Bank of Canada Rate Announcement

central 1 Economics

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As expected, there were few surprises in today's Bank of Canada rate decision. The Bank held the policy rate at 0.25 per cent and maintained quantitative easing (QE) at a pace of $2 billion per week and highlighted disappointing GDP data. It also re-iterated its commitment to keep the policy rate at the effective lower bound until economic slack is absorbed and the two per cent inflation target is sustainably achieved.

Diving into the surprise contraction in Q2 GDP of 1.1 per cent, it was noted that this was driven by a shock to exports from global supply chain disruptions and the anticipated easing of housing activity, while domestic demand growth remained on the upswing with a three per cent increase. Growth is anticipated to improve in the second half of the year, aligning with positive employment trends in recent months. That said, negative risks persist with the effects of the delta variant induced fourth wave and supply chain bottlenecks.

On the inflation front, the Bank of Canada continued to emphasize the transitory of nature of elevated CPI growth due to base- year effects, gasoline price and supply bottlenecks. However, it also noted that magnitude and persistence are uncertain. Wage pressures were deemed moderate, and core inflation has been less than headline CPI.

Central 1's outlook for growth is for 3.5 per cent GDP growth in Q3 and 6.6 per cent in Q4 which broadly aligns with the Bank's narrative. We expect the recovery to persist, with vaccine coverage and vaccine passports contributing to a continued re-opening of the economy. Labour Force Survey data for August is expected to show a gain of 100k jobs (Reuters consensus) which should moderate fears that growth is stagnating. That said, there remains the risk what the economy underperforms due to aforementioned risks which could push off QE tapering and rate hikes. Meanwhile, inflation pressures remain worth watching as supply chains disruptions continue to hit prices, and while still transitory, could lift inflation expectations which the Bank will need to manage.

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