Bank of Canada Rate Announcement

June 7 2023

Bank of Canada ends rate pause, hikes 25 basis points

It is decision day for the Bank of Canada. After a string of stronger than expected economic data releases and firm inflation readings, the Bank of Canada hiked 25 basis point hike to lift the target for the overnight rate to 4.75 per cent and it continued quantitative tightening. In doing so, this marked an end to its conditional pause. Market expectations were relatively split on whether the Bank would hike or hold, but clearly it did not have the patience to assess for another month.

The Bank's statement highlighted global factors in its decision, including more aggressive signals of further hikes around the world to stave off "stubbornly high" inflation, which is rising in some key markets. In the U.S., consumer activity remains strong despite a broadly slowing economy.

Domestically, the Bank referenced strength in the Canadian economy of 3.1 per cent in the first quarter. We note this was far stronger than expected (and above the bank's own forecast of 2.3 per cent) with firm consumption driving growth. Labour demand has been strong. The Bank noted that, "excess demand in the economy looks to be more persistent than anticipated".

On the inflation front, the Bank still anticipates headline CPI inflation to slip to about 3 per cent in the summer despite the uptick in April. That said, it highlighted that core inflation trends remain high in the 3.5-4 per cent range and given excess demand in the economy, it fears inflation could stay "stuck" above 2 per cent.

The latest move signals the Bank's discomfort with current inflation trend and economic resilience, despite the long lags of monetary policy likely to slow the real economy in coming quarters. Current rates, in the Bank's view, were insufficient in its view to balance supply and demand. The door is still open to further hikes or at least a prolonged period of higher rates which. The Bank stated that, "*Governing Council will continue to assess the dynamics of core inflation and the outlook for CPI inflation. In particular, we will be evaluating whether the evolution of excess demand, inflation expectations, wage growth and corporate pricing behaviour are consistent with achieving the inflation target*".

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