. Will the BoC have to soften such a reference if core inflation doesn't average out higher over the next one or more months? Can you still say that if core inflation is stuck unchanged for 4, 5, 6 or more months? We'll see, conditioned by data that no one in consensus tries to credibly forecast for monthly core inflation readings. Secondly, the BoC didn't flag any concern about business investment given gains in Q3 but it could well have done so given three months of declining imports of machinery and equipment given Canada imports most of its capital goods. Again, the evolution of data will inform how strongly they stand by this remark in January onward.

- On headline inflation, the BoC noted that "temporary factors, particularly gasoline prices" are boosting headline inflation which implies at least a partial bias to look through some of the rise. The BoC targets headline with core as the operational guide and they're saying headline isn't a big worry near-term.
- Last, the BoC continues to see slack "albeit diminishing" in the labour market regardless of very strong job gains. Some measures they and others have tended to cite have included the labour force participation rate that is still hovering around cycle lows, people working part-time who would prefer full-time work, shrinking average weekly hours worked over the years etc. Indeed, if wage growth accelerates as we think, then in theory that should attract more contestants into the work force to contest higher pay.
- Please see the attached statement comparison.

RELEASE DATE: DECEMBER 6, 2017

The Bank of Canada today maintained its target for the overnight rate at 1 per cent. The Bank Rate is correspondingly 1 1/4 per cent and the deposit rate is 3/4 per cent.

The global economy is evolving largely as expected in the Bank's October *Monetary Policy Report* (MPR). In the United States, **growth in the third quarter was stronger than forecast but is still expected to moderate in the months ahead.** Growth has firmed in other advanced economies. Meanwhile, oil prices have moved higher and financial conditions have eased. **The global outlook remains subject to considerable uncertainty, notably about geopolitical developments and trade policies.**

Recent Canadian data are in line with October's outlook, which was for growth to moderate while remaining above potential in the second half of 2017. Employment growth has been very strong and wages have shown some improvement, supporting robust consumer spending in the third quarter. Business investment continued to contribute to growth after a strong first half, and public infrastructure spending is becoming more evident in the data. Following exceptionally strong growth earlier in 2017, exports declined by more than was expected in the third quarter. However, the latest trade data support the MPR projection that export growth will resume as foreign demand strengthens. Housing has continued to moderate, as expected.

Inflation has been slightly higher than anticipated and will continue to be boosted in the short term by temporary factors, particularly gasoline prices. Measures of core inflation have edged up in recent months, reflecting the continued absorption of economic slack. Revisions to past quarterly national accounts have resulted in a higher level of GDP. However, this is unlikely to have significant implications for the output gap because the revisions also imply a higher level of potential output. Meanwhile, despite rising employment and participation rates, other indicators point to ongoing—albeit diminishing—slack in the labour market.

Based on the outlook for inflation and the evolution of the risks and uncertainties identified in October's MPR, Governing Council judges that the current stance of monetary policy remains appropriate. While higher interest rates will likely be required over time, Governing Council will **continue to be cautious,** guided by incoming data in assessing the economy's sensitivity to interest rates, the evolution of economic capacity, and the dynamics of both wage growth and inflation.

RELEASE DATE: OCTOBER 25, 2017

The Bank of Canada today maintained its target for the overnight rate at 1 per cent. The Bank Rate is correspondingly 1 1/4 per cent and the deposit rate is 3/4 per cent.

Inflation has picked up in recent months, as anticipated in the Bank's July *Monetary Policy Report* (MPR), reflecting stronger economic activity and higher gasoline prices. Measures of core inflation have edged up, in line with a narrowing output gap and the diminishing effects of lower food prices. The Bank projects inflation will rise to 2 per cent in the second half of 2018. This is a little later than anticipated in July because of the recent strength in the Canadian dollar. The Bank is also mindful that global structural factors could be weighing on inflation in Canada and other advanced economies.

The global and Canadian economies are progressing as outlined in the July MPR. Economic activity continues to strengthen and broaden across countries. The Bank still expects global growth to average around 3 1/2 per cent over 2017-19. However, this outlook remains subject to substantial uncertainty about geopolitical developments and fiscal and trade policies, notably the renegotiation of the North American Free Trade Agreement.

Canada's economic growth in the second quarter was stronger than expected, and was more broad-based across regions and sectors. Growth is expected to moderate to a more sustainable pace in the second half of 2017 and remain close to potential over the next two years, with real GDP expanding at 3.1 per cent in 2017, 2.1 per cent in 2018 and 1.5 per cent in 2019. Exports and business investment are both expected to continue to make a solid contribution to GDP growth. However, projected export growth is slightly slower than before, in part because of a stronger Canadian dollar than assumed in July. Housing and consumption are forecast to slow in light of policy changes affecting housing markets and higher interest rates. Because of high debt levels, household spending is likely more sensitive to interest rates than in the past.

The Bank estimates that the economy is operating close to its potential. However, wage and other data indicate that there is still slack in the labour market. This suggests that there could be room for more economic growth than the Bank is projecting without inflation rising materially above target.

Based on this outlook and the risks and uncertainties identified in today's MPR, Governing Council judges that the current stance of monetary policy is appropriate. While less monetary policy stimulus will likely be required over time, Governing Council will be cautious in making future adjustments to the policy rate. In particular, the Bank will be guided by incoming data to assess the sensitivity of the economy to interest rates, the evolution of economic capacity, and the dynamics of both wage growth and inflation.