Rates Scenario for August 13, 2026

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Forecast Summary

(avg.)	Actual	Forecasts									
	2026	2026					2027	2027			
	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Q1	Q2	Q3	Q4
BoC overnight[1]	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25
10-yr Canadas	3.55	3.65	3.65	3.65	3.65	3.65	3.60	3.60	3.50	3.45	3.50
Fed funds[1]	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.38	3.13
10-yr Treasuries	4.60	4.70	4.70	4.70	4.65	4.60	4.55	4.50	4.40	4.30	4.25
C$ per US$	1.41	1.40	1.39	1.39	1.38	1.38	1.38	1.37	1.36	1.35	1.33
US$/€	1.14	1.15	1.15	1.15	1.15	1.16	1.16	1.16	1.17	1.17	1.18
US$/£	1.34	1.35	1.35	1.35	1.35	1.35	1.35	1.35	1.35	1.36	1.36
¥/US$	162	159	158	158	157	156	156	155	154	153	152

[1] end of period

Sources: BMO Economics, Haver Analytics

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Canada-U.S. Rates

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To Hike, Or Not to Hike?

That is the question FOMC participants will be pondering when they gather again on September 15-16. We reckon the question will also be debated during subsequent confabs, as it was in the July 28-29 meeting, until the inflation all-clear signal is sounded.

Last month, the **FOMC left policy rates unchanged**, with the fed funds target range at 3.50%-to-3.75% for the fifth consecutive meeting. The vote was 9-to-3 with Cleveland President Hammack, Minneapolis' Kashkari, and Dallas' Logan dissenting in favour of a 25-bp rate hike. If the data and developments that drove this trio to vote for tightening last month were to continue thematically until next month, we judge more voters will jump on the tightening train. It takes at least seven (so four of the remaining nine) to switch policy onto a tightening track.

So far, the **post-confab data and developments have unfolded in a fashion that's unlikely to convince** more voters to jump on board, and those already on the tightening train to jump off. The uncompelling 0.2% increase in July's core CPI (0.22% unrounded) still caused the three-month trend to cool to 1.6% annualized thanks to June's anomalous flat reading. The PPI excluding food, energy and trade services rose 0.4%, which was a bit more concerning. Meanwhile, new tariffs are replacing expired ones with newly proposed others looming (meaning whatever inflationary impact is unfolding isn't over yet), as crude oil and particularly gasoline prices remain stubbornly high.

Elsewhere, July's **employment** data were weak. Payrolls slipped 23k leaving the three-month average up only 20k, while household-surveyed jobs dropped for the sixth time in the past seven months. However, the unemployment rate dipped a tenth to 4.1%, matching an 18-month low (the labour force has been contracting more than employment partly owing to restrictive immigration policy). The absence of a slackening trend probably pushes weak employment growth down the Fed's policy agenda amid 64 consecutive months (and counting) of inflation running above the 2% target.

There are just under five weeks to go until September's policy gathering, with another round of inflation and labour market data looming. If the Fed doesn't hike in September, doing so the following meeting (on October 28) could be trickier just six days before the midterm election. The market is currently pricing a 36% chance of a rate hike next month, rising to 58% by October, and 95% by December (with the trigger pulled by January).

As before, our base case has the Fed holding through the turn of the year, with the net short-term risk skewed to the hike side reflecting the net upside risk around our inflation forecast (which is back to 2% y/y around mid-2027). Apart from the expected absence of rate-hike-compelling data, we judge there's **another motivation for policy standing pat**. By the end of the year, most of the five task forces examining the Fed's conduct of monetary policy are expected to have their analyses completed and recommendations made. Should the FOMC adopt any of the recommendations, there's a chance that policy decisions deemed appropriate today might not appear similarly appropriate post-adoption. As next year unfolds, and core PCE inflation continues converging to 2%, we have 50 bps worth of rate cuts in the final trimester to align policy rates with their neutral range. Note that this is more than a year away and a lot can happen between now and then (including rate hikes).

Bank of Canada: Last month (July 15), the **Bank also left policy rates unchanged**, with the overnight rate target at 2.25% for the sixth consecutive meeting. In the press conference, Governor Macklem had three key messages. *"First, after stalling over the past year, economic growth looks to have resumed in Canada. While US trade policy continues to be a headwind, consumers have been resilient and businesses are adapting."* Real GDP growth was -0.1% y/y in 2026 Q1 (registering negative quarter-to-quarter moves in three of the four quarters… but not big or broad enough to call it a recession). In the Monetary Policy Report, a solid 2.5% annualized gain was projected for Q2, but we're now tracking 3.8% (to be released August 28).

