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Bank of Canada remains proactive with 25 bp rate hike

- Following a two meeting pause, the BoC resumed tightening with a 25 bp hike lifting the overnight rate to 4.75%
- Today's increase is hardly shocking given recent data flow but was only expected by a handful of analysts
- No clear tightening bias but a follow up hike in July is likely

There were plenty of reasons for the BoC to restart its tightening cycle today. GDP growth was stronger than expected in Q1 led by robust consumer spending, inflation surprised to the upside in April, unemployment has been steady near a record low for five straight months, and Canada's housing correction appears to have run its course. We thought the BoC might wait until July to accumulate a few more data points and refresh its forecasts, but consistent with a proactive approach throughout this tightening cycle, Governing Council surprised the consensus (and us) with a 25 bp rate hike. While Governor Macklem sounded like he was in no rush to raise rates at his FSR press conference in mid-May—focusing on broader CPI trends rather than the April miss and downplaying the rebound in housing—today's policy statement reads like there was little doubt that a hike was appropriate. The BoC's key message is that "excess demand in the economy looks to be more persistent than anticipated" and there is growing risk that inflation "could get stuck materially above the 2% target."

With Macklem's "accumulation of evidence" criteria having been met, Governing Council determined monetary policy was not sufficiently restrictive to return inflation sustainably to target. The concluding statement doesn't include a clear tightening bias but our expectation has been that if the BoC was coming off the sidelines, they would intend to hike more than once—if 4.50% wasn't restrictive enough it's hard to think 4.75% is. Governing Council laid out its now-familiar criteria for future policy decisions: the evolution of excess demand, inflation expectations, wage growth and corporate pricing behaviour. It's an unusually short five weeks until the July rate decision, but that period is packed with key releases including two employment reports, another CPI reading, an updated April GDP estimate and May flash, and the Q2 Business Outlook Survey. The onus is clearly on that data to soften broadly to preclude another rate hike, and timing a slowdown has been challenging. We'll publish updated forecasts in our *Macro & Provincial Outlook* and *Financial Markets Monthly* tomorrow.

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