C.D. Howe Institute Monetary Policy Council Calls for Bank of Canada to Hold Overnight Rate at 4.50 Percent through September, Cut to 4.25 Percent by March of 2024

March 02, 2023 – The C.D. Howe Institute's **Monetary Policy Council** (MPC) recommends that the Bank of Canada hold its target for the overnight rate, its benchmark policy interest rate, at 4.50 percent on March 8th, and keep it at that level for the next six months. By March of 2024, the Council recommends a cut to 4.25 percent.

The MPC provides an independent assessment of the monetary stance consistent with the Bank of Canada's 2 percent inflation target. **William Robson**, the Institute's CEO, chairs the Council.

Council members make recommendations for the Bank of Canada's upcoming interest-rate announcement, the subsequent announcement, and the announcements six months and one year ahead. The Council's formal recommendation for each announcement is the median vote of members attending the meeting.

The Council also offers a view on whether the Bank should accelerate, maintain or slow the planned reduction in its holdings of Government of Canada bonds. On this occasion, the majority voted for the Bank to maintain its planned pace of reduction.

Although the median vote of Council members was for no change in the overnight rate target at the upcoming announcement and the April announcement, three of the 11 members attending the meeting wanted a hike to 4.75 next week, and two of those members wanted a further hike to 5.00 percent in April. By September, the balance of opinion had shifted the other way – while two members favoured 5.00 at that setting, four favoured a cut to 4.25. By March of 2024, the balance had shifted more decisively down: two members continued to favour 5:00, while the votes of the other nine ranged from a high of 4.50 to a low of 3.75 (see table below).

The Bank of Canada's current policy with respect to its holdings of Government of Canada bonds is to buy nothing and let its holdings shrink as the bonds mature. Three Council members called for the Bank of Canada to accelerate the reduction, two of them noting that nothing will mature between now and April 12th, and one emphasizing that the Bank of Canada should sell its holdings of real-return bonds. The other eight members indicated that they were comfortable with the Bank's intended schedule.

The group's discussion at this meeting emphasized more than usual challenges in interpreting recent data on economic activity and inflation. With respect to activity, several members noted that unusual seasonal

factors in late 2022 and early 2023 might have distorted some numbers, notably on labour-force and employment, in both Canada and the United States. A number of members noted that lingering impacts of the pandemic, and increases in temporary and permanent immigration in Canada, complicated judgements about how quickly productive capacity is expanding. Some members expressed concern that weak business investment and poor productivity growth might be causing Canadian productive capacity to stall, which would require the Bank to adopt a more restrictive stance than would otherwise be needed to bring inflation back to target. Notwithstanding these uncertainties, the majority of the group seemed satisfied that spending has slowed to a pace that prefigures further declines in inflation.

With respect to the group's confidence that inflation will return to target over the timeframe projected by the Bank of Canada – that is, by the end of 2024 – much of the discussion centered on the reliability of various CPI measures. Some members advocated paying more attention to measures that strip out, or give less weight to, products that are more prone to supply disruptions, and mortgage interest costs, which tend to rise when interest rates rise. Others advocated paying more attention to broader measures, not least because the inflation target is for the total CPI. Another point of interest was the behaviour of inflation measures over intervals shorter than the typically referenced 12-month rate of change. Some members noted that higher-frequency measures suggest that inflation is already within the 1-to-3 percent target range; others argued that a decisive victory over inflation requires the 12-month figure to be back to target. Differing judgements on these questions help explain why some members continued to look for an overnight rate as high or higher than it is now through the end of the year, while the majority expected that falling inflation would lead the Bank to cut the overnight rate target by March of 2024.

Votes of MPC Members and the Council Median for Each Announcement (*percent*)					
MPC Members	**8 March, 2023**	**12 April, 2023**	**6 Sept, 2023**	**24 March, 2024**	**Reduction in Bond Holdings**
Steve Ambler Université du Québec à Montréal (UQAM)	4.50	4.50	4.25	3.75	Accelerate
Beata Caranci TD Bank Group	4.50	4.50	4.25	3.75	Maintain
Edward A. Carmichael Ted Carmichael Global Macro	4.75	5.00	5.00	5.00	Maintain
Michael Devereux University of British Columbia	4.75	4.75	4.50	4.50	Maintain
Stéfane Marion National Bank of Canada	4.50	4.50	4.25	4.00	Maintain
Angelo Melino University of Toronto	4.50	4.50	4.50	4.25	Accelerate
Jean-François Perrault Scotiabank	4.50	4.50	4.50	4.00	Maintain
Douglas Porter BMO Capital Markets	4.50	4.50	4.50	4.25	Accelerate
Avery Shenfeld CIBC	4.50	4.50	4.50	4.25	Maintain
Pierre Siklos Wilfrid Laurier University	4.75	5.00	5.00	5.00	Maintain
Stephen D. Williamson Western University	4.50	4.50	4.25	4.00	Maintain
Median Vote	4.50	4.50	4.50	4.25	N/A

The views and opinions expressed by the participants are their own and do not necessarily reflect the views of the organizations with which they are affiliated, or those of the C.D. Howe Institute.

The MPC's next vote will take place on April 6, 2023, prior to the Bank of Canada's overnight rate announcement on April 12.

* * * * *

Contact: Mawakina Bafale; e-mail: mbafale@cdhowe.org.