Interest Rates, Energy Prices, & the Economy: Impacts on Auto Dealers.

BMO Economics Contributions to the 2026 Q3 Dealer Finance Report

Welcome to our quarterly publication focusing on the automotive industry, the goal of this report is to give you an overview of what we're hearing and seeing in the market both locally and across our shared border.

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Interest Rates and the Oil Shock

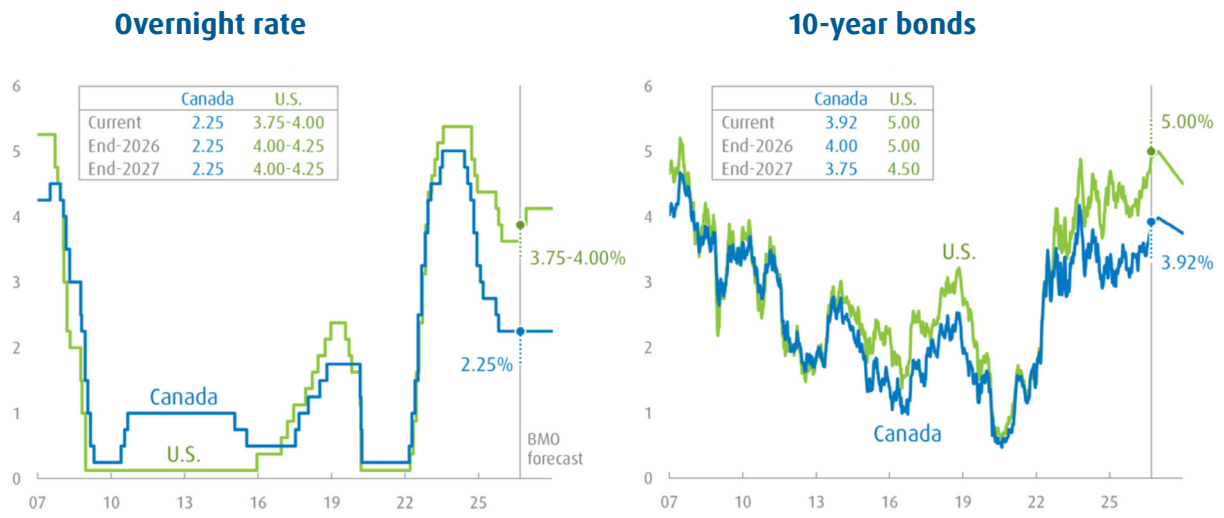
- The sharp rebound in energy prices has changed the interest rate outlook West Texas Intermediate (WTI) is currently over U.S. $100 per barrel adding to near-term inflation pressures and pushing government bond yields higher on both sides of the border.
- In the United States, August core CPI rose 0.3% as firm services inflation reinforced concerns that higher energy costs could spread to broader prices. BMO Economics now expects the **Federal Reserve to follow up its September hike by raising rates by 25 basis points in December**, taking the target range to 4.00%–4.25%.
- Longer-term borrowing costs have risen alongside that revised outlook. The 10-year Treasury yield recently hit 5% on September 15 while the 30-year mortgage rate moved above 7%.
- In Canada, the Bank of Canada is expected to hold the overnight rate at 2.25% through 2027. Higher oil prices and U.S. yields have lifted longer-term Canadian borrowing costs, but weak growth, core inflation near 2% and a soft labor market argue against renewed policy tightening.

Dealer Finance takeaway

Expected relief in vehicle-financing and floorplan costs could be delayed. Higher borrowing costs will keep affordability under pressure and reinforce customers' focus on monthly payments, vehicle size and price.

Fed to hike, Bank of Canada to hold steady through 2027[1]

(%: September 16, 2026)



[1] **Sources**: BMO Economics, Haver Analytics • BMO Capital Markets, © Copyright 2026 BMO Capital Markets, Corp. | https://economics.bmo.com

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North American Growth Outlook

- The two economies are entering the latest trade and energy shocks from very different positions. U.S. demand remains resilient, supported by consumer spending and strong business-equipment investment, while Canada's economy is expanding much more slowly and remains more exposed to the renewed trade dispute.
- Based on BMO Economics' forecast U.S. real GDP is expected to grow 2.1% in 2026 and 2.2% in 2027. Canada is expected to grow just 1.0% in 2026 before improving to 1.8% in 2027.

