Weekly Bottom Line

TD Economics / TD Securities · 2026-09-04 · English original

- Category:
- Canada

Canadian Highlights

- The Bank of Canada held rates at 2.25% but struck a more hawkish tone, citing elevated energy prices and upside risks to inflation.
- Canada's labour market lost some momentum in August, shedding over 40k jobs. The unemployment rate remained stable at 6.4%.
- July trade data showed a partial unwinding of Q2's net export contribution. Tariff-related distortions are likely to keep trade flows volatile in the months ahead.

U.S. Highlights

- Treasury yields moved higher this week amid uncertainty about the Fed's next move, higher oil prices and ongoing fiscal concerns.
- Vehicle sales, ISM business surveys and the Beige Book's anecdotal evidence all pointed to continued economic expansion in August.
- Payrolls surprised to the upside in August, with employers adding 162k new jobs, while the unemployment rate held steady at 4.1%.

Canada – A Complicated Outlook

This week featured a jam-packed calendar with the Bank of Canada (BoC) taking center stage. The Bank left its policy rate unchanged at 2.25% for a seventh consecutive meeting, a move that was widely expected by markets. The BoC acknowledged the economy's recent momentum but also flagged that the recovery is set to face a new set of hurdles with the escalation in trade tensions with the U.S. Their tone on new U.S. tariffs – and forthcoming Canadian counter-tariffs effective next week – is that increasing frictions represent more of a confidence risk as opposed to a material hit to growth and inflation. That doesn't take away from the fact that a smaller subset of industries (autos, steel, aluminum, and lumber) will continue to bear the brunt of the trade war.

More notably, the Bank leaned into the risks stemming from a prolonged conflict in the Middle East. They noted that still-elevated oil prices have "increased the upside risks to the outlook for inflation". It was a key message in the BoC's communications that markets interpreted as modestly hawkish. Markets initially repriced the probability of a 25 basis point (bps) hike by year-end to nearly 100% (60% prior to the announcement) with a cumulative three hikes priced in by mid-2027. Despite the market reaction, core inflation pressures remain broadly contained (Chart 1) and tariff-related risks are pulling growth and inflation risks in opposite directions. This should warrant a more cautious central bank stance and underpins our assessment that the Bank of Canada should be in a comfortable holding pattern for now.

And this week's domestic data flow supports this view. Employment sagged by 41k jobs in August – though an offsetting decline in the labour force left the unemployment rate steady at 6.4% – while wage growth softened to 2%. August reversed part of the employment gains recorded in recent months and highlights that excess supply remains in the economy, even as broader measures of activity continue to improve.

Meanwhile, merchandise trade data for July showed a pullback in export activity and a rebound in imports, marking a partial reversal of Q2's outsized contribution from net exports. Trade flows may very well see a temporary boost from businesses rushing shipments ahead of higher tariffs, but these gains are unlikely to be sustained. This should keep net trade contributions volatile in the quarters ahead as new levies weigh on cross-border flows.

The conversation is likely shifting from whether growth can recover to whether inflation will prove more persistent. Markets have begun to price that possibility, but we would caution against getting too far ahead of the data. A still-recovering labour market, moderating wage growth, and renewed trade uncertainty are hardly conditions that demand a more restrictive policy stance. By the week's end, Canadian 2-year bond yields settled 9 basis points (bps) higher while the Loonie gained roughly three-tenths of a cent against the U.S. dollar.

U.S. – A Hawkish Assessment, Still No Forward Guidance

Bond markets dominated the headlines this week. Following Chair Warsh's hawkish Jackson Hole speech, Treasury yields moved sharply higher on the week, with the 10-year yield briefly touching 4.82%, its highest level since late 2023. The move partially reversed after New York Fed President Williams and Governor Waller pushed back against the notion that a September rate hike was a fomanregone conclusion. Waller said he would be "inclined to support holding rates steady if inflation data continue to cooperate." Markets took the hint, with the implied odds of a September hike falling to a coin toss from nearly two-thirds earlier in the week, but retraced a bit on Friday following a strong jobs report.

That said, expectations for the Fed are only a small part of the story underpinning the recent rise in yields. A re-escalation in the Middle East conflict has pushed oil prices higher, with WTI currently hovering around $90 per barrel. At the same time, growing concerns around government debt burdens and a significant increase in investment grade debt issuance by the hyperscalers have added fuel to the fire. Ten-year Treasury yields remain roughly 60 basis points above year-ago levels, leading to some tightening in financial conditions even if the Fed ultimately remains on hold this month.

Away from the market turbulence, the economic data continued to point to a resilient economy. Vehicle sales rose to a healthy 16.8 million annualized pace in August, extending a six-month run above 16 million units. ISM business surveys also reinforced the resilient narrative, with both manufacturing and services indexes remaining well in expansionary territory, even as the manufacturing index edged lower on the month (Chart 1). Expansion in the services sector strengthened for a second consecutive month. The Beige Book painted a similar picture. Economic activity expanded modestly in 10 of 12 Federal Reserve districts, only one fewer than in July.

Friday's payroll report also brought good news. Hiring rose at its fastest pace in five months in August, adding 162k new positions – well above the 55k expected by the markets (Chart 2). Importantly, revisions to prior months were higher by 55k, which helped to flip July's initially reported pullback of -23k to a positive gain of 21k. Over the last three months, payrolls have averaged a healthy 71k. Meanwhile, the unemployment rate held steady at 4.1%, while the broader U-6 measure, which includes those who are marginally attached to the labor force, fell to a 14-month low of 7.7%. On balance, this was a very healthy jobs report and pushed back on any fears that may have surfaced following July’s setback.

At this point, all eyes now shift to next week’s inflation data. As we noted in a report released this week, a softer CPI reading would likely be enough to keep the Fed on hold, but a hotter report would solidify the case for some policy tightening. Exactly how much tightening the FOMC would undertake is up for debate, but given most Fed officials are of the mind that today’s policy stance is already “somewhat restrictive,” it likely wouldn’t be more than one or two quarter-point moves. Our baseline remains for the Fed to stay on hold in September, but much is riding on next week’s inflation data. Stay tuned!

Source: https://economics.td.com/ca-weekly-bottom-line