

ESSENTIALS OF MONETARY POLICY

Bank of Canada (BoC)

Colossal rate hike aims to lower actual and expected inflation

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ACCORDING TO THE BOC

- ▶ The Bank of Canada hiked the overnight rate by 100 bps today – the largest rate increase since 1998. This takes the Bank’s policy rate to 2.50%, which is a level we haven’t seen since 2008 and is squarely in the middle of the estimated range of the nominal neutral rate (2-3%). The Governor Council also “... continues to judge that interest rates will need to rise further ...”
- ▶ The BoC made no mistake in spelling out the justification for this. Inflation rapidly accelerated to 7.7% y/y in May and is “... likely remain around 8% in the next few months”. The same can be said for every measure of core inflation. And households have made clear that they expect inflation to hit record highs in the short term while raising their outlook for long-term price growth. This is bad news for the Bank as it risks its credibility.
- ▶ And it’s not just inflation that’s on the Bank’s mind. The labour market is too hot to handle in Canada, with the unemployment rate falling to the lowest level since the early 1970s in June (4.9%). At the same time, wage growth advanced at its fastest pace since the data started being published in the late 1990s (5.2% y/y).
- ▶ In contrast, economic growth is starting come down fast. Rapidly rising rates have already hit the housing market hard, and this has forced the Bank to meaningfully revise down its forecast for real GDP growth in 2022 and, in particular, 2023. It now expects growth to advance by 1.8% next year, down from 3.2% in the April 2022 Monetary Policy Report.

COMMENTS

It’s not easy being a central banker these days, and they’re certainly not winning any popularity contests. Inflation is red hot and household inflation expectations keep moving higher, risking further accelerating wage gains and a vicious wage-price spiral. The Bank’s Governing Council recognizes that it’s behind the curve and rates need to rise aggressively to force inflation back to target. With global factors like the war in Ukraine and supply chain disruptions still keeping prices elevated, the domestic economy is bearing the burden lowering inflation through a chilling of domestic demand. Interest-sensitive sectors like housing are bearing the brunt of the adjustment, and consumption may be next.

IMPLICATIONS

In spite of signs that the economy is slowing quickly, the Bank of Canada is being very clear in its intention to continue raising rates. So expect further tightening, as policy seems to be on a pre-set course. This will cause economic activity to come down even more rapidly than we anticipated in [our recent forecast](#), increasing the odds of a recession in 2023 (see our recent [Economic Viewpoint](#) on the odds of a recession in Canada).

Schedule 2022 of Central Bank Meetings

| Date | Central banks | Decision | Rate |
|-----------------|-----------------------------|-----------|-------|
| January | | | |
| 13 | Bank of Korea | +25 b.p. | 1.25 |
| 17 | Bank of Japan | s.q. | -0.10 |
| 20 | Bank of Norway | s.q. | 0.50 |
| 26 | Bank of Canada* | s.q. | 0.25 |
| 26 | Federal Reserve | s.q. | 0.25 |
| 31 | Reserve Bank of Australia | s.q. | 0.10 |
| February | | | |
| 2 | Bank of Brazil | +150 b.p. | 10.75 |
| 3 | European Central Bank | s.q. | 0.00 |
| 3 | Bank of England | +25 b.p. | 0.50 |
| 10 | Bank of Sweden | s.q. | 0.00 |
| 10 | Bank of Mexico | +50 b.p. | 6.00 |
| 22 | Reserve Bank of New Zealand | +25 b.p. | 1.00 |
| 23 | Bank of Korea | s.q. | 1.25 |
| 28 | Reserve Bank of Australia | s.q. | 0.10 |
| March | | | |
| 2 | Bank of Canada | +25 b.p. | 0.50 |
| 10 | European Central Bank | s.q. | 0.00 |
| 16 | Bank of Brazil | +100 b.p. | 11.75 |
| 16 | Federal Reserve | +25 b.p. | 0.50 |
| 17 | Bank of England | +25 b.p. | 0.75 |
| 17 | Bank of Japan | s.q. | -0.10 |
| 24 | Bank of Norway | +25 b.p. | 0.75 |
| 24 | Bank of Mexico | +50 b.p. | 6.50 |
| 24 | Swiss National Bank | s.q. | -0.75 |
| April | | | |
| 5 | Reserve Bank of Australia | s.q. | 0.10 |
| 12 | Reserve Bank of New Zealand | +50 b.p. | 1.50 |
| 13 | Bank of Korea | +25 b.p. | 1.50 |
| 13 | Bank of Canada* | +50 b.p. | 1.00 |
| 14 | European Central Bank | s.q. | 0.00 |
| 27 | Bank of Japan | s.q. | -0.10 |
| 28 | Bank of Sweden | +25 b.p. | 0.25 |
| May | | | |
| 3 | Reserve Bank of Australia | +25 b.p. | 0.35 |
| 4 | Bank of Brazil | +100 b.p. | 12.75 |
| 4 | Federal Reserve | +50 b.p. | 1.00 |
| 5 | Bank of England | +25 b.p. | 1.00 |
| 5 | Bank of Norway | s.q. | 0.75 |
| 12 | Bank of Mexico | +50 b.p. | 7.00 |
| 24 | Reserve Bank of New Zealand | +50 b.p. | 2.00 |
| 25 | Bank of Korea | +25 b.p. | 1.75 |
| June | | | |
| 1 | Bank of Canada | +50 b.p. | 1.50 |
| 7 | Reserve Bank of Australia | +50 b.p. | 0.85 |
| 9 | European Central Bank | s.q. | 0.00 |
| 15 | Bank of Brazil | +50 b.p. | 13.25 |
| 15 | Federal Reserve | +75 b.p. | 1.75 |
| 16 | Bank of England | +25 b.p. | 1.25 |
| 16 | Bank of Japan | s.q. | -0.10 |
| 16 | Swiss National Bank | +50 b.p. | -0.25 |
| 23 | Bank of Norway | +50 b.p. | 1.25 |
| 23 | Bank of Mexico | +75 b.p. | 7.75 |
| 30 | Bank of Sweden | +50 b.p. | 0.75 |

