

Monthly forecast update



July 13,
2026

RBC Economics

Cyclical rebound in Canada and structural strength in the U.S.

Highlights:



Canada's economy is on track to rebound in Q2, driven by resilient household spending, recovering business investment and expanding net trade. Growth is expected to continue over the second half of 2026 with CUSMA exemptions still protecting most Canadian exports from U.S. tariffs.



The Bank of Canada is expected to remain on hold in 2026. Uncertainties around trade and energy prices are persisting but recent developments—broadly easing energy price growth and firming economic growth—have evolved broadly as expected, reaffirming the BoC's steady stance.



U.S. productivity growth has continued to surprise on the upside. We've raised our assumptions for GDP growth through the forecast horizon to 2027, driven by higher trend productivity growth rather than expected job growth. We now expect the economy will expand 2.2% in both 2026 and 2027.



The Federal Reserve is still expected to hold rates steady through 2027. Recent labour market improvement and higher-than-expected inflation readings are tilting risks towards more interest rate hikes from the Fed, but not yet by enough to shift our base case view of a hold.

Issue in focus:



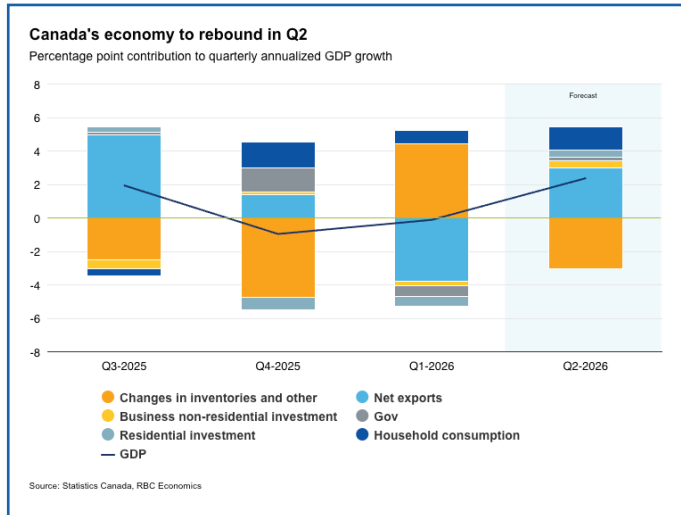
CUSMA remains in effect despite a lack of formal extension on July 1. The deal won't mechanically expire until a decade from now, and negotiations to extend that deadline have begun.

While an earlier termination is possible, it's not our base case assumption, and its economic impact has grown less dire as U.S. tariffs broadly continue to ease. Future negotiations may focus on the Rules of Origin requirements or U.S. trade policy alignment, although we expect little tangible changes near term.

Forecast changes:

Minor changes to Canada's forecast outside of stronger Q2 GDP growth

Canada's economy likely rebounded in Q2 after two quarters of stagnating activity. Consumer spending has proven resilient over a period of high gasoline prices cutting into households' buying power. Business investment has strengthened, and net trade is set to add significantly to growth.



We're now tracking stronger GDP growth in Q2 at 2.2% from 1.7% previously. Uncertainties around the CUSMA Joint Review (read below), and the Middle East conflict remain elevated. However, our longstanding assumptions about the CUSMA agreement and related exemptions being preserved, and a partial retracement of the spring global oil price surge have held up well.

Overall, we see less risk of higher or lower interest rates in the near term, as growth picks up while oil-related inflation concerns ease. Canada's unemployment rate remains high despite recent improvements, suggesting interest rates at the lower end of the estimated "neutral" range are still appropriate.

Raising labour productivity in the U.S. adds to GDP growth; Fed expected to stay put

Persistently strong labour productivity gains in the U.S.—averaging above an annualized 2 ½ % quarterly since the start of 2024—have led us to revise our GDP and potential GDP growth estimates slightly higher over the forecast period to 2027, but that should have a neutral impact on our inflation outlook.

As a starting point, however, U.S. inflation continues to run well above the Fed's 2% target even without the impact of energy prices, and the unemployment rate has remained historically low. That combination suggests the Fed will, at a minimum, need to maintain interest rates at current levels before more meaningful progress with inflation comes through to start the easing conversation again.

Our forecast still assumes a steady Fed until the end of 2027. Risks, however, are that further (non-energy) inflation flare-ups, while the unemployment rate stays low, suggest monetary policy may not be restrictive enough to propel inflation back toward the 2% target, and prompt more rate hikes.