"Second, inflation in Canada is poised to ease gradually provided global oil prices decline from elevated levels." This is because there is a sizeable output gap exerting disinflationary pressure while the various core inflation metrics are already well-behaved. Indeed, for June (released after the BoC meeting), for both the CPI-trim (mean) and CPI-median, the three-, six- and 12-month changes were all running under 2% annualized. However, oil prices have remained elevated, with Macklem having reiterated that *"the longer they remain elevated, the bigger the risk they spill over to other goods and services"* and that *"we will not let higher oil prices become persistent inflation."*

"Third, uncertainty remains elevated. The conflict in the Middle East has re-escalated in recent days and trade discussions with the United States are ongoing." Nearly a month after the fact, with an August 19 deadline for new tariffs on Canada looming and WTI crude oil prices still topping US$80, the message remains pertinent.

The juxtapositions of favourable core inflation dynamics amid lingering oil-related upside risks, along with improving economic performance amid rising U.S. trade policy risks, are the stuff of policy rate stability well into next year. This is contrary to the market's pricing of a rate hike by January. However, longer term (say, sometime in 2028), we could see the Bank moving policy rates closer to the midpoint of the 2.25%-to-3.25% neutral range.

Bond yields: Ten-year Treasury yields averaged 4.60% last month, the fourth-highest mark in 19 years (since July 2007 which saw the last '5-handle'), surpassed by 4.63% in January 2025 (as the Trump Administration took the reins), 4.80% in September 2023 (in the wake of the Fed's 525-bp tightening tear), and 4.67% in August 2007. Through mid-August, yields are already averaging 4.68%, to potentially take possession of second place. The (net) upward pressure reflects a trifecta of forces.

First, **higher Fed policy rate expectations and risks**. The latter was given additional impetus by the Fed now employing less forward guidance and as the market awaits the outcomes of the five task forces.

Second, **higher inflation expectations and risks**. In the wake of the Iran war, inflation expectations (from 10-year TIPS) averaged a 45-month high of 2.44% in May but are averaging around 2¼% so far in August (showing essentially no net change over the year). Of course, the volatility itself is what is partly prodding higher inflation risk premiums.

Third, **deteriorating U.S. fiscal prospects and rising credit risks**. Even before the cost of the Iran war and tariff refunds, debt, interest payments, and deficits were already on unsustainable paths.

We look for yields to average a mostly sideways pattern over the next several months with the net risk of a higher profile (and a daily '5-handle' at one point can't be ruled out). However, by late next year, as Fed rate cuts come back into focus, yields should be averaging closer to around 4¼%.

Elsewhere, 10-year Canada-U.S. bond yield spreads continue to trade at or slightly more negative than -100 bps. Investors appear comfortable for now with such 'rich' spreads, perhaps eyeing Canada's superior core inflation performance and economic underperformance versus the U.S. (despite a decent Q2), along with a fiscal outlook that is not deteriorating as badly as south of the border. However, we expect spreads to narrow gradually again, particularly as next year's Fed cuts come into focus with the BoC standing pat (and looking to normalize over the long haul).

U.S. dollar: In recent months, the greenback has been driven by undulating geopolitical and global economic risks owing to the Iran war (the more the perceived risks, the more the big dollar benefits from its safe-haven role, and vice versa), along with oscillating Fed policy prospects (gaining as rate hike expectations mount, and vice versa). Note that some of the latter impact is tempered a bit by other major global central banks actually hiking rates and not just talking about it, including the European Central Bank, along with those of Japan, Norway, Australia, and New Zealand.

According to the Wall Street Journal Dollar Index, after averaging a near four-year low in February (recall the war 'started' on the 28th), the greenback appreciated nearly 3% by July. So far in August, it's averaging about 1% weaker. We reckon the USD will likely at least hold on to most of its through-July gain (if not grind stronger) as long as Fed rate hike expectations and uncertainty remain elevated, and oil prices (as a barometer of geopolitical risks) also remain elevated.

Canadian dollar: The loonie averaged C$1.411 or US$0.709 in July, the weakest level in 16 months (since new U.S. tariffs first came into effect in March 2025). On July 20, President Trump announced new 50% tariffs on about C$28 billion of Canadian goods effective August 19, invoking Section 338 of the Trade Act of 1930 for the first time in 96 years. Negotiations to avoid these new tariffs and lessen the burden of others are ongoing. Meanwhile, the July 1 outcome on the USMCA was as expected: it triggered an annual series of potentially difficult negotiations (although this seems to be getting muddled with the above-mentioned tariff negotiations).

