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Article

Poor Canadian wage growth gives central bank further reason to hold in January

Wage growth failed to pick up in December, which coupled with other global risk factors, means the Bank of Canada is likely to side with caution and push back the next rate hike until March

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In their December press release, the Bank of Canada (BoC) reiterated that the policy rate will need to rise into their neutral range (2.5%-3.0%) to achieve target inflation. Although this implies that there are likely to be multiple rate hikes on the horizon (given the policy rate is currently at 1.75%) we don't see one coming when the Bank meets on Wednesday, 9 January.

Economic growth prospects dampened

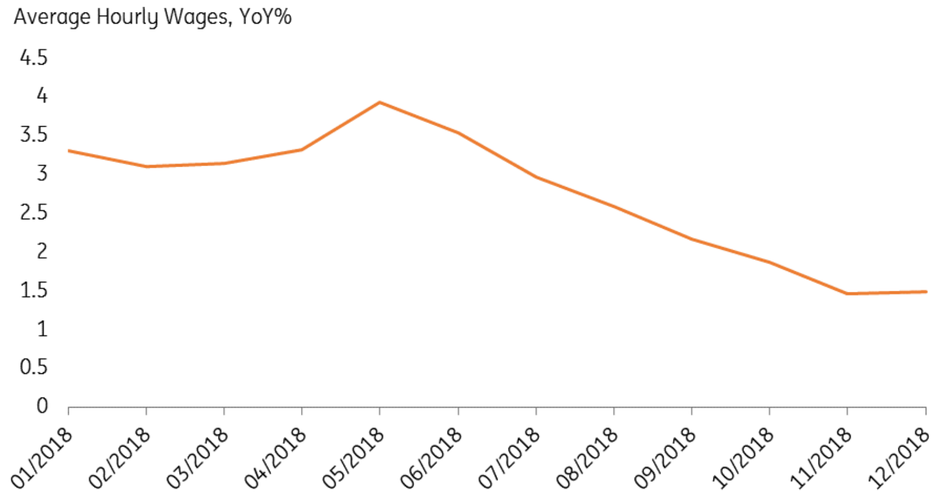
The current risk environment is likely to push the BoC to side with caution. World oil prices have fallen back sharply, while Alberta has enforced a sizable cut to production to help support prices in Western Canada. This lower production may have an adverse effect on some domestic producers.

Third quarter data hasn't helped either, particularly the fall in business investment spending. However, this was likely to have been influenced by the lack of certainty surrounding a new Nafta deal at the time. Now that a deal has been reached, we would expect to see investment recover – at least outside of the energy sector anyway.

Wage growth...De ja vu?

From May's 3.9% peak, November was the sixth month running to see a decline in year-on-year growth in average hourly wages (for permanent workers) to 1.5%, and stayed there in December. This weaker trend, coupled with the higher rates are beginning to feed through to growth, helping the housing market to stabilise, gives further reasons for the BoC to hold off pushing the policy rate higher next week.

Average hourly wages fail to pick up in December



Source: Macrobond

Having said that, we expect the wage growth story to improve in 2019. In the BoC's most recent Business Outlook Survey, firms reported pushing wages higher will be one of their strategies to attract workers, in light of labour-related production constraints that were frequently noted to be an issue.

We still expect the Bank of Canada to hike in the first quarter

A rate hike later in the first quarter (in March) still could be on the cards, unless the risk environment worsens further. This would allow policymakers a bit more time to evaluate the impact of lower energy prices on growth, as well as whether business investment and wage growth have begun to perform more strongly.

Either way, with core inflation measures still sitting around the 2% target and unemployment at a 40-year low, we still expect to see at least two further Bank of Canada rate hikes this year.

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