Bank of Canada sticks to its guns

BoC has kept the overnight rate at 1.75%. While global trade concerns remain a significant threat, better than predicted 2Q growth and higher wage and price inflation readings suggest a stable outlook for rates

Highlighting uncertainties

As widely anticipated, the Bank of Canada left its overnight rate unchanged at 1.75% today. The statement highlights the uncertainties on the outlook that will likely keep policy stable for a prolonged period.

The accompanying statement acknowledged the threat posed by global trade tensions, which in turn risks curbing manufacturing activity, weakening investment and dampening commodity prices. As such, it's not surprising that the BoC believes any "escalation of trade conflicts remains the biggest downside risk to the global and Canadian outlooks".

However, the BoC also acknowledges that the domestic story has improved from the weakness seen in 4Q18 and 1Q19. Canada is growing at potential with second quarter activity described as being "stronger than predicted". This was partly attributed to temporary factors such as the re-starting of oil fields and better weather, but there was also an acknowledgement of stronger consumer spending and housing activity resulting from the firm labour market and falling mortgage rates.

Inflation is broadly expected to remain in line with the bank's target with the recent upward surprises set to be reversed thanks to lower gasoline prices. However, the recent stronger than anticipated wage figures could yet limit the downside moves in price inflation, while also keeping consumer spending stronger.

Reasonably relaxed

Overall, the tone of the statement suggests that the BoC is reasonably relaxed with the situation given that downside external risks are being offset by the positive domestic activity story. The BoC acknowledges that both the Federal Reserve and European Central Bank have signalled a willingness to provide more monetary stimulus, while China is implementing some fiscal stimulus too, but there seems little appetite for Canada to follow just yet.

We continue to look for the Bank of Canada to leave monetary policy unchanged both this year and next given the Bank still talks about the degree of accommodation it is providing and the fact that the BoC was far less aggressive in hiking rates than the Federal Reserve over the past couple of years. As such, there is arguably less need for a corrective move lower in rates.

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