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Plotting the policy path through an empircal lens

By Taylor Schleich

As expected, the Bank of Canada and Federal Reserve lowered their policy rates last week as each nation's labour market has softened of late. While these cuts were fully expected, the outlooks remain a bit hazy.

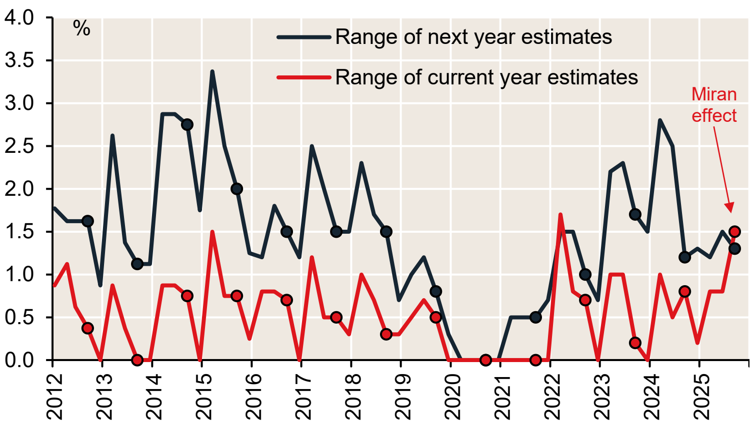
At the Fed, a new dot plot indicates the median participant sees 50 bps of further easing this year. There are, however, still two distinct camps on the FOMC as a large minority penciled in no more cuts in 2025. In fact, there's never been a range of views so wide for a same-year projection this late in the year. Of course, that's due to Stephen Miran's dot—projecting 125 bps of further easing—but even excluding this, the range is still large. But for all the talk of diverging Fed views, disagreement beyond 2025 is not particularly pronounced, at least relative to the past.

As for how things play out, we're fading the hawks' preferred policy path. For one, it's rare for the policy rate to end the year at a different level than the September median dot. Since 2012, that's happened just twice (2019, 2023) and neither of those involved *higher* rates. Moreover, it appears that voting members are concentrated at the lower end of the spectrum (e.g., Waller, Bowman, Miran). So even though we see think the jobless rate will end the year stronger than the Fed does, we're not doubting the median 2025 dot, especially not in favour of a more restrictive alternative.

On the other side of the border, the BoC always makes it more challenging to gauge the policy rate path as there's no dot plot style document to dissect. Nor did the Bank's communique *clearly* lean towards a cut or hold over coming meetings. But as we've argued, if you're going to cut once, you're probably going to cut again (after all, what difference does a single 25 bp cut *really* make?). Naturally then, we expect a follow-on cut at the next decision in October, a call that's supported by the empirical record. In the fixed announcement data era (starting in 2000), the only 'hold-cut-hold' sequence you'll find was in 2015. Recall, there was not much room to manoeuvre during that 'mini' easing cycle, as cuts occurred when the Bank's policy rate was at or below 1%. The overnight target isn't particularly high today, but Governing Council has plenty of room to go again. Beyond October, the picture is a bit murkier. The accumulation of economic and inflation data and greater clarity on fiscal policy (via a budget on November 4th) will dictate how much more rate relief is needed. For now, our baseline view entails a terminal rate of 2.25% but we'd judge that risks are skewed towards greater easing being required. OIS markets reflect this view, but the implied easing path may deepen and get pulled forward if sluggish economic data continues to accumulate.

Chart 1: Internal Fed divergence, beyond 2025, is overstated

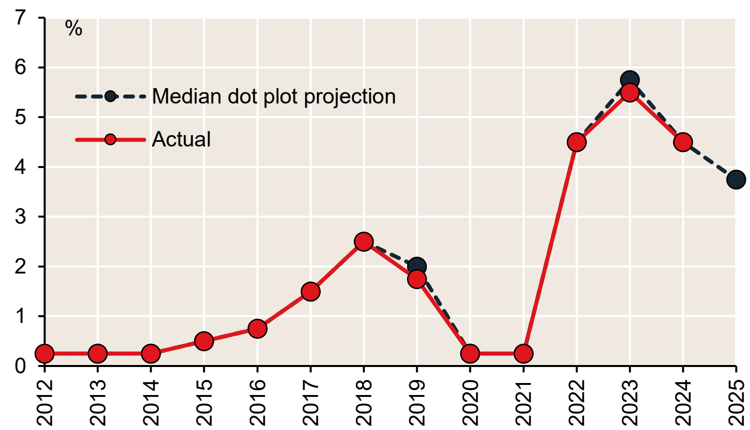
Range of fed funds projections in historical dot plots: Current year, 1-year ahead



Source: NBC, FRB | Note: Range = High-low projection. Markers denote September dot plots.

Chart 2: Don't doubt September's dots

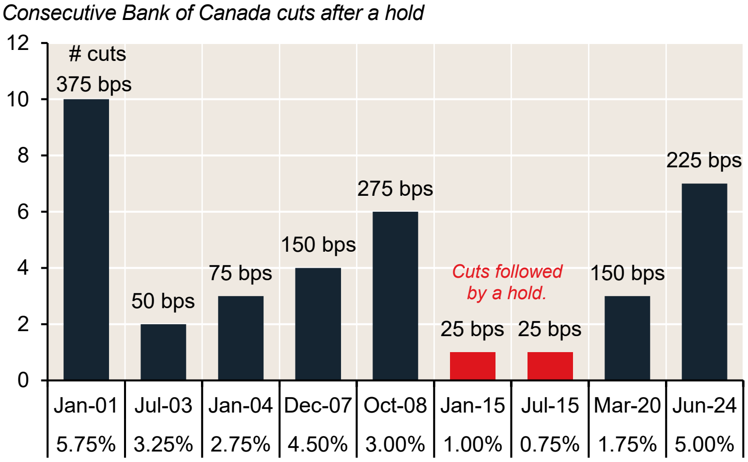
Actual fed funds target, median projection for the current year as of September



Source: NBC, FRB | Note: E.g., Blue 2025 dot refers to the year-end 2025 estimate, as of Sept.

Chart 3: When the BoC cuts, they (usually) cut again

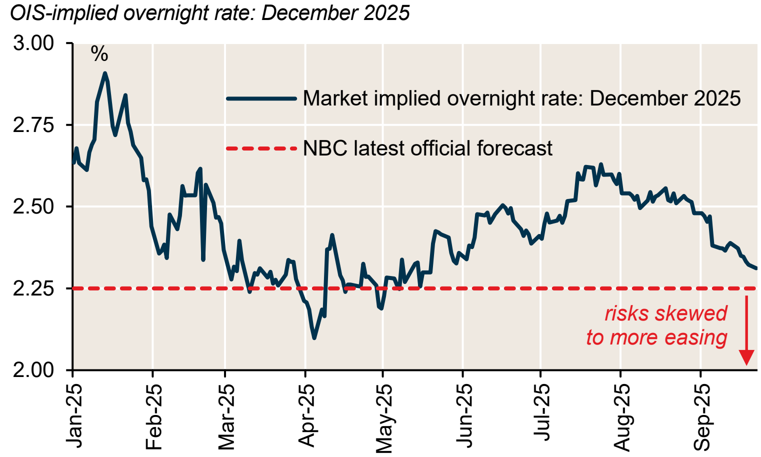
Consecutive Bank of Canada cuts after a hold



Source: NBC, BBG, BoC | Note: Label = total easing in cycle. X-axis = first cut date, start rate

Chart 4: Market priced for 2 more cuts, but risks skew to more

OIS-implied overnight rate: December 2025



Source: NBC, BBG

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