

May 28, 2020

Bank of Canada Should Keep Overnight Rate at 0.25 Percent, Focus on Implications of Expanded Balance Sheet: C.D. Howe Institute Monetary Policy Council

May 28, 2020 – The C.D. Howe Institute’s **Monetary Policy Council** (MPC) recommends that the Bank of Canada maintains its target for the overnight rate, its benchmark policy interest rate, at 0.25 percent for at least a year.

The MPC provides an independent assessment of the monetary stance consistent with the Bank of Canada’s 2 percent inflation target. **Jeremy Kronick**, Associate Director, Research, chaired today’s meeting, sitting in for the MPC’s usual chair, **William Robson**, the Institute’s President and CEO. 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.

All ten members attending today’s Monetary Policy Council meeting voted to keep the overnight rate at least as low as its current setting – 25 basis points – for the next year, with six members favoring 25 basis points and four members favoring a move to 10 basis points. The latter members (see table) did feel that there was further scope to lower the overnight rate, but stopped short of voting for a zero, or even negative, rate. The consistency in voting for continued monetary stimulus for the foreseeable future reflected the fact that, despite some positive news in consumer spending in sectors that have reopened following the COVID-19 economic shutdown, the output gap will create downward pressure on the inflation rate for some time.

With the overnight rate unlikely to drop much further, members turned their focus to the Bank of Canada’s balance sheet and the implications of the actions taken to date, and what they mean for both monetary policy and financial stability in the short- to medium-term.

Members pointed out that the Bank of Canada has expanded the balance sheet by more than \$300 billion since early March, with the bulk of that expansion coming in the form of repurchase agreements with financial institutions (repos). Most of these repos are short-term assets that will run off the Bank’s balance sheet as they mature. Members judged that, once these repos roll off, there is some indication that a similar expansion on the short end of the yield curve may not be necessary. However, as fiscal expansion continues, the balance sheet will have to turn toward more traditional quantitative easing, buying up government debt at longer-term maturities.

Members highlighted the need for transparency as the Bank of Canada transitions between the run off of short-term assets and further expansion on the longer end of the balance sheet, as well as through purchases of private sector and non-sovereign debt. At the outset of the crisis, the measures put in



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place focused on liquidity and support for key credit markets. As the economy reopens, members felt it was important for the Bank to clarify how it will use both the balance sheet and the overnight rate in conducting monetary policy to hit the 2 percent inflation target over the upcoming six-to-eight-quarter period. Continued guidance and clarity were judged to be essential for Bank operational independence and credibility.

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

MPC Members	Jun. 3	Jul. 15	Dec. 9	Jun. 2021
Steve Ambler Université du Québec à Montréal (UQAM)	0.10	0.10	0.10	0.10
Beata Caranci TD Bank Group	0.25	0.25	0.25	0.25
Edward A. Carmichael Ted Carmichael Global Macro	0.10	0.10	0.10	0.10
Michael Devereux University of British Columbia	0.25	0.25	0.25	0.25
Thorsten Koepl Queen's University	0.10	0.10	0.10	0.10
Stéfane Marion National Bank of Canada	0.25	0.25	0.25	0.25
Angelo Melino University of Toronto	0.10	0.10	0.10	0.10
Avery Shenfeld CIBC	0.25	0.25	0.25	0.25
Pierre Siklos Wilfrid Laurier University	0.25	0.25	0.25	0.25
Craig Wright RBC	0.25	0.25	0.25	0.25
Median Vote	0.25	0.25	0.25	0.25

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 July 9, 2020 prior to the Bank of Canada's interest rate announcement on July 15, 2020.

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