

Bank of Canada hikes interest rate by 25bp

The Bank of Canada has raised interest rates by 25bp. It acknowledged the uncertainty caused by Russia's invasion of Ukraine, which could weaken growth and boost inflation. Nonetheless, Canada's economy is likely to be one of the more insulated from damaging economic effects and we look for five further hikes this year



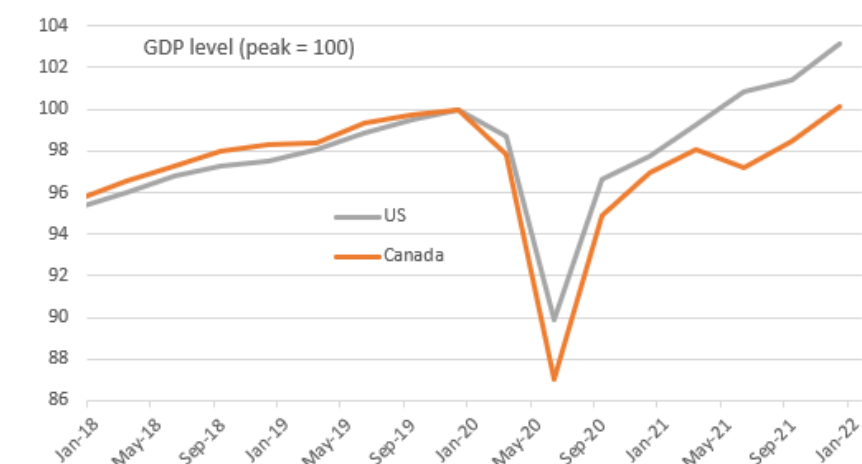
Bank of Canada starts to tighten policy

As widely expected we have a 25bp interest rate hike from Bank of Canada (BoC), taking the target for the overnight rate to 0.5%. It is keeping the balance sheet stable with all maturing assets continuing to be reinvested.

The bank acknowledged that Russia's invasion of Ukraine is a "major new source of uncertainty" that will "add to inflation around the world... [and] could weigh on global growth". Nonetheless the strong domestic growth story provides support with the lifting of Covid restrictions meaning "growth is now looking more solid than previously projected". As the chart below shows, the economy has now recovered all of the lost output caused by the pandemic while employment is

actually above pre-pandemic levels. So while the economy hasn't grown quite as vigorously as in the US, the labour market has actually outperformed.

Canada vs US size of the real economy (4Q19 = 100)

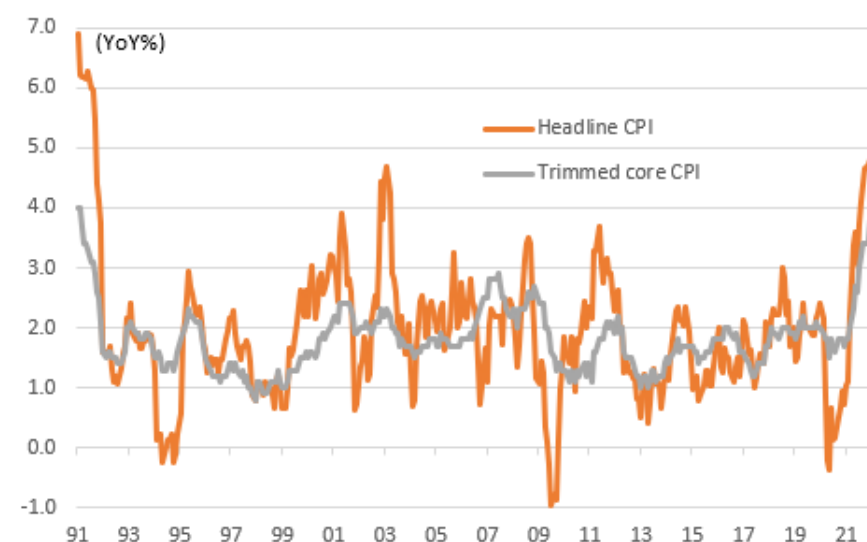


Source: Macrobond, ING

More rate hikes are coming and quantitative tightening will be utilised

Inflation, which is already at 30-year highs, is also now expected to be higher in the near term than projected in January and the risk is that inflation expectations "could drift upwards". Consequently the Bank of Canada "expects interest rates will need to rise further" and this will be complemented by "quantitative tightening" via ending the reinvestment phase of its bond holdings.

Canada inflation rates (YoY%)



Source: Macrobond, ING

Russia risks are high, but Canada is in a strong position

The BoC did not provide specific guidance due to the uncertainty and economic implications from "the unprovoked invasion of Ukraine by Russia". We are looking for six rate hikes from the BoC in total this year (so five more to come). Canada is relatively insulated due to being a major commodity producer and having far less direct economic and financial linkages with Russia and Ukraine. Markets are currently pricing for another 5.5 hikes this year.

Author

James Knightley

Chief International Economist, US

james.knightley@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.