Dealer Finance takeaway

U.S. vehicle demand should remain better supported by the broader economy, but higher financing costs are a growing constraint. In Canada, stable policy rates provide some protection, although trade uncertainty and slower income growth will continue to encourage cautious purchasing decisions.

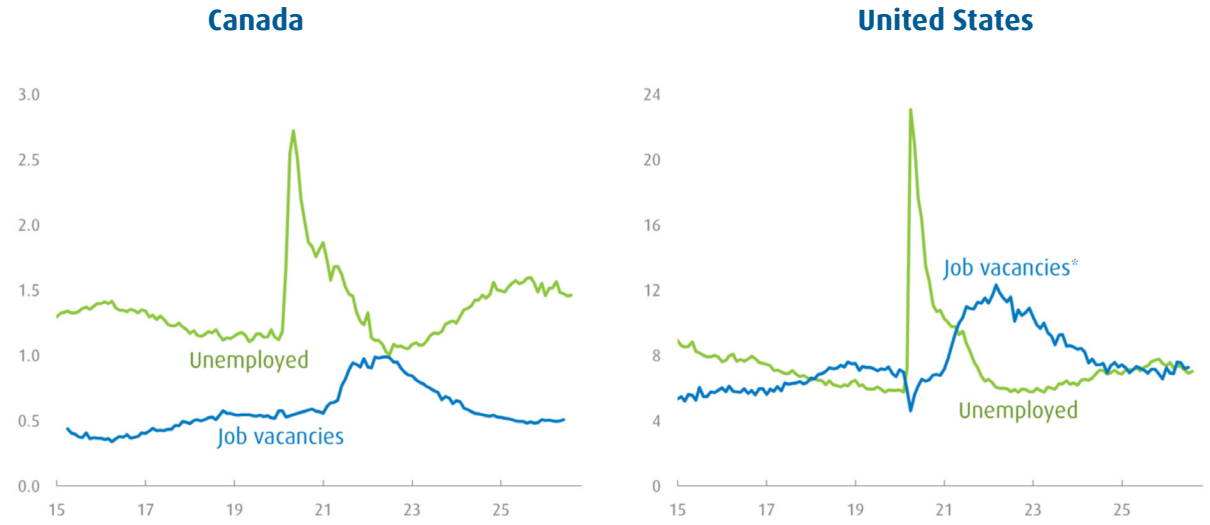
Labor Market Overview

- The U.S. labor market remains relatively stable, but employment growth has narrowed. Healthcare accounted for nearly half of the latest year-over-year increase in private payrolls, while employment elsewhere rose only modestly.
- BMO expects the U.S. unemployment rate to remain near 4.2% through 2027. The labor market is no longer overheating, but it has not weakened enough to materially undermine household spending.
- Conditions are softer in Canada. The unemployment rate is expected to average 6.6% in 2026 before gradually declining to 6.2% in 2027. Slower hiring, fewer vacancies and greater worker availability should restrain wage pressures, but also point to a more cautious consumer. Slower population growth could curb future vehicle sales growth.

Dealer Finance takeaway

A firm labor market continues to support vehicle demand, especially in the United States, but households have less room to absorb higher financing, fuel and insurance costs. Affordability-sensitive consumers are likely to keep moving toward lower-priced vehicles.

Labor market tightness is easing[1] (millions)



*Job Openings and Labor Turnover Survey (JOLTS)

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Automotive Industry Sales and Trade Overview

