

ESSENTIALS OF MONETARY POLICY

Bank of Canada (BoC)

It's 'Two and Through' as the Bank of Canada Pauses Interest Rate Hikes Again

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ACCORDING TO THE BOC

- ▶ As was widely expected, the Bank of Canada kept the overnight policy rate unchanged today at 5.00%, following 25 basis point increases in both June and July.
- ▶ There was plenty of evidence to back the move. Real GDP contracted by 0.2% annualized in the second quarter of the year, well below the Bank's 1.5% forecast in the July Monetary Policy Report (MPR). Our tracking suggests real GDP growth in Q3 is likely to come in similarly below the Bank's projection. While some of this reflected temporary factors like wildfires and strikes, a gradual easing of Canada's tight labour market and a downward move in home sales contributed to the "recent evidence that excess demand in the economy is easing ..."
- ▶ However, still broad-based inflationary pressures remain a concern. Even looking through higher food and energy prices in July, "... there has been little recent downward momentum in underlying inflation. The longer high inflation persists, the greater the risk that elevated inflation becomes entrenched, making it more difficult to restore price stability."
- ▶ Taken together, while the Bank decided to stay on hold today, "Governing Council remains concerned about the persistence of underlying inflationary pressures, and is prepared to increase the policy interest rate further if needed."

IMPLICATIONS

While today's rate decision didn't come as a surprise, the question now is: "What's next?" The Bank has said it's prepared to do more if needed, and the last two interest rate hikes have helped to reinforce the central bank's credibility. However, the policy rate is the highest it's been since early 2001 and well above the estimated 2-3% range of the neutral interest rate (where the Bank thinks the policy rate will settle in the long run).

At the same time, quantitative tightening is expected to continue apace, passively putting further upward pressure on interest rates.

Reading the tea leaves of the press release that accompanied the announcement, it seems that the Bank is confident it has done enough to gradually bring the Canadian economy back to balance. And we agree. Now it's just a waiting game as the Bank of Canada surveys the impact of past hikes on economic activity. Once the Bank's satisfied the economy has slowed enough to support a gradual return of inflation to its 2% target, we expect it to begin cutting interest rates. This may happen as early as the first quarter of 2024.

2023 Schedule of Central Bank Meetings

	Central bank	Decision	Rate
January			
12	Bank of Korea	+25 b.p.	3.50
17	Bank of Japan	unchanged	-0.10
19	Bank of Norway	unchanged	2.75
25	Bank of Canada*	+25 b.p.	4.50
February			
1	Bank of Brazil	unchanged	13.75
1	Federal Reserve	+25 b.p.	4.75
2	European Central Bank	+50 b.p.	3.00
2	Bank of England	+50 b.p.	4.00
6	Reserve Bank of Australia	+25 b.p.	3.35
9	Bank of Sweden	+50 b.p.	3.00
9	Bank of Mexico	+50 b.p.	11.00
21	Reserve Bank of New Zealand	+50 b.p.	4.75
22	Bank of Korea	unchanged	3.50
March			
6	Reserve Bank of Australia	+25 b.p.	3.60
8	Bank of Canada	unchanged	4.50
9	Bank of Japan	unchanged	-0.10
16	European Central Bank	+50 b.p.	3.50
22	Bank of Brazil	unchanged	13.75
22	Federal Reserve	+25 b.p.	5.00
23	Bank of England	+25 b.p.	4.25
23	Bank of Norway	+25 b.p.	3.00
23	Swiss National Bank	+50 b.p.	1.50
30	Bank of Mexico	+25 b.p.	11.25
April			
4	Reserve Bank of Australia	unchanged	3.60
4	Reserve Bank of New Zealand	+50 b.p.	5.25
10	Bank of Korea	unchanged	3.50
12	Bank of Canada*	unchanged	4.50
26	Bank of Sweden	+50 b.p.	3.50
28	Bank of Japan	unchanged	-0.10
May			
2	Reserve Bank of Australia	+25 b.p.	3.85
3	Bank of Brazil	unchanged	13.75
3	Federal Reserve	+25 b.p.	5.25
4	European Central Bank	+25 b.p.	3.75
4	Bank of Norway	+25 b.p.	3.25
11	Bank of England	+25 b.p.	4.50
18	Bank of Mexico	unchanged	11.25
23	Reserve Bank of New Zealand	+25 b.p.	5.50
24	Bank of Korea	unchanged	3.50
June			
6	Reserve Bank of Australia	+25 b.p.	4.10
7	Bank of Canada	+25 b.p.	4.75
14	Federal Reserve	unchanged	5.25
15	European Central Bank	+25 b.p.	4.00
15	Bank of Japan	unchanged	-0.10
21	Bank of Brazil	unchanged	13.75
22	Bank of England	+50 b.p.	5.00
22	Bank of Norway	+50 b.p.	3.75
22	Bank of Mexico	unchanged	11.25
22	Swiss National Bank	+25 b.p.	1.75
29	Bank of Sweden	+25 b.p.	3.75

	Central bank	Decision	Rate
July			
4	Reserve Bank of Australia	unchanged	4.10
11	Reserve Bank of New Zealand	unchanged	5.50
12	Bank of Korea	unchanged	3.50
12	Bank of Canada*	+25 b.p.	5.00
26	Federal Reserve	+25 b.p.	5.50
27	European Central Bank	+25 b.p.	4.25
27	Bank of Japan	unchanged	-0.10
August			
1	Reserve Bank of Australia	unchanged	4.10
2	Bank of Brazil	-50 b.p.	13.25
3	Bank of England	+25 b.p.	5.25
10	Bank of Mexico	unchanged	11.25
15	Reserve Bank of New Zealand	unchanged	5.50
17	Bank of Norway	+25 b.p.	4.00
23	Bank of Korea	unchanged	3.50
September			
5	Reserve Bank of Australia	unchanged	4.10
6	Bank of Canada	unchanged	5.00
14	European Central Bank		
20	Bank of Brazil		
20	Federal Reserve		
21	Bank of England		
21	Bank of Norway		
21	Bank of Sweden		
21	Bank of Japan		
21	Swiss National Bank		
28	Bank of Mexico		
October			
2	Reserve Bank of Australia		
3	Reserve Bank of New Zealand		
18	Bank of Korea		
25	Bank of Canada*		
26	European Central Bank		
30	Bank of Japan		
November			
1	Bank of Brazil		
1	Federal Reserve		
2	Bank of England		
2	Bank of Norway		
6	Reserve Bank of Australia		
9	Bank of Mexico		
23	Bank of Sweden		
28	Reserve Bank of New Zealand		
29	Bank of Korea		
December			
4	Reserve Bank of Australia		
6	Bank of Canada		
13	Bank of Brazil		
13	Federal Reserve		
14	European Central Bank		
14	Bank of England		
14	Bank of Norway		
14	Bank of Mexico		
14	Swiss National Bank		
18	Bank of Japan		

NOTE: Central banks may decide to change rates between the scheduled meetings. The abbreviation b.p. stands for basis points. * Monetary Policy Report published; ** To be determined.