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# Rate cuts drive cautious optimism among Canadian businesses in Q4

## The Bottom Line:

- Message from businesses that participated in the Q4 Bank of Canada quarterly outlook survey were a healthy mix of a thawing in the weak demand conditions as interest rates drop, and broadly slowing inflation pressures.
- As much as the pick-up in sales outlooks is welcome, it doesn't mean the Bank of Canada is done with supporting the economy. We continue to expect the central bank will need to keep lowering interest rates to 2%, to ensure the early signs of strengthening in demand can be sustained and inflation doesn't undershoot the central bank's target.
- We expect a 25bps rate cut from the meeting later this month.

## The Details:

- In Q4, businesses sentiment was still "subdued". Demand was particularly soft for firms catering to discretionary (or non-essential) consumer spending, that was reportedly tied down by past interest rate increases. The outlook, however, showed signs of improvement.
- Thanks to easing monetary policy since June, businesses reported cautious optimism in their demand outlooks and investment intentions over the next year, although tariff risks were emerging to offset.
- Most optimistic was the oil and gas sector that reported a 4% expected increase in their 2024-25 CapEx budget and a 5% expected rise in production, thanks to the start of the TMX project last year and the launch of LNG Canada's Phase 1 by the middle of this year.

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- Outside of the energy sector, investment intentions were more modest given most firms were still reporting excess capacity and limited need to expand. Rising trade disruptions tied to the new U.S. administration were also weighing on business investment plans.
- Indeed, as much as 40% of firms surveyed expected negative effects, especially on their input costs and export sales from the U.S. election while a third were unsure.
- On net, businesses continued to think growth in their input costs will slow over the next year. Wage growth was also expected to moderate amid relatively soft hiring intentions – most firms surveyed expected to maintain the same level of employment over the next year.
- As cost pressures ease, the anticipated rebound in demand was seen as an opportunity for businesses to restore their margins, although only to the extent that market competitive forces will allow.
- Finally, inflation expectations among firms largely remained in check in Q4. 75% of firms surveyed were expecting average inflation in the next two years will be within the BoC's 1% to 3% target, up from 42% in Q4 2023 but still below the ~90% share in pre-pandemic 2019.unwind.