Monetary Policy Council

Communiqué

March 4, 2021

Bank of Canada Should Hold Overnight Rate at 0.25 Percent, Prepare to Reduce Government Bond Purchases: C.D. Howe Institute Monetary Policy Council

March 4, 2021 – The C.D. Howe Institute's **Monetary Policy Council** (MPC) recommends that the Bank of Canada keep its target for the overnight rate, its benchmark policy interest rate, at 0.25 percent at least until March of 2022. The MPC was divided on whether the Bank of Canada should maintain its current pace of Government of Canada bond purchases between now and its next policy-rate announcement on April 21st, but members who voted for the Bank to maintain its current pace said it should prepare markets for a winding down of the program.

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. The Council's principal recommendations are about the overnight rate target. 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. At recent MPC meetings, members have also voted on the Bank's quantitative easing program – in this instance, its commitment to buy at least $4 billion of Government of Canada bonds per week between now and its next overnight rate announcement in April.

All 12 members of the MPC called for the Bank to keep the overnight rate at 0.25 at its upcoming setting on March 10th, and at the following setting in April. By September, nine members called for 0.25 percent, two for 0.50 percent, and one for 0.75 percent. By March of 2022, eight members called for 0.25 percent, two for 0.50 percent, one for 1.00 percent, and one for 1.50 percent (see table below).

With respect to the Bank's commitment to buy at least $4 billion of federal government bonds per week, six members voted in favour of the Bank's continuing with quantitative easing on that scale until April 21st, and six voted for the Bank to reduce its purchases. Most of the members who voted in favour of maintaining the program at its current level, however, called for a slower pace of purchases in the future, with one noting that a key reason for not announcing a slower pace on March 10th is that a Monetary Policy Report will accompany the April 21st announcement, giving the Bank more scope to elaborate its reasons and its plans.

Two themes dominated the MPC's discussion of events since the Bank of Canada's last policy-rate announcement in January: more robust economic activity than expected, and heightened concerns about inflation. Members noted that both the Canadian and US economies had finished 2020 on a strong note, and that the first quarter of 2021, previously expected to show real GDP flat or negative, is now expected to show GDP growth, prefiguring a strong 2021 overall. Turning to inflation, members noted strength in commodity prices, wage growth stronger than measures of slack in the labour market would have suggested, and rising inflation expectations, including those reflected in long bond yields.

Notwithstanding the improved outlook for growth and greater evidence of inflationary pressure, the group did not favour any increase in the Bank of Canada's overnight rate target in the near term. In addition to continuing uncertainties about the pace of vaccinations and the resumption of activities suppressed by COVID, the group highlighted the challenge of judging the amount of slack in the economy when the pandemic has affected different sectors so differently. With respect to inflation, several members highlighted the fact that year-over-year increases in the consumer price index will be high through much of 2021 because the recession depressed the year-ago measures, and that other measures of inflationary pressure are consistent with a gradual return to 2 percent increases over the long term.

The group's positive assessment of growth, and response to heightened worries about inflationary pressure, was more evident in its discussion of the quantitative easing program. The majority judged that the need for the Bank to support financial markets with bond purchases had diminished, and that the program should wind down. A desire to prepare market participants for a slower pace of purchases, especially in light of last week's sudden back-up in long bond yields, explains the group's split decision on the program, with several members urging the Bank to maintain the current pace until April.

Votes of MPC Members and the Council Median for Each Announcement (*percent*)					
MPC Members	**Mar 10, 2021**	**Apr 21, 2021**	**Sept 8, 2021**	**Mar 2022**	**Vote on QE ($billions/week)**
Steve Ambler Université du Québec à Montréal (UQAM)	0.25	0.25	0.25	0.50	Less than $4B
Beata Caranci TD Bank	0.25	0.25	0.25	0.25	Less than $4B
Edward A. Carmichael Ted Carmichael Global Macro	0.25	0.25	0.75	1.50	Less than $4B
Michael Devereux University of British Columbia	0.25	0.25	0.50	0.50	Less than $4B
Stéfane Marion National Bank of Canada	0.25	0.25	0.25	0.25	At least $4B
Angelo Melino University of Toronto	0.25	0.25	0.25	0.25	At least $4B
Jean-François Perrault Scotiabank	0.25	0.25	0.25	0.25	Less than $4B
Douglas Porter BMO Capital Markets	0.25	0.25	0.25	0.25	At least $4B
Avery Shenfeld CIBC	0.25	0.25	0.25	0.25	At least $4B
Pierre Siklos Wilfrid Laurier University	0.25	0.25	0.25	0.25	At least $4B
Stephen D. Williamson Western University	0.25	0.25	0.50	1.00	At least $4B
Craig Wright RBC	0.25	0.25	0.25	0.25	Less than $4B
Median Vote	0.25	0.25	0.25	0.25	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 15, 2021 prior to the Bank of Canada's interest rate announcement on April 21, 2021.

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