Market View
Economics and Strategy

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A clearer path to early-2027 BoC rate hikes

By Taylor Schleich & Ethan Currie

*In lieu of an August Fixed Income Monitor, we use this Market View to reaffirm our BoC rate call. See the **July FIM** for our detailed rate projections.*

Last week, Canada's labour market added jobs for a third straight month. A ~180K 3-month increase was last seen in late 2025 and, before that, in late 2024. In both cases, momentum quickly fizzled out and employment fell soon after. Naturally then, there's skepticism that recent job gains will hold. But empirically, these recent episodes are exceptions rather than the rule. From 2000 to 2019, we identify 16 unique instances of three-month job growth rising to a 3% annualized pace. In nearly every case, hiring subsequently cooled—but in all cases, employment kept rising.

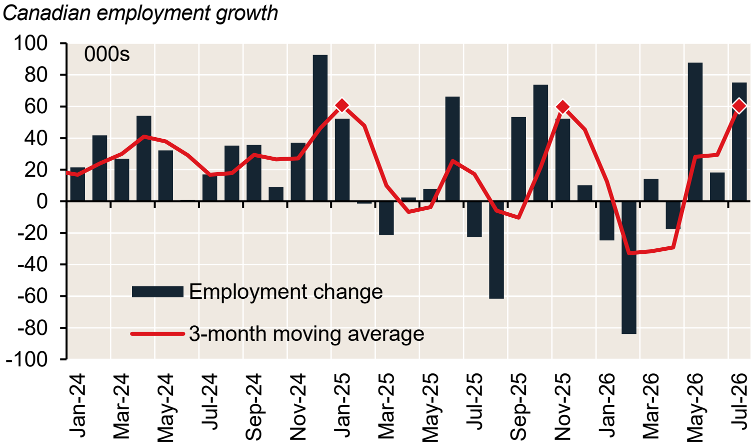
Another reason to take recent jobs data as a sign of a legitimate rebound? It's consistent with economic data more broadly. By now, it's widely accepted that Q2 GDP growth will be robust. And while there's scant data available to form the Q3 growth picture, the strong pick-up in hours worked implies momentum was carrying over.

With inflation near 3% and set to remain above target, one might argue a sustained economic rebound will prompt a BoC rate hike this year. But we think the Bank will need more time to become convinced that the improvement has staying power. For one, not all job market data have improved, including job vacancies and the BoC's own *Business Outlook Survey*. There's also July's tariff threats which introduced a new source of downside risk. Even before this, the Bank wasn't sure if growth would persist. Per the July Summary of Deliberations, "*Governing Council was confident about the rebound in GDP growth in [Q2]. But there was a range of views about the sustainability of the rebound beyond the near term*."

Accumulated slack also argues for patience. According to the BoC, the output gap stood at 1.3% of GDP in Q1. This won't be absorbed in one quarter. The Bank also called the labour market 'soft' last month, with the jobless rate at 6.5%. July's 1-tick decline may prompt a less downbeat tone, but the UR's volatility should keep them cautious. To the Bank's way of thinking, slack apparent in recent quarters should keep underlying inflation contained, allowing them to let the economy, and job market, run.

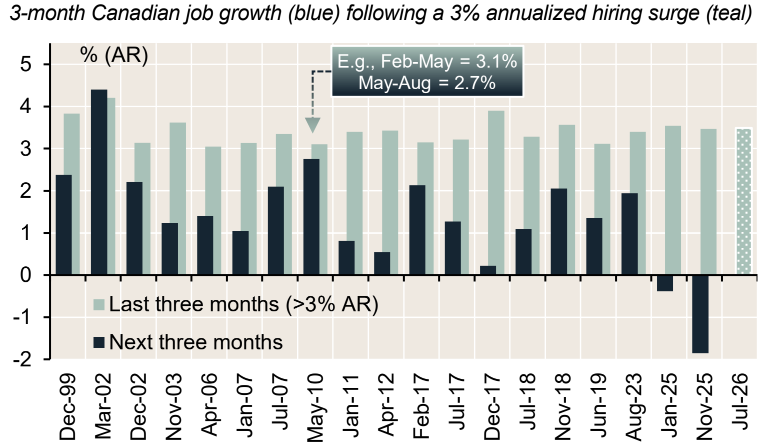
Given the lags in data publication (e.g., Q3 GDP isn't published until late November), it's hard to see the conditions for lift-off being met in 2026. We therefore continue to view Q1:2027 as a more plausible starting point for BoC tightening. That's a tad later than OIS markets imply but well before Bloomberg's median forecast, which sees the BoC sidelined until H2:2027. If we're right, short-term GoC bonds are poised to underperform U.S. Treasuries over the next year. Aided by a sidelined Fed, the underwhelming loonie may finally find its footing (see our latest **Forex**).