| Date | Central banks | Decision | Rate |
|------------------|-----------------------------|-----------|------|
| July | | | |
| 5 | Reserve Bank of Australia | +50 b.p. | 1.35 |
| 12 | Reserve Bank of New Zealand | +50 b.p. | 2.50 |
| 13 | Bank of Korea | +50 b.p. | 2.25 |
| 13 | Bank of Canada* | +100 b.p. | 2.50 |
| 20 | Bank of Japan | | |
| 21 | European Central Bank | | |
| 27 | Federal Reserve | | |
| August | | | |
| 2 | Reserve Bank of Australia | | |
| 3 | Bank of Brazil | | |
| 4 | Bank of England | | |
| 11 | Bank of Mexico | | |
| 16 | Reserve Bank of New Zealand | | |
| 18 | Bank of Norway | | |
| 24 | Bank of Korea | | |
| September | | | |
| 6 | Reserve Bank of Australia | | |
| 7 | Bank of Canada | | |
| 8 | European Central Bank | | |
| 15 | Bank of England | | |
| 20 | Bank of Sweden | | |
| 21 | Bank of Brazil | | |
| 21 | Bank of Japan | | |
| 21 | Federal Reserve | | |
| 22 | Bank of Norway | | |
| 22 | Swiss National Bank | | |
| 29 | Bank of Mexico | | |
| October | | | |
| 3 | Reserve Bank of Australia | | |
| 4 | Reserve Bank of New Zealand | | |
| 13 | Bank of Korea | | |
| 26 | Bank of Brazil | | |
| 26 | Bank of Canada* | | |
| 27 | European Central Bank | | |
| 27 | Bank of Japan | | |
| 31 | Reserve Bank of Australia | | |
| November | | | |
| 2 | Federal Reserve | | |
| 3 | Bank of England | | |
| 3 | Bank of Norway | | |
| 10 | Bank of Mexico | | |
| 22 | Reserve Bank of New Zealand | | |
| 23 | Bank of Korea | | |
| 24 | Bank of Sweden | | |
| December | | | |
| 5 | Reserve Bank of Australia | | |
| 7 | Bank of Brazil | | |
| 7 | Bank of Canada | | |
| 14 | Federal Reserve | | |
| 15 | European Central Bank | | |
| 15 | Bank of England | | |
| 15 | Bank of Norway | | |
| 15 | Bank of Mexico | | |
| 15 | Swiss National Bank | | |
| 19 | Bank of Japan | | |

NOTE: Certain banks may decide to change rates in-between the scheduled meetings. The abbreviations s.q. and b.p. correspond to status quo and basis points respectively. * Monetary Policy Report published.