



Laurentian Bank Securities ECONOMIC RESEARCH AND STRATEGY

Bank of Canada Decision – Rate Hike: Not Today but Moving Closer

The Bank of Canada (BoC) left its overnight rate target unchanged at 1.25% this morning. More importantly for financial markets, the statement explaining this decision took a hawkish turn: *"Overall, developments since April further reinforce Governing Council's view that higher interest rates will be warranted to keep inflation near target. Governing Council will take a gradual approach to policy adjustments, guided by incoming data."*

In comparison, the April statement ended by: *"higher interest rates will be warranted over time, although some monetary policy accommodation will still be needed to keep inflation on target...In this context, Governing Council will remain cautious with respect to future policy adjustments, guided by incoming data".* Our interpretation is that the BoC sees a growing case for a rate hike in the near future. Citing a *"gradual approach"* also means the BoC does not plan to hike 3-4 times during the second half of 2018.

This relatively more hawkish tone from the BoC is driven by stronger oil prices, some upside for the U.S. economy and by the recognition that *"activity in the first quarter appears to have been a little stronger than projected"* in Canada. The Canadian real GDP report will be released tomorrow at 8:30AM; the BoC had projected 1.3% q/q saar growth in its April's *MPR* (our call stands at 1.5% while the consensus is at 1.9%).

The BoC nevertheless did not hike today, preferring to wait at least until the July 11th decision. In our view, the biggest single event that could prevent the BoC from raising its policy rate in mid-July is the announcement of punitive tariffs on Canadian steel and aluminium products this Friday by the U.S. White House. *"Guided by incoming data"*, the positive global and domestic economic momentum will need to be sustained for the BoC to hike in mid-July.

Bottom Line: Although U.S. trade policy uncertainty remains in place, the list of justifications to delay the next policy rate hike is shrinking. We continue to see a 25bps hike at the July 11th meeting if steel and aluminium tariffs are not enacted. Beyond July 11th, the monetary tightening cycle is expected to be smooth. Back-to-back 25bps policy rate increases, as the BoC was able to do in July and September of last year due to extremely robust GDP growth readings, are very unlikely this time around. We see the subsequent BoC rate hike in December or early 2019.

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