

## **BANK OF CANADA**

### Monetary authorities stay the course despite the economic difficulties

#### ACCORDING TO THE BANK OF CANADA (BoC)

- The target for the overnight rate stays at 0.50%.
- Global growth in the first half of 2016 was slower than the Bank had projected in its July *Monetary Policy Report*, although the Bank continues to expect it to strengthen gradually in the second half of this year. The US economy was weaker than expected in the second quarter, notably reflecting a contraction in business and residential investment.
- While Canada's economy shrank in the second quarter, the Bank still projects a substantial rebound in the second half of this year. The economy is expected to rebound in the third quarter as oil production recovers, rebuilding commences in Alberta, and consumer spending gets an additional lift from Canada Child Benefit payments. As federal infrastructure spending starts to have more impact, growth in the fourth quarter is projected to remain above potential.
- While the strength in exports during July was encouraging, the ground lost over previous months raises the possibility that the profile for economic activity [in Canada] will be somewhat lower than anticipated in July.
- Inflation is roughly in line with the Bank's expectations.
- On balance, risks to the profile for inflation have tilted somewhat to the downside since July. At the same time, while there are preliminary signs of a possible moderation in the Vancouver housing market, financial vulnerabilities associated with household imbalances remain elevated and continue to rise.

#### COMMENTS

As expected, Canada's economy experienced significant difficulties in the second quarter, with real GDP declining 1.6% (quarterly annualized). Not only was oil production hampered by temporary problems caused by the forest fires in Alberta, but non-energy exports also lost ground during the quarter.

Despite these setbacks, the monetary authorities did not succumb to the temptation of lowering key interest rates again. This is without a doubt the right decision, as another interest rate cut would have kick-started credit at a time when

high household debt is already a concern. In any case, as shown by weak exports last spring, the root of the problems in Canada's economy is located abroad. In fact, domestic demand advanced 2.2% in the second quarter. Additional monetary stimulus measures are therefore not needed given these circumstances. Yet, as rightfully pointed out by the BoC, all signs point to a rebound in Canada's economy as of the third quarter. July's sharp increase in merchandise exports is quite telling in this regard.

**Implications:** At first glance, today's decision does not in any way change our forecasts on future changes in the federal funds target rate. Finding some balance between upside and downside risks will help extend the status quo on key interest rates until the spring of 2018.

That said, we cannot completely rule out the possibility that the rebound expected in Canada's economy in the second half of 2016 might disappoint in the end. This is no doubt what motivated the monetary authorities to show more caution, by mentioning that inflation risks have somewhat tilted downwards. The BoC is clearly not shutting the door to an additional interest rate cut. This should keep the financial markets guessing—and limit the loonie's flight.

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## Schedule 2016 of Central Bank meetings

