Bank of Canada to look through inflation threat

The BoC left its overnight policy rate unchanged at 2.25%. While acknowledging the prospect of higher energy costs pushing up inflation, it recognises there is excess supply in the economy with unemployment rising. This will help limit the pass-through to prices more broadly at a time when trade tensions continue to pose challenges for Canadian growth

Bank of Canada Governor Tiff Macklem

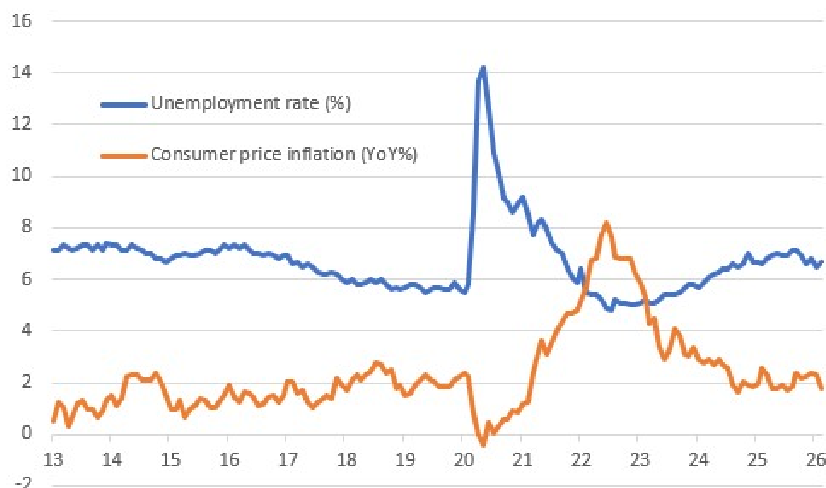
Job worries mount as price pressures increase

The Bank of Canada left its policy overnight interest rate unchanged at 2.25%, as widely predicted, citing the volatility in energy and financial markets and the "heightened risks to the global economy".

Regarding growth, they acknowledge that the economy was weaker than anticipated in the fourth quarter of 2025, but that underlying consumer and government spending remained relatively firm. While it is "too early to assess" the economic implications from the conflict in the Middle East, the jobs market is a concern, with unemployment rising to 6.7% in February from January's 6.5% rate, and the economy losing 109k jobs in the first two months of 2026. At the same time they continue to highlight the headwinds that trade tensions and US tariffs on Canadian made products present.

Headline inflation was lower than predicted in February at 1.8%, but this is being temporarily depressed to base effects tied to sales tax changes last year while higher energy costs point to upward pressure on prices.

Canadian inflation & unemployment



Source: Macrobond, ING

BoC sees limited scope for broadening price pressures

The BoC concludes that “risks to growth look tilted to the downside”, while inflation risks “have gone up”. Canada is not alone in this situation, with Governor Tiff Macklem acknowledging this presents a “dilemma for central banks” since hiking rates to slow inflation will hurt growth, while lowering rates could stoke inflation to levels well above target. For now, it appears that the BoC will “look through” the threat of near-term inflation, with Macklem suggesting that the BoC’s base case is that with excess supply in the economy, the prospect of higher inflation feeding through into other prices “looks contained”. Still, the BoC will be watchful for potential second-round effects, such as higher wage demands and stands ready to act should they appear.

Given uncertainty over how long the situation will last and the continued focus on trade – remember the USMCA trade deal between the US, Mexico and Canada is up for joint review in July – we see little prospect of a near-term rate move from the BoC. With the jobs market clearly cooling again and the economy looking set to grow by little more than 1% this year, we don’t see the demand impetus that would lead to broader, more persistent inflation. As such, we continue to expect the BoC to leave the overnight rate unchanged throughout 2026.

Author

James Knightley
Chief International Economist, US
james.knightley@ing.com

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