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Bank of Canada's Macklem talks down interest rate cuts, but says 2% inflation 'now in sight'

It's still too early to consider undoing the most aggressive series of rate hikes in decades, central bank governor says

Denise Paglinawan || December 15, 2023

Bank of Canada governor Tiff Macklem says it's still too soon to talk about cutting interest rates. PHOTO BY DAVE CHAN/AFP VIA GETTY IMAGES

Cutting the Bank of Canada’s policy interest rate doesn’t seem to be top of mind for governor Tiff Macklem, who said Dec. 15 that it’s still too early to consider undoing the most aggressive series of rate hikes in decades. Macklem made the remarks while delivering his end-of-year speech before the Canadian Club Toronto on Friday, two days after United States Federal

Reserve chair Jerome Powell poured fuel on a stock market rally by suggesting that rates were at or close to their peak. The Financial Post's Denise Paglinawan breaks down what you need to know about Macklem's speech.

It's too early to consider cuts

Despite widespread predictions that the Bank of Canada will start cutting interest rates next year, Macklem said that until the central bank sees evidence that Canada is clearly on a path back to two per cent inflation, cuts are off the table. Macklem said the central bank doesn't need to wait until inflation is all the way back to that target to consider easing policy, but it does need to be clearly headed to two per cent. "When it's clear that inflation is on a sustained downward track, we can begin discussing lowering our policy interest rate," he said. "We have not started having that discussion, because it's too early to have that discussion. We're still discussing whether we've raised interest rates enough and how long they need to stay where they are."

Economic growth is expected to remain weak into 2024

Macklem said the excess demand that drove prices higher over the past two years is now gone. Higher interest rates and tighter global financial conditions have helped rebalance the economy, he said. With growth subdued and the cost of living still increasing too quickly, Macklem forecast the next two to three quarters will be difficult for many. He said consumers will continue to hold back spending, businesses will see weak demand and employment will probably grow more slowly in the labour force. That means the unemployment rate will likely increase further.

Expect some push and pull on inflation

Over the coming months, Canadians should expect to see some push and pull on inflation. While the cooling economy will reduce price pressures, Macklem said other forces will continue to exert upward pressure on prices. As a result, further decreases in inflation will likely be gradual. He noted that new surprises can't be ruled out, either. For one, an escalation of war in Europe or the Middle East may divert trade, investment and disrupt supply chains. Climate events have become more frequent and more extreme, both at home and abroad. These risks often affect prices, and the bank needs to be vigilant and ready to adjust as needed.

Two per cent inflation isn't here yet, but the target is 'in sight'

Macklem said that looking back at 2023 reminds us of how far we've come. "The two per cent inflation target is now in sight. And while we're not there yet, the conditions increasingly appear to be in place to get us there," he said. Macklem said we still need to see more downward momentum in core inflation and that the bank will be watching the supply-demand balance, wage growth, corporate pricing behaviour and inflation expectations closely as it assesses where Canada is on the path to price stability. Macklem said he expects inflation will be getting close to the two per cent target by the end of next year.