- North American vehicle demand has remained relatively resilient despite elevated financing and fuel costs. U.S. sales through August were 2.7% lower year-to-date, while Canadian sales were down a milder 1.2%.
- The limited decline in total sales partly reflects consumers' ability to substitute. Buyers facing higher prices can shift toward smaller vehicles, lower-priced models or comparable vehicles assembled outside the United States rather than leave the new-vehicle market altogether.
- Tariff exposure is therefore likely to be more concentrated by model and dealer than the aggregate sales figures suggest. Canada's existing auto surtax places the greatest pressure on U.S.-assembled vehicles with high U.S. content, particularly full-size pickups, large SUVs and some luxury and performance vehicles. Canadian-, Mexican- and overseas-built alternatives are less directly exposed.
- The larger risk is further escalation. The White House has threatened to raise tariffs on Canadian vehicles and parts to 50% on January 1, 2027. Motor vehicles accounted for about 7.6% of Canadian exports to the United States in the 12 months ending in June, with parts, bodies and trailers accounting for another 4.4%.
- That potential exposure is much larger than the latest Section 338 measures. According to the September 8 government notice, the revised Section 338 measures apply tariffs and import restrictions to specified Canadian goods but do not introduce additional measures targeting the auto sector. BMO Economics estimates that the measures affect approximately 5% of Canadian goods exports to the United States.
- A broad 50% auto tariff would disrupt integrated North American production, raise vehicle and parts costs, and reduce incentive activity. The risks also extend to medium- and heavy-duty trucks, including planned production at Ford's Oakville facility and GM's Silverado HD operations in Oshawa.

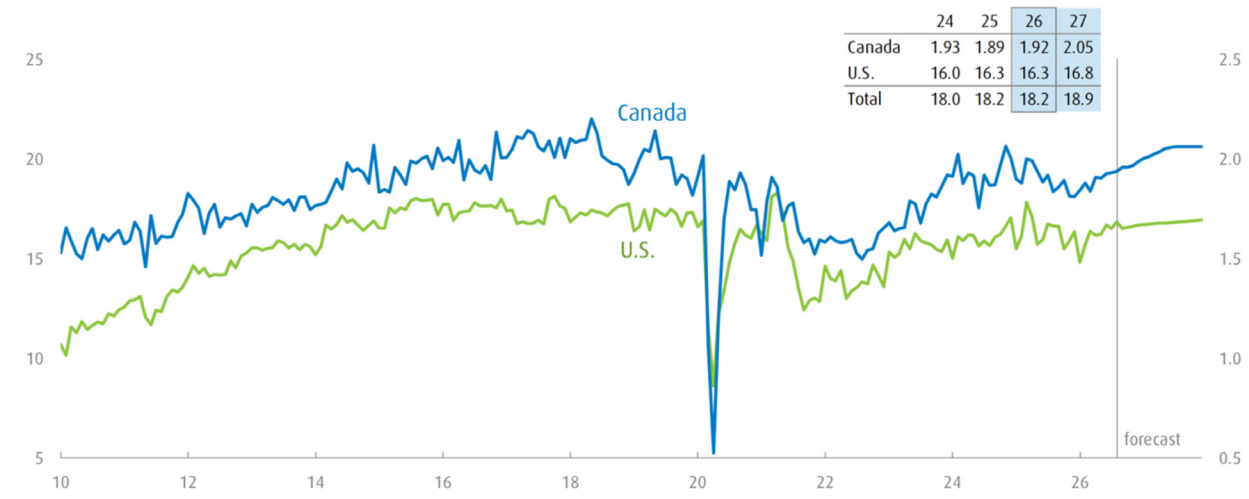
Dealer Finance takeaway

Near-term industry volumes remain relatively stable, but the impact of threatened tariffs will vary considerably by dealer and product mix. Dealers with a broader range of brands, vehicle classes and price points should be better positioned to redirect customers toward less-exposed alternatives.

Volumes held up in 2025, oil shock clouds 2026 outlook[1]

(mlns of units : s.a.a.r.)

