

POLICY COMMENTARY · JUNE BOC

June 10, 2026

Bank of Canada holds at 2.25%, maintains previous guidance

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THE TAKE

“The Bank of Canada is getting closer ending its hold, and will likely not wait longer than September to pick a direction. Officials were clear that the most important indicators to watch are core inflation, the share of the CPI basket running above 3%, and medium-to-long term inflation expectations.”

— JAY ZHAO-MURRAY · CHIEF ECONOMIST · SIBLEY CREEK

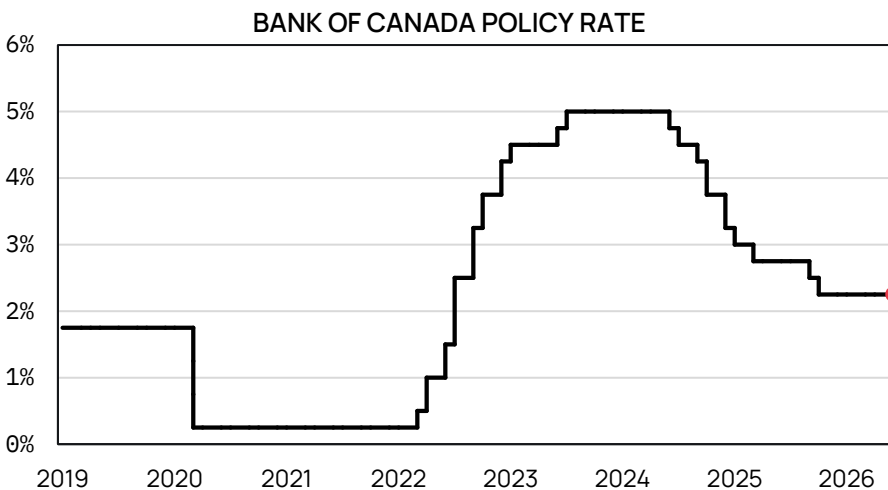
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Bank of Canada holds for fifth straight meeting.

The Bank of Canada maintained its policy rate at 2.25%, meeting expectations. Guidance was little changed from April—Governor Macklem repeated that in the case of significant new trade restrictions the bank “may need to cut the policy rate,” but if the war in the Middle East and high oil prices led to “ongoing generalized inflation,” the bank might deliver “consecutive increases.”

In our view, the bank is getting closer to ending its pause, and is waiting for the data to tell it which way to go. The tell is that today’s hold was framed purely as a balance of risks—language about current policy being “appropriate” and the base case guidance that “changes in the policy rate can be expected to be small” were both dropped. We expect that officials will have enough information to make a decision about which of their two main scenarios is playing out by the September meeting.

Bank of Canada maintains policy rate at 2.25%.



Source: Bank of Canada.

Back in April, the bank held rates out of patience—looking to buy time and wait out the oil price shock. Today, it held rates out of a tension between two opposing forces: Macklem explicitly referenced the policy “dilemma” of how to deal with weak growth and rising inflation, a classic stagflationary dynamic. Officials are worried that raising rates would unnecessarily hamstring what’s already a weak economy, but lowering them risks making inflation persistent.

Macklem was explicit about the main signals to watch to judge the pass-through from high oil prices to inflation. Specifically, it’s core inflation, the proportion of CPI components rising faster than 3%, and medium and long-term inflation expectations. If those indicators are rising, it would

be a blaring alarm that it's time to hike rates. If they do start going up in the coming weeks and months, the game will be judging how much is enough to trigger a rate hike.

On the growth side, Macklem said he was expecting a rebound in the second quarter, noting that high-frequency indicators including StatCan's flash GDP estimate as well as consumption and housing data looked positive.

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