BoC hits (hopeful) pause on rate hikes

- The Bank of Canada decided to pause the hiking cycle and left the overnight rate unchanged at 5% in today’s announcement, in line with our and markets’ pre-meeting expectations.

- The BoC (also as expected) kept the option open to hike further if necessary down the road. Inflation has slowed substantially but the central bank's own preferred 'core' measures are still running persistently above the 2% target. Wage growth is still high and near-term CPI growth rates are likely to rise in the near-term with oil prices higher in recent weeks.

- But interest rates are already at levels that the central bank views as 'restrictive' enough to put downward pressure on economic growth and inflation pressures over time. And today's decision followed a slew of softer economic data releases that suggest the lagged growth headwinds from the 475 bp cumulative rate hikes since March 2022 are building.

- The unemployment rate in Canada rose by half a percentage point from April to July. And GDP edged lower in Q2 alongside a soft early estimate for July that's tracking potentially a second consecutive quarterly decline in Q3. That GDP data is substantially softer than the 1.5% (annualized) increase in each of Q2 and Q3 that the BoC assumed in July.

- **Bottom line:** The BoC remains highly data-dependent and won't hesitate to push interest rates higher if necessary to return inflation to the 2% target rate. And there are two additional labour market reports and two additional inflation reports before the next scheduled decision in October. But we continue to expect that the recent soft-patch in economic data will continue, and look for the overnight rate to hold where it is through the end of this year.