Summary of changes in May:

- **We revised Canada's Q2 2026 GDP growth estimate higher** from 1.7% annualized growth to 2.2%. Our annual growth projection for 2026 edged up to 0.7% from 0.6% as a result.
- **Other forecasts are unchanged for Canada.** We continue to expect the BoC will hold rates steady in 2026 before hiking modestly in 2027, contingent on the economy and labour markets improving over the interim without stoking inflation.
- **U.S. GDP and potential GDP growth estimates were raised through 2027**, driven by stronger assumed trend productivity gains. The output gap estimates were also revised to be slightly more positive but remain within the 0 to 0.5% range in 2026 and 2027.
- **The Federal Reserve is expected to hold rates steady.** We forecast the Fed Funds range will remain at 3.5%–3.75% through 2027, with risks shifting toward a more hawkish Fed.

Central bank	current policy rate	next decision	
	2.25% 0 bps in Jun/26	0 bps Jul/26	The BoC held the overnight rate at 2.25% in June with Governor Tiff Macklem reiterating the current stance of monetary policy remains appropriate to balance the growth-inflation trade-off. Recent developments (stronger growth, lower oil prices) should have eased concerns on both sides of that trade-off. We continue to expect no changes to the overnight rate in 2026 before moderate hikes in 2027.
	3.5-3.75% 0 bps in Jun/26	0 bps Jul/26	The Fed held interest rates steady in June with a decidedly hawkish pivot. The updated dot plot (submitted before recent easing in oil prices) showed expectations for tighter monetary policy in 2026 relative to April. The statement was short but blunt with a focus on inflation, while worries about the labour market took a backseat. We expect the Fed Funds rate will be held at moderately restrictive levels through 2027.
	3.75% 0 bps in Jun/26	0 bps Jul/26	The Bank of England's Monetary Policy Committee voted 7-2 in favour of holding Bank Rate at 3.75% in June, but retained a moderate hiking bias. Still, a run of weaker domestic data (CPI, PMIs, wages) and lower oil prices have led us to revise our forecast to now expect no more hikes from the MPC. Instead, we expect the bank rate will be held steady at 3.75% for the foreseeable future.
	2.25% +25 bps in Jun/26	0 bps Jul/26	The European Central Bank raised the deposit rate by 25 basis points in June as expected. Easing oil prices since then have reduced the risk of indirect/second round effects on inflation although the ECB's stance has been consistently hawkish despite the oil move. We expect it to err on the side of caution and hike once more in September, bringing the deposit rate to a terminal of 2.5%.
	4.35% 0 bps in Jun/26	0 bps Aug/26	The Reserve Bank of Australia left the cash rate unchanged in a unanimous vote in June, still placing strong emphasis on above-target inflation, but also acknowledged soft data and tighter financial conditions. With oil prices trending lower, we don't foresee enough inflation pressures that could force the RBA back into action. We now expect the RBA will maintain the 4.35% cash rate through the forecast period.

