Bank of Canada Rate Announcement
January 9, 2019

The Bank of Canada left its policy rates unchanged in response to weaker economic growth. Weaker than expected oil prices, housing activity and consumer spending prompted a downward revision to Canada’s near-term growth forecasts. This growth slowdown increases excess capacity relative to the Bank’s October 2018 forecasts and lessens the need for monetary tightening. The overnight target rate remains at 1.75 per cent. With this announcement, the Bank released its Monetary Policy Report January 2019 containing its updated projections.

The Bank’s growth forecast for the first quarter of 2019 was 0.8 per cent annualized. This would be the slowest pace since the second quarter of 2016, when the economy briefly contracted due to the disruption in oil production from the Alberta wildfires and weak commodity prices in general. With the Bank’s potential output growth estimate put at around 1.9 per cent and the output gap forecast to increase in the fourth quarter of 2018 and the first quarter of 2019—the Bank will rarely, if ever, raise rates under these conditions.

Beyond the near-term, Canada’s growth is forecast to rebound to around two per cent during 2019 from the first quarter slowdown. Canada’s 2019 growth forecast is 1.7 per cent, rising to 2.1 per cent in 2020. As in previous forecasts, the Bank is relying on better export and business investment spending to achieve its growth forecasts. The Bank sees slower global and U.S. growth in 2019 and a further slowing in U.S. growth in 2020. Growth in the rest of the world economy, excluding Japan and China, is seen improving.

While the Bank is currently on hold, its statement reiterated that “...the policy interest rate will need to rise over time into a neutral range to achieve the inflation target.” The Bank will be data and trade policy dependent in its future rate decisions, and should its forecast materialize, we should see rate increases during the next two years.

This forecast has the Bank on hold until late 2019 before implementing a quarter-point increase, and admittedly, there is more downside than upside risk to this forecast. The three-month Canadian Bankers’ Acceptance Futures market is not pricing a rate increase through to 2020. Our forecast is less positive in 2020 compared to the Bank, with growth put at 1.7 per cent versus the Bank’s 2.1 per cent due weaker housing, business investment and exports. The bottom line is that rate will remain low and below the neutral range into the foreseeable future.

Helmut Pastrick
Chief Economist, Central 1 Credit Union
hpastrick@central1.com
www.central1.com  604.737.5026