

July 9, 2020

## Bank of Canada Should Keep Overnight Rate at 0.25 Percent over Coming Year: C.D. Howe Institute Monetary Policy Council

July 9, 2020 – 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 until at least July of 2021.

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 eight members of the MPC attending this meeting were unanimous in calling for the Bank to keep the overnight rate low for at least the next year. Six of the members called for maintaining the target at 0.25 percent. Two called for lowering it to 0.10 percent and maintaining it there (see table below).

In looking at the outlook for economic activity, the group noted a number of positives since the Bank of Canada’s last overnight rate announcement. Indicators of spending and output in many advanced economies, notably the United States, suggest a rebound after the COVID-19-induced shutdowns of the spring. Income and credit support policies appear to have cushioned the downturn and boosted the recovery. Less positively, the coronavirus continues to spread in emerging markets, and resurgences, notably in the United States, threaten setbacks in the second half of the year.

On balance, the news about Canada’s economy has been good, with stronger-than-expected jobs and housing-starts numbers getting particular attention. Government income supports and stronger oil prices have also been near-term positives. The group generally expected solid third-quarter growth. Expectations for the later part of the year were tempered by the same uncertainties that affect the global outlook, as well as particular concerns about the phase-out of fiscal measures and buildups of debt, including mortgages.

With respect to inflation, the group debated the extent to which Canada’s productive capacity has suffered long-lasting damage from COVID-19, as well as the implications of damage to productive capacity for the size and likely duration of the current disinflationary output gap. While the group did not see any likelihood of near-term inflationary pressure, some members commented that traditional measures of economic slack, such as the unemployment rate, might be misleading, and some noted that current measures of consumer price inflation are less reliable than usual because the CPI basket does not take account of recent changes in purchasing patterns and the reduced availability of many goods and services.

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The rapid expansion and changing composition of the Bank of Canada's balance sheet was a major focus of the MPC's discussion. Here, too, the group had few concerns about near-term inflationary pressure – seeing the Bank's asset purchases and provision of liquidity as straightforward responses to the COVID-19 crisis, and in line with moves by other major central banks. Looking ahead, however, several members noted that government financing needs are going to continue to be extraordinarily high for some time, and that the Bank of Canada needs to avoid becoming a significant allocator of credit. A theme of many comments was that the Bank should be clearer about its criteria for future changes in its balance sheet, both as regards its overall size, and particular categories of assets.

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

| MPC Members   | Jul. 15 | Sep. 9 | Jan. 2021 | Jun. 2021 |
|---|---------|--------|-----------|-----------|
| <b>Steve Ambler</b><br>Université du Québec à Montréal (UQAM) | 0.25    | 0.25   | 0.25      | 0.25      |
| <b>Edward A. Carmichael</b><br>Ted Carmichael Global Macro    | 0.25    | 0.25   | 0.25      | 0.25      |
| <b>Stéfane Marion</b><br>National Bank of Canada              | 0.25    | 0.25   | 0.25      | 0.25      |
| <b>Angelo Melino</b><br>University of Toronto                 | 0.10    | 0.10   | 0.10      | 0.10      |
| <b>Douglas Porter</b><br>BMO Capital Markets                  | 0.25    | 0.25   | 0.25      | 0.25      |
| <b>Pierre Siklos</b><br>Wilfrid Laurier University            | 0.10    | 0.10   | 0.10      | 0.10      |
| <b>Stephen D. Williamson</b><br>Western University            | 0.25    | 0.25   | 0.25      | 0.25      |
| <b>Craig Wright</b><br>RBC                                    | 0.25    | 0.25   | 0.25      | 0.25      |
| <b>Median Vote</b>  | 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 September 3, 2020 prior to the Bank of Canada's interest rate announcement on September 9, 2020.

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