Light vehicle sales



	24	25	26	27
Canada	1.93	1.89	1.92	2.05
U.S.	16.0	16.3	16.3	16.8
Total	18.0	18.2	18.2	18.9

[1] **Sources**: BMO Economics, Haver Analytics • BMO Capital Markets, © Copyright 2026 BMO Capital Markets, Corp. | https://economics.bmo.com

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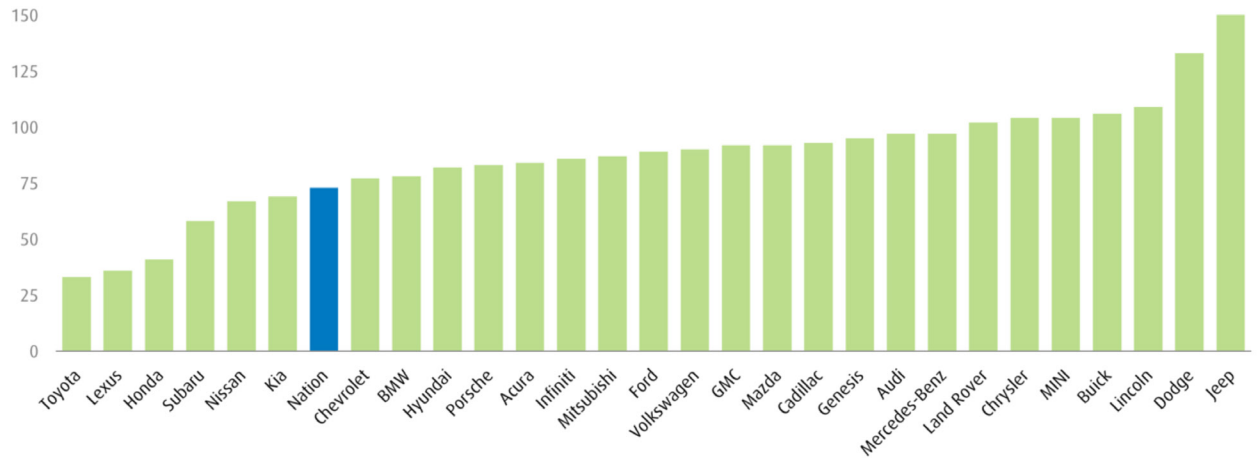
Vehicle supply supporting sales but significant differences across brands[2]

Days' supply of inventory*



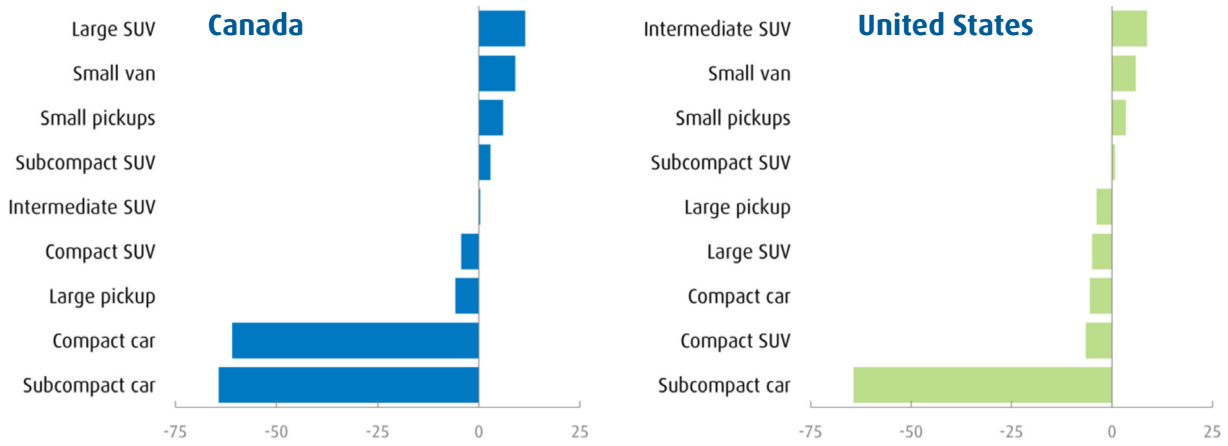
* Days' supply calculation includes vehicles in dealer inventory and in-transit/pipeline

[2] **Sources**: BMO Economics • Cox Automotive • BMO Capital Markets, © Copyright 2026 BMO Capital Markets, Corp. | https://economics.bmo.com

Affordability still shaping consumer choice[1]

(y-t-d % chng : as of 2026 Q2)

New vehicle sales by segment



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Alternative-Fuel Vehicle Sales

