BoC: Policy Still "Appropriate"

- Markets didn't like what the BoC had to say as CAD rallied and short-term market rates increased a bit, but that's not necessarily to be taken as an indication that the statement itself was hawkish in nature. I think the market reaction was more about position covering in anticipation of a more dovish statement than was delivered which had markets swinging too far in the opposite direction.
- One thing markets probably didn't like is the fact that the BoC retained "the current degree of monetary policy stimulus remains appropriate." They said "current" in the last statement as well but only slightly altered the positioning which doesn't strike me as relevant. Yes, maybe the BoC didn't wish to tee up an October cut explicitly given Poloz loathes forward guidance, but they've played with that final paragraph so many times this year each time the winds shift that it was a reasonable expectation for the 'appropriate' reference to be at least modified without taking it as explicit reference to anything versus leaving the door more open to uncertainty. So why didn't they? I find it a stretch to say policy is appropriate in light of everything that has happened since they last spoke nearly two months ago. Regardless, saying that policy remains appropriate while core inflation remains around 2% and the economy "is operating close to potential and inflation is on target" isn't terribly dovish if a cut lurks around the corner. The effect was to modestly tighten financial conditions when central banks arguably shouldn't be tightening financial conditions.
- What I think will inform cut risks as soon as the October decision will be three things. One is domestic data and they'll get two more rounds of this before the October 30th decision. They want to see if the disconnect between stronger wage growth and soft consumption results in a firming consumption profile or not as one example.
- Second will be external developments that include references to "escalating trade conflicts and related uncertainty" that the BoC says "is weighing more heavily on global economic momentum the Bank had projected in its July Monetary Policy Report" specifically in reference to the US-China trade conflict. Bear in mind, however, that on external risks, the BoC still references a "solid" US economy.
- Balance comes through in referencing stronger than expected Q2 growth with only "some" of this expected to be temporary, while lower mortgage rates feed some concern that at least some of this effect will drive "already-high household debt" despite tightened mortgage rules. Overall, the BoC expects growth to slow over H2 along with everyone else, but it's unclear how negative they are prepared to go and we see nothing in this statement about 2020 which is the more relevant policy horizon.
- As much as I'd like the statement to have cooperated with a forecast October cut, there is enough ambiguity and an "appropriate" tone to the statement to leave uncertainty focused upon data and developments over the next eight weeks in addition to uncertainty over how the BoC will read it all in October's forecasts.

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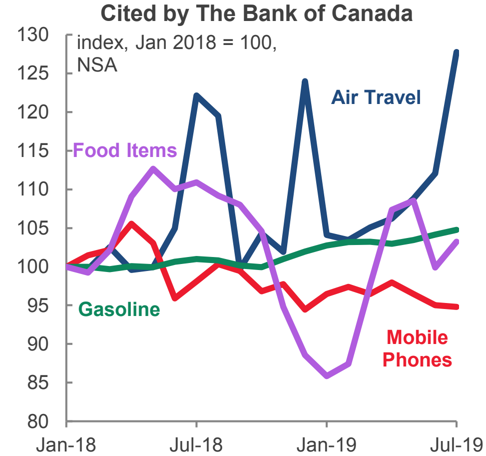
July Transitory Effects in CPI Categories Cited by The Bank of Canada



Sources: Scotiabank Economics, Statistics Canada.

- What I think will happen will be a forecast downgrade in October that pushes out the closure of spare capacity, in turn creating slack for longer than the July MPR anticipated and therefore creating concern about core inflation remaining durably on target. That would be a solid framework around which to position an insurance cut or two starting after the federal election. But if you were looking for a nod from this statement to the effect that OIS markets should be catapulting rate cut odds in October to enormous heights, then clearly that market expectation was dashed. The BoC wouldn't do that. But presumably a market savvy central bank also wouldn't have gone out of its way to even modestly tighten financial conditions in this environment.