

## Bank of Canada holds, but July cut quite possible

The BoC held rates today in line with expectations, but growth and labour market deterioration can easily tilt the balance to a cut at the July meeting. As it's now the new normal, much will also depend on the US-Canada trade relationships. Anyway, CAD remains one of our least favourite currencies in G10



Bank of Canada  
Governor Tiff Macklem

### Still strong case for cuts

In what was likely a very close decision, the Bank of Canada opted to keep its policy rate at 2.75%. The market had favoured such an outcome, but economists were, in general, looking at a cut, certainly up until last week's GDP numbers. Unemployment is in danger of breaching 7% in Friday's jobs report, but despite a low headline inflation print, core CPI has been moving higher again with the BoC warning that *"recent surveys indicate that households continue to expect that tariffs will raise prices and many businesses say they intend to pass on the costs of higher tariffs. The Bank will be watching all these indicators closely to gauge how inflationary pressures are evolving."* 1Q GDP growth was also stronger than expected at 2.2% annualised versus the 1.7% consensus, but this was primarily being driven by tariff front running with inventories and net exports

That said, confidence is weak, consumer spending stalled, and business investment fell in Q1. Trade is critical to the outlook given the importance of US exports to the Canadian economy, and

while there has been a slight calming in tensions post Prime Minister Carney's visit to the White House, nothing can be taken for granted. For now, the BoC acknowledges that the Canadian economy is *"softer but not sharply weaker, and [given] some unexpected firmness in recent inflation data, Governing Council decided to hold the policy rate as we gain more information on US trade policy and its impacts."*

The worry is that the latest de-escalation will only lead to a renewed escalation of trade tension that tips Canada's economy into recession. As such we predict another 25bp cut in July; the market is currently pricing 55-45 in favour of such a move.

## CAD remains unattractive

While the upside for USD/CAD may stay capped on the back of the USD's own woes, the loonie appears rather unattractive in the near term against most other G10 currencies. The new US steel and aluminium tariffs spell trouble for the already highly affected Canadian economy, and CAD has been trading more and more closely with US data sentiment, which may well deteriorate as the tariff impact unravels.

Also, market pricing for BoC cuts (35bp by year-end) looks too conservative, and growth/labour weakness in Canada may well drive some dovish repricing along the way.

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