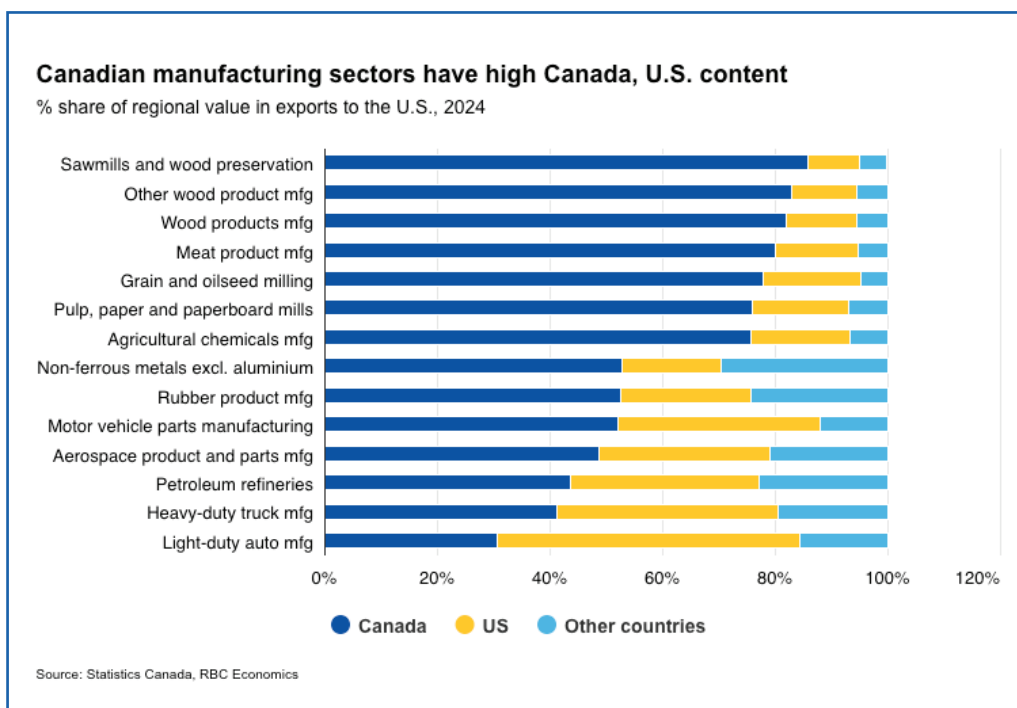
Issue in focus

Navigating the CUSMA Joint Review: Where we go from here

CUSMA has served as a critical backstop for Canada-U.S. trade amid U.S. tariffs. While no deal was reached on July 1 to extend the free trade agreement, it doesn't expire until 2036.

Broadly, we assume that neither the specifics of CUSMA nor the effectiveness of related exemptions will meaningfully change this year as a result of the review. Businesses seeking immediate resolutions will be disappointed, but the impact of a (unlikely) CUSMA termination has also grown less significant.

Over the last few months, not only has the tariff rate that would replace CUSMA trended lower, the share of CUSMA protected trade has also gotten smaller as other tariff exemptions expand. Under current U.S. tariff schedules, we estimate about a third of Canada's exports to the U.S. are at risk of seeing a 10% tariff should CUSMA lapse—not all of the about 90% that's exempt from tariffs.



Interest rate outlook | July 2026

Policy rates and government bond yields, end of period

	Q1-25	Q2-25	Q3-25	Q4-25	Q1-26	Q2-26	Q3-26	Q4-26	Q1-27	Q2-27	Q3-27	Q4-27
Canada												
Overnight rate	2.75	2.75	2.50	2.25	2.25	2.25	2.25	2.25	2.50	2.75	3.00	3.25
3-month	2.62	2.65	2.42	2.15	2.31	2.26	2.20	2.25	2.55	2.80	3.00	3.20
2-year	2.46	2.59	2.47	2.58	2.82	2.74	2.75	3.10	3.25	3.30	3.35	3.40
5-year	2.61	2.83	2.74	2.96	3.09	3.01	3.05	3.30	3.40	3.45	3.50	3.50
10-year	2.97	3.28	3.18	3.42	3.46	3.38	3.45	3.60	3.60	3.60	3.60	3.60
30-year	3.23	3.56	3.64	3.85	3.88	3.77	3.85	3.85	3.80	3.80	3.75	3.75
United States												
Fed funds midpoint	4.38	4.38	4.13	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.63	3.63
3-month	4.32	4.41	4.02	3.67	3.70	3.87	3.70	3.67	3.65	3.65	3.65	3.65
2-year	3.89	3.72	3.60	3.47	3.79	4.14	4.25	4.15	4.35	4.45	4.35	4.30
5-year	3.96	3.79	3.74	3.73	3.92	4.19	4.30	4.15	4.30	4.35	4.25	4.20
10-year	4.23	4.24	4.16	4.18	4.30	4.44	4.50	4.35	4.45	4.50	4.45	4.40
30-year	4.59	4.78	4.73	4.84	4.88	4.91	4.95	4.80	4.90	4.95	4.90	4.85
United Kingdom												
Bank Rate	4.50	4.25	4.00	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75
2-year	4.20	3.81	3.99	3.71	4.37	4.22	4.10	4.05	4.00	4.00	4.10	4.20
5-year	4.29	3.95	4.14	3.93	4.43	4.31	4.30	4.25	4.20	4.20	4.30	4.40
10-year	4.70	4.48	4.70	4.47	4.88	4.76	4.85	4.80	4.75	4.80	4.90	5.00
30-year	5.29	5.25	5.49	5.21	5.49	5.51	5.65	5.70	5.70	5.80	5.90	6.00
Euro area*												
Deposit rate	2.50	2.00	2.00	2.00	2.00	2.25	2.50	2.50	2.50	2.50	2.50	2.50
2-year	2.05	1.85	2.02	2.12	2.58	2.53	2.70	2.80	2.70	2.70	2.60	2.60
5-year	2.34	2.15	2.31	2.45	2.69	2.60	2.80	2.90	2.80	2.80	2.75	2.75
10-year	2.74	2.59	2.72	2.86	2.98	2.92	3.20	3.25	3.20	3.25	3.30	3.40
30-year	3.09	3.12	3.30	3.48	3.46	3.44	3.80	3.90	4.00	4.10	4.20	4.30
Australia												
Cash rate	4.10	3.85	3.60	3.60	4.10	4.35	4.35	4.35	4.35	4.35	4.35	4.10
2-year	3.68	3.21	3.49	4.06	4.66	4.42	4.35	4.25	4.25	4.10	4.00	3.95
5-year	3.86	3.46	3.75	4.29	4.70	4.40	4.40	4.35	4.35	4.30	4.30	4.30
10-year	4.39	4.16	4.30	4.75	4.98	4.72	4.80	4.60	4.65	4.70	4.60	4.55
30-year	4.97	4.84	4.96	5.22	5.36	5.25	5.25	5.05	5.10	5.15	5.05	5.00
New Zealand												
Cash rate	3.75	3.25	3.00	2.25	2.25	2.25	2.75	3.00	3.00	3.00	3.00	3.00
2-year swap	3.33	3.18	2.60	2.92	3.45	3.31	3.50	3.40	3.30	3.30	3.30	3.30
10-year swap	4.05	4.03	3.66	4.08	4.34	3.99	4.30	4.15	4.25	4.30	4.25	4.20