As the U.S. dollar has weakened so far this month, the Canadian unit has gained but to a lesser degree (+0.8%) as U.S. trade policy uncertainty intensifies. Our working assumption is that the 338s will be postponed given active negotiations (and precedents), but anything could happen. It's primarily U.S. trade policy uncertainty and, to a lesser extent, better core inflation performance, that make the Bank of Canada much less likely than the Fed to live up to the market's tightening expectations over the short term. Presuming the above-mentioned uncertainty eventually ebbs and Fed rate cuts re-enter the market's musings, the Canadian dollar should improve. After averaging C$1.38 by year-end, we look for it to strengthen to C$1.33 by 2027-end.

Overseas

Jennifer Lee, Senior Economist

Although most central bank chiefs are shunning forward guidance, a view that was expressed politely but firmly in Sintra, it is pretty clear that **monetary policy is becoming more restrictive**; that is, outside of Canada and the U.S. Let's take a random walk and look at the latest decisions made since July....

The **RBA** stayed on hold for the second meeting in a row, unanimously voting to keep the cash rate at 4.35%. After Governor Bullock's late-July warning that "*the full effects of earlier hikes will take time to emerge*", this decision was not a shock. It tightened in each of the three meetings that began in February by a combined 75 bps, so financial conditions are now tighter than they once were, but this was a **hawkish hold**. The possibility of easing did not enter the conversation, nor should it, given the recent data for June: household spending jumped 0.8%; trade swung back into a surplus after exports surged 9.6%; both the headline and trimmed mean inflation rates were slightly better but still well above target; and, employment surged 76,300. The RBA is clearly not finished. According to the Governor, "*the Board remains concerned*" and "*we still need to see some further progress before the board can be confident that we are going to get inflation back to target with current monetary policy settings*." And, it is "*quite possible we need to raise rates again*." The view that "*inflation is still too high*" was stated twice in the Press Release, and though it is not expected to return to the midpoint of the 2%-to-3% target until late 2027, the risks are to the upside. No one wants high inflation to become embedded, so expect further tightening "*if upside risks materialize*".

The **BoJ** kept rates at "*around 1%*", though one voter wanted a 25 bp hike. This was one of the more intriguing decisions… although it was widely expected, there was an element of hope that maybe, just maybe, the Policy Board would hike, which would throw USDJPY off the 40-year extreme of ¥164. The currency has strengthened since the announcement (to ¥155 at one point) as the MoF and the U.S. Treasury intervened (at the expense of the EUR). The BoJ still sounded hawkish given that it saw upside risks to CPI, and that wage increases (labour shortage), higher prices for energy and semiconductors, along with the recent depreciation of the yen, "*are likely to lead to an increase in prices*". Indeed. Also, the Bank suggested that it could "*speed up the pace*" of hikes. Our expectation for a September move hasn't budged.

The **ECB** maintained its deposit rate at 2.25% in late July, as it was too soon to move since the June hike. Still… the line in the Press Release that the "*full inflationary impact of the energy shock has yet to play out*" likely prepares the market for a September increase. And since that meeting, the extreme heat has the potential for more price pressures: freight rates are near 15-year highs, and some nuclear and coal plants were forced to close after water levels dried up to record lows in rivers across Europe, including the Rhine, Danube and Vistula.

The **BoE** kept its Bank Rate at 3.75%, but there was disagreement, with three policymakers voting to hike rates 25 bps. That's one more than in June, and two more compared to April. The differences between both camps were mainly on the second-round effects (were there any and where?), and past disinflation trends. So… inflation expectations and wage demands will be eyed carefully, and if there are signs of second-round effects, the Bank will be more inclined to hike, but not until there is more "*material*" evidence. Throwing a log on the fire was the latest KPMG and REC jobs report, which showed "*stronger increases*" in starting salaries for permanent and temporary workers as more job vacancies became available. It was also helpful that the economy grew 0.4% in Q2, or +1.7% a.r., and 0.3% in June alone, although the World Cup played a key role.

