Bank of Canada Preview: And hold...

The Bank of Canada meets again this Wednesday. Although a surprise rate hike can't be ruled out completely, a 2Q GDP print fractionally undershooting the consensus and Nafta uncertainty gives us enough reason to favour a pause until October

Source: shutterstock

The Bank of Canada's policy tightening journey on hold

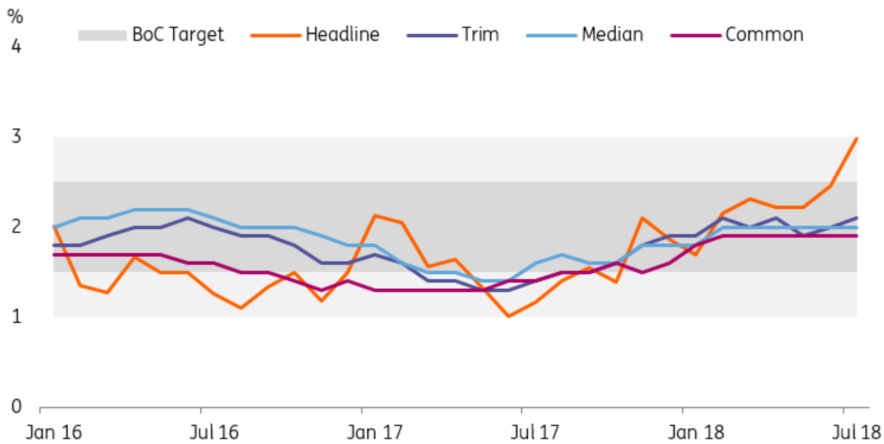
We expect the Bank of Canada (BoC) to pause its tightening cycle and maintain the policy rate of 1.5% at the September meeting this Wednesday. But our prediction of a 4Q rate hike still stands - coming as soon as October, although contingent on domestic data staying firm.

We've been confident for some time now that the BoC will follow July's rate hike with another in the second half of 2018, supported by a summer of high inflation and strong growth, but we don't expect this to come at the September meeting. Two consecutive rate hikes would not be out of character – we saw this just last year – but the 2.9% 2Q GDP figure, which was a touch disappointing amid a deceleration in business investment, suggests the odds for a September hike are low.

Bumper inflation? Not to worry

July's 3% inflation touched what the BoC considers to be the upper bound for CPI, tempting some to back a September hike. However, Governor Stephen Poloz's most recent statement – although vague – calmed the waters stating, "Our measures of core inflation, which extract all the noise from the data, are all right around two per cent — so, very close to target", emphasising that policymakers aren't too concerned about current price levels, which are likely related to the fact that headline CPI has been driven mostly by volatile components.

Core measures show stability, but headline data touches the BoC's upper bound



Source: Macrobond

Typical Trump talk clouds Nafta outlook – again

Promising signs were shown only last week as Canada re-joined Nafta talks, but negotiations concluded on 31 August with no agreement and 'Trump talk' fired up again over the weekend, albeit through a series of tweets, dampening the optimism behind a trilateral deal.

A lot of jawboning against Canada was evident in the tweets on Saturday, emphasising that there is "no political necessity to keep Canada in the new NAFTA deal". This does pose further risks in regard to finalising a deal, but 'Trump talk' is generally used as a negotiating tactic – in this case to push for Nafta advancements and unless we see a serious breakdown in the discussions, the BoC's outlook for another hike in late 2018 should remain intact.

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