Chart 1: Surging job growth? We've seen this recently.
Canadian employment growth



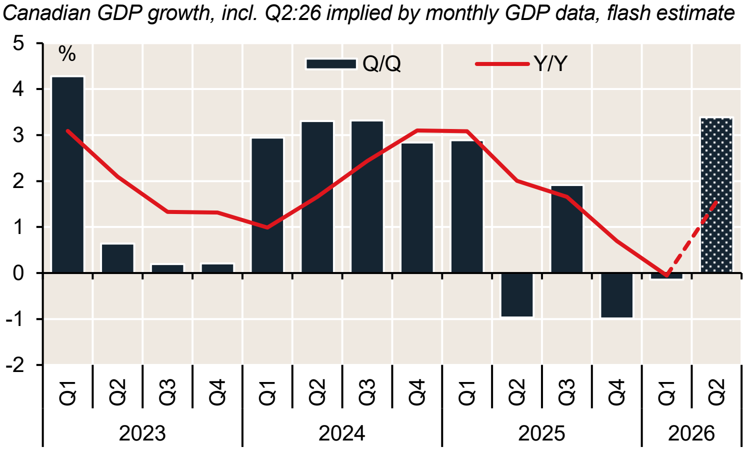
Source: NBC, StatCan

Chart 2: Hiring surges rarely unwind, despite recent episodes
3-month Canadian job growth (blue) following a 3% annualized hiring surge (teal)



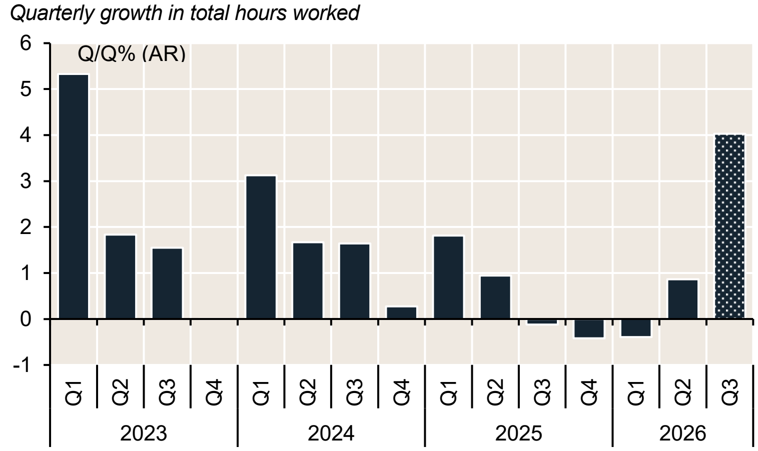
Source: NBC, StatCan | Note: Excl. 2020-22; only includes 1st month of 3% surge, if applicable.

Chart 3: Monthly GDP implies a sharp Q2 growth rebound...
Canadian GDP growth, incl. Q2:26 implied by monthly GDP data, flash estimate