Sources: Refinitiv, BoC, Fed, BoE, ECB, RBA, RBNZ, RBC Economics, RBC Capital Markets | *German government bond yields

Economic outlook | July 2026

Real GDP, quarter-over-quarter percent change

	Q1-25	Q2-25	Q3-25	Q4-25	Q1-26	Q2-26	Q3-26	Q4-26	Q1-27	Q2-27	Q3-27	Q4-27	2025	2026	2027
Canada*	2.9	-1.0	1.9	-1.0	-0.1	2.2	1.8	1.5	1.3	1.3	1.5	1.7	1.9	0.7	1.5
United States*	-0.6	3.8	4.4	0.5	2.1	2.4	2.1	2.2	2.2	2.3	2.3	2.2	2.1	2.2	2.2
United Kingdom	0.6	0.2	0.1	0.1	0.6	0.2	0.1	0.2	0.3	0.3	0.3	0.3	1.3	1.0	1.0
Euro area	0.7	0.1	0.3	0.2	-0.2	0.3	0.2	0.4	0.3	0.3	0.2	0.2	1.5	0.4	1.2
Australia	0.3	1.0	0.4	0.9	0.3	0.1	0.3	0.3	0.4	0.4	0.5	0.5	2.0	1.7	1.5

*annualized

Inflation, year-over-year percent change

	Q1-25	Q2-25	Q3-25	Q4-25	Q1-26	Q2-26	Q3-26	Q4-26	Q1-27	Q2-27	Q3-27	Q4-27	2025	2026	2027
Canada	2.3	1.8	2.0	2.2	2.2	2.9	2.5	2.2	2.2	1.6	2.1	2.1	2.1	2.4	2.0
United States	2.7	2.4	2.9	2.7	2.7	3.9	3.0	2.8	2.3	1.3	1.9	1.9	2.7	3.1	1.9
United Kingdom	2.8	3.5	3.8	3.4	3.1	3.1	3.4	3.7	2.6	2.4	1.9	1.9	3.4	3.3	2.2
Euro area	2.3	2.0	2.1	2.1	2.0	3.0	2.8	2.9	2.6	2.0	2.2	2.1	2.1	2.7	2.2
Australia	2.4	2.1	3.2	3.6	4.1	4.4	3.9	4.2	3.8	3.4	3.2	2.9	2.8	4.2	4.1

Sources: StatCan, BLS, ONS, EuroStat, ABS, RBC Economics, RBC Capital Markets

Currency outlook | July 2026

US dollar cross rates, end of period

	Q1-25	Q2-25	Q3-25	Q4-25	Q1-26	Q2-26	Q3-26	Q4-26	Q1-27	Q2-27	Q3-27	Q4-27
USD/CAD	1.44	1.36	1.39	1.37	1.40	1.42						
EUR/USD	1.08	1.18	1.17	1.17	1.15	1.14						
GBP/USD	1.29	1.37	1.34	1.34	1.32	1.33						
USD/JPY	149.9	144.2	148.0	156.8	159.1	162.6						
AUD/USD	0.62	0.66	0.66	0.67	0.69	0.69						

Under Review

Canadian dollar cross rates

	Q1-25	Q2-25	Q3-25	Q4-25	Q1-26	Q2-26	Q3-26	Q4-26	Q1-27	Q2-27	Q3-27	Q4-27
EUR/CAD	1.55	1.60	1.63	1.61	1.61	1.62						
GBP/CAD	1.86	1.87	1.88	1.84	1.84	1.88						
CAD/JPY	104.3	105.7	106.1	114.4	114.2	114.4						
AUD/CAD	0.90	0.89	0.92	0.91	0.96	0.98						

Under Review

Sources: Federal Reserve Board, Bank of Canada, RBC Economics, RBC Capital Markets

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