- Canada's alternative-fuel segments have rebounded in 2026 even as the broader market has softened. More than one-quarter of new registrations now use an alternative-fuel platform, led by continued growth in hybrids.
- Canadian hybrid-electric vehicle registrations are up approximately 22% year-to-date, while battery-electric registrations have risen roughly 26% following the return of federal purchase incentives. Total vehicle registrations are down about 2.5%.
- Growth is broad-based but uneven across provinces. Hybrid registrations are up almost 45% in Quebec, 19% in Ontario and 6.5% in British Columbia. Battery-electric registrations have increased 25%, 32% and 17% in those provinces, respectively.
- The U.S. market is moving in a different direction. Hybrid sales rose 23% year-over-year in July and approximately 21% year-to-date, while zero-emission vehicle sales fell 36.4% and 26.3%, respectively.
- Consumers remain interested in fuel savings, but increasingly favor options that involve fewer compromises on price, range and charging access. In Canada, hybrids have increased their market share by roughly 3 percentage points over the past year to 15.4%.

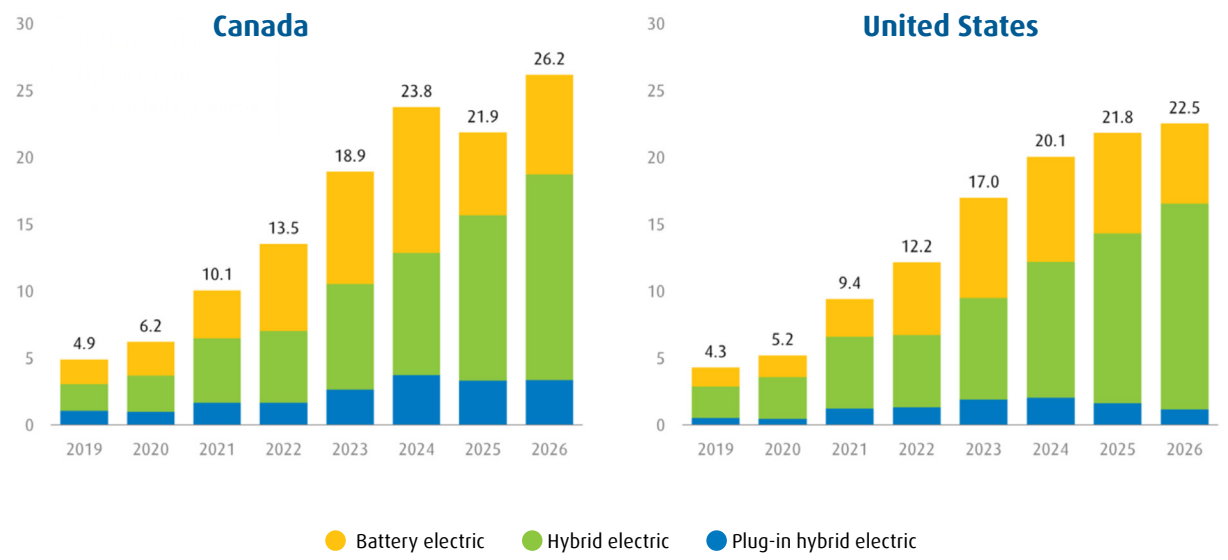
Dealer Finance takeaway

The alternative-fuel transition is broadening rather than moving uniformly toward fully electric vehicles. Hybrids offer the clearest near-term growth opportunity, while EV demand remains more sensitive to incentives, pricing and local conditions.

Tax incentive volatility reshapes consumer demand for EVs[3]

Alternative fuel new vehicle sales

(% of total light vehicle sales)



[3] **Sources**: BMO Economics • Statistics Canada • Argonne National Laboratory • U.S. Department of Energy • BMO Capital Markets, © Copyright 2026 BMO Capital Markets, Corp. | https://economics.bmo.com

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Closing Thought

The North American auto sector is navigating higher interest rates, renewed energy inflation and escalating trade uncertainty. Overall demand has remained resilient, but affordability increasingly determines which vehicles consumers buy, not simply whether they buy. The clearest themes are continued trading down, strong hybrid demand and the growing importance of product line diversification as tariff and incentive policies evolve.

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