

Interest-rate forecast: Update

The Bank of Canada hiked its policy rate for the first time in seven years, raising the overnight rate 25 basis points to 0.75%. This came as no surprise as the BoC had set the stage for it through its communications. The real question is whether the decision to raise the overnight rate should be seen as a first step in removing the “insurance policy” taken out in 2015 or as the first of a series of upcoming rate hikes. BoC Governor Stephen Poloz was unwilling to categorize the rate decision along those lines. In his press conference, Poloz stated: “In the full course of time, I don’t doubt that interest rates will move higher, but there’s no pre-determined path in mind at this stage. It’s a data dependent, quarter-by-quarter analysis that we’ll be doing.” With interest rates still very low and the bank projecting the output gap closing by the end of this year, we think that there are more rate hikes to come and that the next one will be delivered later this year.

In her semi-annual report on the economy and monetary policy before the House of Representatives Financial Services Committee, Fed Chair Janet Yellen reminded her audience that the Fed’s stance remained accommodative and that positive economic developments would “warrant gradual increases in the federal funds rate over time.” She reiterated that the Fed would “likely begin to implement the program this year” but mentioned that no decision had been made regarding the sequencing of actions. She left the door open to speculation that the FOMC might announce the beginning of balance sheet reduction before the next rate hike. We believe that balance sheet normalization will be announced in September and begin in October and that the next rate hike will occur in December. According to our base case scenario, two additional hikes will take place in 2018 instead of the three previously forecasted.

Paul-André Pinsonnault

Interest rate forecast

United States

Quarters	Fed Fund	3 Mth Bill	2YR	5YR	10YR	30YR
07/12/17	1.25	1.05	1.35	1.88	2.32	2.89
Q3	1.25	1.13	1.46	1.96	2.38	2.94
Q4	1.50	1.36	1.80	2.27	2.68	3.20
Q1/18	1.75	1.58	1.91	2.34	2.81	3.30
Q2	1.75	1.74	2.02	2.41	2.86	3.32
Q3	2.00	1.83	2.12	2.49	2.90	3.33
Q4	2.00	1.83	2.19	2.55	3.02	3.43

Canada

Quarters	Overnight	3 Mth Bill	2YR	5YR	10YR	30YR
07/12/17	0.50	0.76	1.19	1.50	1.87	2.23
Q3	0.75	0.89	1.25	1.60	1.95	2.31
Q4	1.00	1.16	1.34	1.66	2.00	2.36
Q1/18	1.25	1.42	1.57	1.84	2.15	2.50
Q2	1.50	1.46	1.75	1.96	2.26	2.60
Q3	1.50	1.46	1.74	1.98	2.29	2.60
Q4	1.50	1.46	1.78	2.00	2.33	2.63

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