Elsewhere, the **Norges Bank** kept the policy rate at 4.25% but cautioned that although inflation has slowed, it was "*too early to conclude*" that the outlook had changed. So, "*it may thus still become necessary to raise the policy rate.*" The **Reserve Bank of New Zealand** hiked for the first time in three years, lifting the OCR by 25 bps to a 9-month high of 2.50%, and warned that "*some further reduction in monetary stimulus is likely*." And, the **Bank of Korea** raised its repo rate 25 bps to 2.75%, its first hike in 3½ years, with warnings of more to come. In fact, it "*will respond until we are confident*" that inflation is heading back to the target.

Foreign Exchange Forecasts

(local currency per US$: avg.)	Actual 2026 Jul	Forecasts 2026 Aug	Sep	Oct	Nov	Dec	2027 Jan	2027 Q1	Q2	Q3	Q4
Canadian Dollar											
C$ per US$	1.41	1.40	1.39	1.39	1.38	1.38	1.38	1.37	1.36	1.35	1.33
US$ per C$[1]	0.709	0.717	0.719	0.721	0.723	0.725	0.727	0.729	0.736	0.743	0.750
Trade-weighted	111.1	111.7	111.9	112.2	112.4	112.6	112.9	113.2	113.9	114.7	115.5
U.S. Dollar											
Trade-weighted[2]	120.6	119.3	119.1	119.0	118.8	118.7	118.5	118.3	117.7	117.1	116.6
European Currencies											
Euro[1]	1.14	1.15	1.15	1.15	1.15	1.16	1.16	1.16	1.17	1.17	1.18
Danish Krone	6.54	6.50	6.50	6.50	6.45	6.45	6.45	6.45	6.40	6.40	6.35
Norwegian Krone	9.69	9.50	9.50	9.50	9.50	9.50	9.50	9.50	9.45	9.40	9.35
Swedish Krona	9.67	9.55	9.55	9.55	9.55	9.55	9.50	9.50	9.45	9.40	9.35
Swiss Franc	0.81	0.81	0.81	0.80	0.80	0.80	0.79	0.79	0.79	0.78	0.78
U.K. Pound[1]	1.34	1.35	1.35	1.35	1.35	1.35	1.35	1.35	1.35	1.36	1.36
Asian Currencies											
Chinese Yuan	6.78	6.74	6.74	6.75	6.75	6.75	6.75	6.75	6.74	6.73	6.72
Japanese Yen	162	159	158	158	157	156	156	155	154	153	152
Korean Won	1,486	1,420	1,420	1,420	1,420	1,420	1,420	1,415	1,415	1,415	1,415
Indian Rupee	95.9	95.4	95.4	95.4	95.5	95.5	95.5	95.4	95.3	95.2	95.1
Singapore Dollar	1.29	1.28	1.28	1.28	1.28	1.28	1.28	1.28	1.28	1.28	1.28
Malaysian Ringgit	4.08	4.10	4.10	4.10	4.10	4.10	4.10	4.10	4.10	4.10	4.10
Thai Baht	33.5	33.1	33.1	33.1	33.1	33.1	33.1	33.1	33.1	33.0	33.0
Philippine Peso	61.6	61.2	61.2	61.3	61.3	61.4	61.3	61.3	61.3	61.2	61.1
Taiwan Dollar	32.2	32.2	32.1	32.1	32.1	32.1	32.1	32.1	32.0	32.0	32.0
Indonesian Rupiah	18,007	17,865	17,870	17,870	17,875	17,880	17,870	17,865	17,845	17,825	17,805
Other Currencies											
Australian Dollar[1]	0.697	0.706	0.706	0.706	0.705	0.705	0.706	0.708	0.711	0.715	0.719
New Zealand Dollar[1]	0.579	0.586	0.587	0.588	0.589	0.590	0.591	0.592	0.594	0.597	0.599
Mexican Peso	17.46	17.10	17.05	17.05	17.00	17.00	16.95	16.90	16.80	16.65	16.55
Brazilian Real	5.11	5.15	5.10	5.10	5.05	5.00	5.00	4.95	4.90	4.85	4.75
South African Rand	16.5	16.2	16.1	16.1	16.0	16.0	16.0	16.0	15.9	15.8	15.8
Cross Rates											
Versus Canadian Dollar											
Euro (C$/€)	1.61	1.60	1.60	1.60	1.60	1.59	1.59	1.59	1.58	1.58	1.57
U.K. Pound (C$/£)	1.89	1.88	1.88	1.87	1.87	1.86	1.86	1.85	1.84	1.83	1.81
Japanese Yen (¥/C$)	115	114	114	114	113	113	113	113	114	114	114
Australian Dollar (C$/A$)	0.98	0.98	0.98	0.98	0.98	0.97	0.97	0.97	0.97	0.96	0.96
Versus Euro											
U.K. Pound (£/€)	0.85	0.85	0.85	0.85	0.85	0.86	0.86	0.86	0.86	0.86	0.87
Japanese Yen (¥/€)	185	183	182	182	181	180	180	180	180	180	179