	<u>Decision</u>	<u>Rate</u>		<u>Decision</u>	<u>Rate</u>		
<b>JANUARY</b>			<b>JULY</b>				
13	Bank of Korea	s.q.	1.50	5	Reserve Bank of Australia	s.q.	1.75
14	Bank of England	s.q.	0.50	6	Bank of Sweden	s.q.	-0.50
20	Bank of Brazil	s.q.	14.25	13	Bank of Korea	s.q.	1.25
20	Bank of Canada	s.q.	0.50	13	Bank of Canada	s.q.	0.50
21	European Central Bank	s.q.	0.05	14	Bank of England	s.q.	0.50
27	Federal Reserve	s.q.	0.50	20	Bank of Brazil	s.q.	14.25
28	Reserve Bank of New Zealand	s.q.	2.50	21	European Central Bank	s.q.	0.00
29	Bank of Japan	s.q.	-0.10	27	Federal Reserve	s.q.	0.50
<b>FEBRUARY</b>			<b>AUGUST</b>				
1	Reserve Bank of Australia	s.q.	2.00	2	Reserve Bank of Australia	-25 b.p.	1.50
4	Bank of England	s.q.	0.50	4	Bank of England	-25 b.p.	0.25
4	Bank of Mexico	s.q.	3.25	10	Bank of Korea	s.q.	1.25
11	Bank of Sweden	-15 b.p.	-0.50	10	Reserve Bank of New Zealand	-25 b.p.	2.00
15	Bank of Korea	s.q.	1.50	11	Bank of Mexico	s.q.	4.25
17	Bank of Mexico	+50 b.p.	3.75	31	Bank of Brazil	s.q.	14.25
29	Reserve Bank of Australia	s.q.	2.00	<b>SEPTEMBER</b>			
<b>MARCH</b>			<b>OCTOBER</b>				
2	Bank of Brazil	s.q.	14.25	6	Reserve Bank of Australia	s.q.	1.50
9	Bank of Korea	s.q.	1.50	7	Bank of Canada	s.q.	0.50
9	Reserve Bank of New Zealand	-25 b.p.	2.25	7	Bank of Sweden	s.q.	-0.50
9	Bank of Canada	s.q.	0.50	8	European Central Bank		
10	European Central Bank	-5 b.p.	0.00	8	Bank of Korea		
14	Bank of Japan	s.q.	-0.10	15	Bank of England		
16	Federal Reserve	s.q.	0.50	15	Swiss National Bank		
17	Bank of England	s.q.	0.50	20	Bank of Japan		
17	Bank of Norway	-25 b.p.	0.50	21	Reserve Bank of New Zealand		
17	Swiss National Bank	s.q.	-0.75	21	Federal Reserve		
18	Bank of Mexico	s.q.	3.75	22	Bank of Norway		
<b>APRIL</b>			<b>NOVEMBER</b>				
5	Reserve Bank of Australia	s.q.	2.00	3	Reserve Bank of Australia		
13	Bank of Canada	s.q.	0.50	12	Bank of Korea		
14	Bank of England	s.q.	0.50	13	Bank of England		
18	Bank of Korea	s.q.	1.50	19	Bank of Brazil		
21	European Central Bank	s.q.	0.00	19	Bank of Canada		
21	Bank of Sweden	s.q.	-0.50	20	European Central Bank		
27	Reserve Bank of New Zealand	s.q.	2.25	27	Bank of Norway		
27	Bank of Brazil	s.q.	14.25	27	Bank of Sweden		
27	Bank of Japan	s.q.	-0.10	31	Reserve Bank of Australia		
27	Federal Reserve	s.q.	0.50	31	Bank of Japan		
<b>MAY</b>			<b>DECEMBER</b>				
3	Reserve Bank of Australia	-25 b.p.	1.75	5	Reserve Bank of Australia		
5	Bank of Mexico	s.q.	3.75	7	Bank of Canada		
12	Bank of England	s.q.	0.50	8	European Central Bank		
12	Bank of Korea	s.q.	1.50	14	Bank of Korea		
12	Bank of Norway	s.q.	0.50	14	Federal Reserve		
25	Bank of Canada	s.q.	0.50	15	Bank of England		
<b>JUNE</b>			<b>NOVEMBER</b>				
2	European Central Bank	s.q.	0.00	2	Federal Reserve		
7	Reserve Bank of Australia	s.q.	1.75	3	Bank of England		
8	Bank of Korea	-25 b.p.	1.25	9	Reserve Bank of New Zealand		
8	Reserve Bank of New Zealand	s.q.	2.25	10	Bank of Korea		
8	Bank of Brazil	s.q.	14.25	17	Bank of Mexico		
15	Bank of Japan	s.q.	-0.10	30	Bank of Brazil		
15	Federal Reserve	s.q.	0.50	<b>DECEMBER</b>			
16	Bank of England	s.q.	0.50	5	Reserve Bank of Australia		
16	Swiss National Bank	s.q.	-0.75	7	Bank of Canada		
23	Bank of Norway	s.q.	0.50	8	European Central Bank		
30	Bank of Mexico	+50 b.p.	4.25	14	Bank of Korea		
				14	Federal Reserve		
				15	Bank of England		
				15	Bank of Norway		
				15	Bank of Mexico		
				15	Swiss National Bank		
				19	Bank of Japan		
				21	Bank of Sweden		

NOTE: Certain banks may decide to change rates in-between the scheduled meetings. The abbreviations s.q. and b.p. correspond to status quo and basis points respectively. \* To be determined.