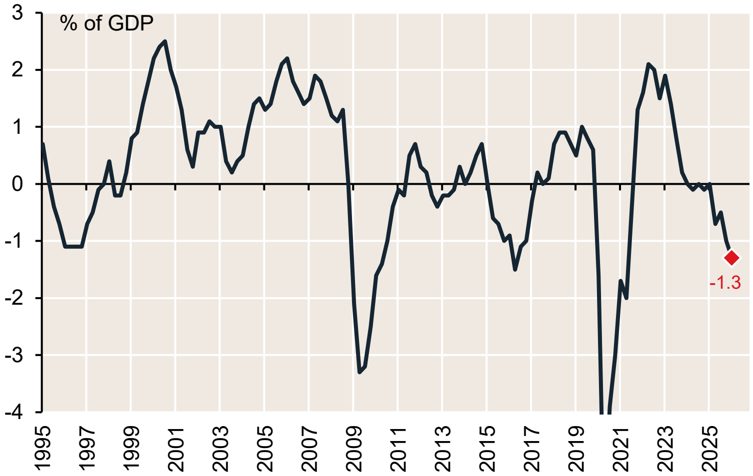
Source: NBC, StatCan

Chart 4: ...and hours worked sees momentum carried into Q3
Quarterly growth in total hours worked



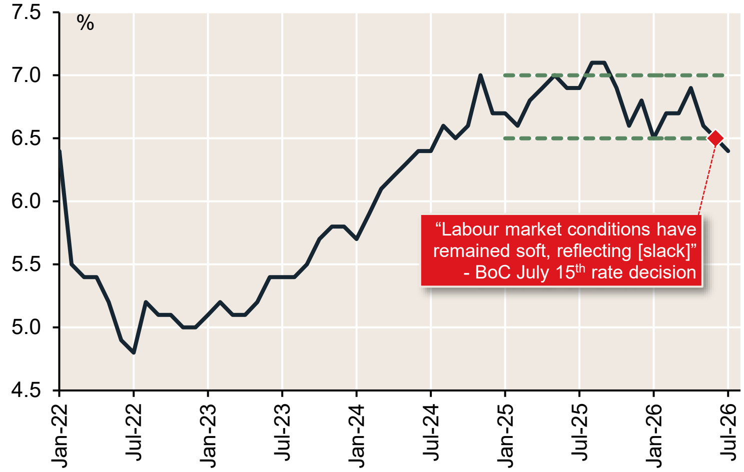
Source: NBC, StatCan | Note: Q3:26 based only on Jul-26, assumes no growth in Aug & Sep

Chart 5: One strong quarter (or two) won't eliminate slack
Bank of Canada estimate of output gap



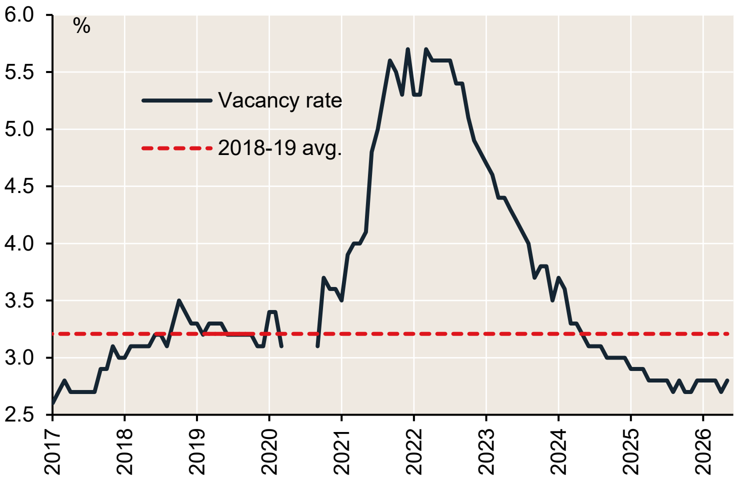
Source: NBC, BoC | Note: Latest estimate is for Q1:2026.

Chart 6: The BoC called labour market 'soft' with UR at 6.5%
Canadian unemployment rate



