Monetary Policy Council

Communiqué

December 3, 2020

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

December 3, 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 at least until December of 2021. A majority of MPC members recommend that the Bank of Canada scale back its quantitative easing program of Government of Canada bond purchases.

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 on January 20th, 2021.

Eight of the nine members of the MPC attending this meeting called for the Bank to keep the overnight rate at 0.25 at its upcoming setting on December 9th, while one member called for a setting of 0.10 percent. The recommendations for the settings in January of 2021 were the same. By June of 2021, one member called for a setting of 0.50 percent. By December of 2021, that member called for 1.25 percent, and another member called for 0.50 percent (see table below).

In assessing the outlook for economic activity, the group emphasized a number of positive developments. Notwithstanding concerns about the impact of recent restrictive measures to contain the spread of COVID-19, members noted improvements in the global outlook, with rebounding trade volumes and strong commodity prices being particularly supportive for Canada, and job-market and other indicators showing a rapid recovery from last spring's collapse. Several members emphasized the strong incomes and high saving rates of Canadian households, which likely prefigure continued strength in consumer spending and residential investment, especially as vaccination protects a growing proportion of the population from the coronavirus.

In assessing inflation, the group debated the short- and longer-run impacts of the pandemic on Canada's productive capacity, and the implications of those impacts for the size and duration of any resulting disinflationary output gap. An important theme in the discussion was that simultaneous down- and up-shifts in demand and supply in some sectors meant that total slack in the economy has been less than the paths of aggregate measures such as GDP would indicate. Members noted that many measures of inflation remain close to the 2 percent target, that wage growth is strong, and that the spread between nominal and real-return bonds has been widening. Given continued uncertainty about the course of the pandemic and its economic impact, however, the majority of members were comfortable with the current level of the overnight rate for some time to come.

The size and composition of the Bank of Canada's balance sheet was a major focus of the MPC's discussion. Some members expressed desire for more clarity from the Bank about the intended effects of its asset purchases, particularly assets it has not traditionally held. Many members noted that the federal government's Fall Economic Statement prefigured high levels of borrowing for an extended period, and expressed concerns about the Bank's apparent role as a major buyer of government debt. While three of the nine MPC members attending the meeting felt that the Bank's current commitment to buy at least $4 billion of Government of Canada bonds per week until its next interest-rate announcement on January 20th, 2021, was appropriate, the other six felt that the Bank should reduce these purchases.

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

MPC Members	Dec 9	Jan 20, 2021	Jun 9, 2021	Dec 8, 2021	Vote on QE ($billions/week)
Steve Ambler Université du Québec à Montréal (UQAM)	0.25	0.25	0.25	0.25	Less than $4B
Beata Caranci TD Bank	0.25	0.25	0.25	0.25	At least $4B
Edward A. Carmichael Ted Carmichael Global Macro	0.25	0.25	0.50	1.25	Less than $4B
Michael Devereux University of British Columbia	0.25	0.25	0.25	0.25	Less than $4B
Stéfane Marion National Bank of Canada	0.25	0.25	0.25	0.25	Less than $4B
Angelo Melino University of Toronto	0.10	0.10	0.10	0.10	At least $4B
Douglas Porter BMO Capital Markets	0.25	0.25	0.25	0.25	At least $4B
Pierre Siklos Wilfrid Laurier University	0.25	0.25	0.25	0.25	Less than $4B
Stephen D. Williamson Western University	0.25	0.25	0.25	0.50	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 January 14, 2021 prior to the Bank of Canada's interest rate announcement on January 20, 2021.

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