Monetary Policy Council

Communiqué

August 31, 2023

C.D. Howe Institute Monetary Policy Council to Bank of Canada: Hold Overnight Rate at 5.00 Percent until Early 2024, Cut to 4.25 Percent by Next September

August 31, 2023 – The C.D. Howe Institute's **Monetary Policy Council** (MPC) recommends that the Bank of Canada maintain its target for the overnight rate, its benchmark policy interest rate, at 5.00 percent on September 6th. The MPC further recommends that the Bank keep the target at 5.00 percent at least until March of 2024, then reduce it to 4.25 percent by September of 2024.

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.

Sentiment in favour of maintaining the target in the near term was strong: six of the eight members attending the meeting called for a target of 5.00 percent on September 6th, while one called for a target of 5.25 percent and one for a target of 4.75 percent. The votes for the following setting on October 25th were the same. By March of 2024, sentiment had shifted somewhat: four members called for a target of 5:00 percent, one called for 4.75 percent and one for 5.25 percent, and two members called for a target of 4.25 percent. In a year's time, one member called for a target of 5.25 percent, while the other seven recommendations ranged from 3.75 to 4.50 percent, yielding a median recommendation of 4.25 percent (see table below).

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. 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. Six of the eight members attending the meeting called for the Bank to maintain that schedule, while two called for it to accelerate the reduction in its holdings.

The group's recommendation for no change in the overnight rate at the upcoming setting and over the next half-year was the product of several considerations. Looking abroad, members noted the surprising recent strength of spending in the United States – a support for Canadian exports – and weakness overseas, particularly in China – a negative for exports and commodity prices. In assessing the situation in Canada, many members emphasized that spending and activity are moderating, but commented that recent disappointing inflation readings and continued pressure on capacity put further timely progress toward the 2 percent target in doubt.

The impact of monetary restraint to date on Canadian households was a major focus of discussion. Higher mortgage rates appear to be gradually restraining spending by homeowners – which is promising for continued reductions in inflation – but strong demand and constrained supply for rental housing is putting upward pressure on rents. With generous pandemic-related income supports having raised household saving, some members argued that consumers still had plenty of capacity to spend even as income growth moderates.

Immigration and fiscal policy were also major themes in the MPC's deliberations. Although recent strong growth in temporary and permanent residents should increase Canada's productive capacity over time, many members judged that rapid population growth is currently adding to inflationary pressure, since demand for housing and consumer goods and services precedes labour-force participation, and business investment and productivity are weak. With respect to fiscal policy, many members noted that governments should be practicing more restraint at this point in the cycle, and worried that political pressures might lead to more spending, which would add to inflationary pressure.

These considerations help explain why the prospect of moderating growth in demand did not lead MPC members to recommend earlier, larger reductions in the overnight rate. Several commented that the Bank of Canada needed to be resolute in ensuring that inflation would continue to decline before lowering its policy rate.

Votes of MPC Members and the Council Median for Each Announcement (*percent*)

MPC Members	6 September, 2023	25 October, 2023	6 March, 2024	September 2024	Reduction in Bond Holdings
Steve Ambler Université du Québec à Montréal (UQAM)	5.00	5.00	4.25	4.00	Maintain
Stéfane Marion National Bank of Canada	5.00	5.00	5.00	4.25	Maintain
Angelo Melino University of Toronto	5.25	5.25	4.75	4.25	Accelerate
Jean-François Perrault Scotiabank	5.00	5.00	5.00	4.25	Maintain
Avery Shenfeld CIBC	5.00	5.00	5.00	4.00	Maintain
Pierre Siklos Research Fellow	5.00	5.00	5.25	5.25	Accelerate
Stephen D. Williamson Western University	4.75	4.75	4.25	3.75	Maintain
Craig Wright RBC	5.00	5.00	5.00	4.50	Maintain
Median Vote	5.00	5.00	5.00	4.25	Maintain

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 October 19, 2023, prior to the Bank of Canada's overnight rate announcement on October 25.

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