[1] (US$ per local currency); [2] Federal Reserve Broad Index
Sources: BMO Economics, Haver Analytics

Interest Rate Forecasts

(% : avg.)	Actual 2026 Jul	Forecasts 2026 Aug	Sep	Oct	Nov	Dec	2027 Jan	2027 Q1	Q2	Q3	Q4
Canada											
Overnight target (period end)	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25
Overnight target	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25	2.25
CORRA[2]	2.30	2.28	2.25	2.22	2.22	2.22	2.22	2.22	2.22	2.22	2.22
3-month bills	2.26	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30	2.30
6-month	2.36	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40	2.40
1-year	2.59	2.65	2.60	2.55	2.50	2.45	2.45	2.45	2.45	2.45	2.45
2-year bonds	2.84	2.95	2.85	2.75	2.60	2.50	2.50	2.50	2.50	2.50	2.50
3-year	2.96	3.05	3.00	2.90	2.85	2.80	2.80	2.80	2.75	2.75	2.75
5-year	3.16	3.30	3.25	3.15	3.10	3.05	3.05	3.05	3.05	3.00	3.00
7-year	3.30	3.40	3.40	3.40	3.35	3.35	3.35	3.35	3.30	3.30	3.25
10-year	3.55	3.65	3.65	3.65	3.65	3.65	3.60	3.60	3.50	3.45	3.50
30-year	3.95	4.05	4.05	4.05	4.05	4.05	4.00	4.00	3.90	3.85	3.90
Prime rate	4.45	4.45	4.45	4.45	4.45	4.45	4.45	4.45	4.45	4.45	4.45
United States											
Fed funds target (period end)	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.38	3.13
Fed funds target	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.60	3.33
EFFR[3]	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.61	3.34
SOFR[4]	3.62	3.63	3.62	3.62	3.62	3.62	3.62	3.62	3.62	3.60	3.33
3-month bills	3.87	3.90	3.85	3.85	3.85	3.85	3.85	3.85	3.85	3.80	3.45
6-month	4.00	4.00	3.95	3.95	3.95	3.95	3.95	3.95	3.95	3.95	3.55
1-year	4.05	4.00	4.00	4.00	4.00	3.95	3.90	3.90	3.80	3.65	3.40
2-year notes	4.22	4.20	4.20	4.20	4.15	4.05	4.00	3.90	3.70	3.45	3.30
3-year	4.26	4.25	4.25	4.25	4.20	4.15	4.10	4.00	3.85	3.65	3.55
5-year	4.33	4.40	4.40	4.40	4.35	4.25	4.20	4.15	4.00	3.85	3.75
7-year	4.46	4.50	4.50	4.50	4.45	4.45	4.40	4.35	4.20	4.10	4.00
10-year	4.60	4.70	4.70	4.70	4.65	4.60	4.55	4.50	4.40	4.30	4.25
30-year bonds	5.10	5.25	5.25	5.25	5.20	5.15	5.10	5.05	4.95	4.85	4.80
Prime rate	6.75	6.75	6.75	6.75	6.75	6.75	6.75	6.75	6.75	6.73	6.46
Other G7											
ECB Deposit Rate[1]	2.25	2.25	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50
10yr Bund	3.09	3.20	3.30	3.40	3.50	3.60	3.55	3.50	3.30	3.10	2.95
BoE Bank Rate[1]	3.75	3.75	3.75	3.75	3.75	3.75	3.75	4.00	4.00	4.00	4.00
SONIA[5]	3.73	3.73	3.73	3.73	3.73	3.73	3.73	3.89	3.98	3.98	3.98
10yr Gilt	4.95	5.00	5.10	5.15	5.25	5.30	5.25	5.20	5.00	4.80	4.65
BoJ O/N[1]	1.00	1.00	1.25	1.25	1.25	1.25	1.25	1.50	1.50	1.75	1.75
10yr JGB	2.77	2.82	2.82	2.81	2.81	2.80	2.79	2.78	2.76	2.73	2.71

[1] end of period; [2] Canadian Overnight Repo Rate Average; [3] Effective Fed Funds Rate; [4] Secured Overnight Financing Rate;
[5] Sterling Overnight Index Average

Sources: BMO Economics, Haver Analytics

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