

Bank of Canada keeps rates on hold

Healthy growth and 2% inflation means policy will be quickly tightened once NAFTA uncertainty clears. We expect two moves in the second half of 2018, starting in July



Source: Bank of Canada

The Bank of Canada met expectations in today's meeting, keeping the overnight interest rate unchanged at 1.25%. This was always likely given trade uncertainties relating to NAFTA and US-tariffs. Unsurprisingly NAFTA was not directly commented on by the BoC, who will not be wanting to infer anything about current negotiations, given a deal could be in the making in upcoming weeks.

1.25% Policy Rate

As expected

Aside from the trade aspect, the Canadian economy is performing well despite a recent slowdown

in growth. This economic moderation was expected after 2017's exceptionally strong performance and has been largely down to the trade uncertainties, measures taken to cool down local housing markets and rising interest rates.

A notable change in the economy is the slight fall in debt to income ratio for the first part of 2018. This has been a growing concern for years where household debt has repeatedly hit record highs, so seeing a downward shift has come as a welcome relief. The Bank will continue to watch this closely as they monitor the economy's sensitivity to interest rate increases.

There has also been a build-up in wage and price pressures due to shrinking slack in the economy, higher gasoline prices and the increase in Ontario's minimum wage. The latest headline CPI reading came in at 2.2% year-on-year in February, the fastest pace in three years, with core inflation climbing slightly above the Bank's 2% target. These figures are likely to challenge the Bank's recent dovish 'wait-and-see' approach.

As discussed in our [latest NAFTA piece](#), although NAFTA seems to be moving in the right direction there is still a wide-divide on some key issues. However upcoming elections, the expiration of the US Trade Promotion Authority, the ending of the reprieve given to Canada on US-tariffs and the possibility of a US-China trade war have increased the urgency for an agreement. Guajardo, the Mexican Economic Minister, among others have said that a deal could be made by the beginning of May as negotiations continue in Washington this week.

Assuming a NAFTA deal is signed, we see the Bank's hiking schedule recommencing in the second half of 2018 with two moves, starting in July.

[NAFTA 2.0: What does this mean for Canada](#)

Author

James Knightley

Chief International Economist, US

james.knightley@ing.com

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