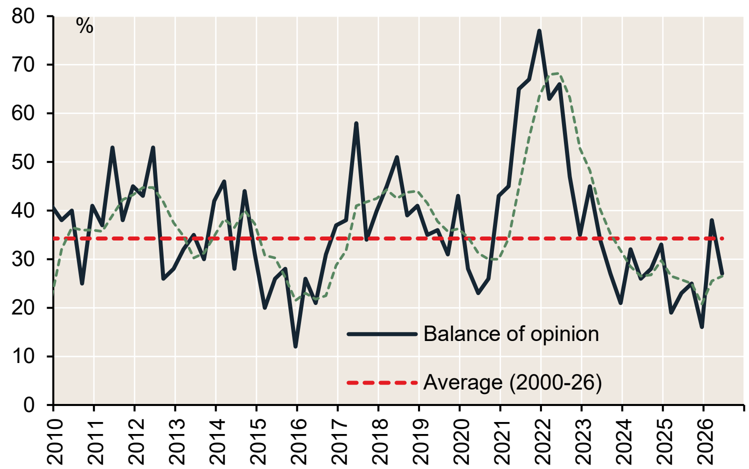
Source: NBC, StatCan, BoC

Chart 7: Despite job growth, labour demand remains cool…
Canada job vacancy rate



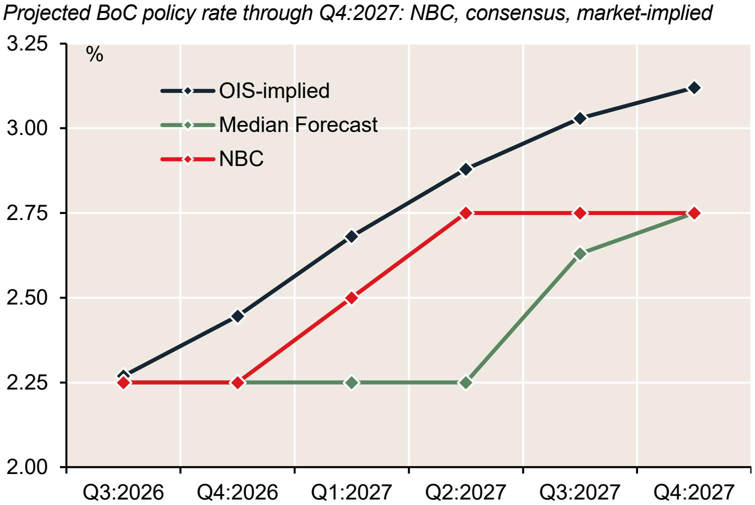
Source: NBC, StatCan

Chart 8: …and business hiring plans are hardly robust
Share of firms adding jobs less share of firms shedding jobs: Next 12 months



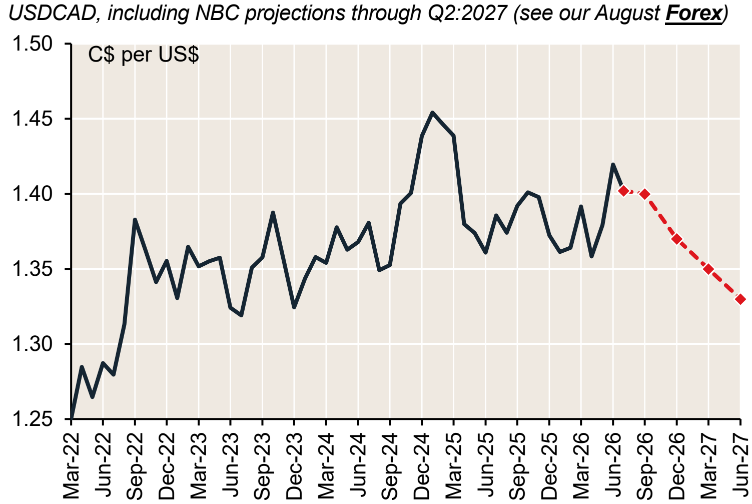
Source: NBC, BoC | Note: Dashed green line = 4Q moving average

Chart 9: We continue to view liftoff as a Q1:2027 event
Projected BoC policy rate through Q4:2027: NBC, consensus, market-implied



Source: NBC, Bloomberg | Note: Q4:2027 OIS-implied is estimated using CORRA futures. Median forecast per Bloomberg's July economic survey (published July 24th).

Chart 10: BoC hikes (and a steady Fed) will be C$-supportive
*USDCAD, including NBC projections through Q2:2027 (see our August **Forex**)*



Source: NBC, Bloomberg | Note: Historical data is monthly, NBC forecast is quarterly.

Economics and Strategy

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