C.D. Howe Institute Monetary Policy Council Calls for Bank of Canada to Hold Overnight Rate at 0.50 through 2016; Looks for 0.75 Percent by April 2017

April 7, 2016 – The C.D. Howe Institute's **Monetary Policy Council** (MPC) today recommended that the Bank of Canada keep its target for the overnight rate, the very short-term interest rate it targets for monetary policy purposes, at 0.50 percent at its next announcement on April 13, 2016. Looking ahead, the Council called for the Bank to hold the target at 0.50 percent through the end of the year, raising it to 0.75 percent by April 2017.

The MPC provides an independent assessment of monetary stance consistent with the Bank of Canada's 2 percent inflation target. **William Robson**, the Institute's President and 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 the members attending the meeting.

On this occasion, a near unanimous recommendation was reached regarding both the Bank of Canada's upcoming announcement, as well as its May decision: leave the overnight rate unchanged at 0.50 percent with one member recommending a cut to 0.25 percent. Looking through the remainder of the year, the consensus was to continue to leave the rate unchanged at 0.50 percent, with the lone dissenting vote recommending an increase to 0.75 percent in six months. By April 2017, five favoured continuing at 0.50 percent, while three favoured an increase to 0.75 percent, and two recommending a larger increase to 1.00 percent (see table below).

The view of the MPC members was that the outlook for Canadian economic activity was strong in the first quarter, led by trade, as the impact of previous Bank of Canada cuts to interest rates and the shifting of the economy away from resources to manufacturing continue. Looking out past the first quarter, MPC members saw more uncertainty, with discussions focusing on the impacts of the recently released federal government budget, the strength of the U.S. economy, central bank easing in the EU and Japan, as well as the effects on disposable income of taxes on past government credits.

From the perspective of actual GDP growth, there was a mix of views among members. On the impact of the federal budget, the consensus view was that no significant lift to the economy would be realized over the course of the year. Trade numbers were stronger at the beginning of the year, though recent numbers suggest a degree of slow down, with mixed signals arising on the world stage as the US experiences its typically slow first quarter, the ECB stands by their accommodative monetary policy, and uncertainty in China continues. One member pointed out that the exchange rate may have over-corrected recently, which may impact how strong trade will be over the remainder of the year. Another member mentioned that trade has to continue to be strong as domestic demand remains flat, bringing into question the sustainability of the rebound.

Some disagreement on inflation expectations arose during the discussions. While some argued that inflation expectations were well-anchored, others made the point that realized inflation in Canada is heavily impacted by global inflation, and with oil prices low, global inflation remains low as well. Spreads between yields on Government of Canada nominal-return and real-return long-term bonds remain well-below 2.0 percent, a level they maintained from late 2011 until late 2014.

MPC members also discussed the issue of central bank coordination. Some members voiced the need to begin normalizing interest rates, however this becomes more complicated if other, larger economies, such as the US and EU are either standing still or being accommodative. The effect of increasing interest rates in Canada in this scenario, simply leads to an appreciation of the exchange rate, disrupting the rebound in trade that is driving the economy.

The median call for the rate to remain unchanged reflected, on the one hand, uncertainty over the sustainability of the rebound given flat domestic demand and global concerns, and, on the other hand, the need to normalize interest rates.

The following table shows the votes of each MPC member, as well as the Council's median vote, for the relevant Bank of Canada policy-rate announcements.

MPC Members	Apr 13	May 25	6 months	12 months
Steve Ambler Université du Québec à Montréal (UQAM)	0.50	0.50	0.50	0.75
Edward Carmichael Ted Carmichael Global Macro	0.50	0.50	0.50	0.50
Thorsten Koeppl Queens University	0.50	0.50	0.50	1.00
Stéfane Marion National Bank Financial	0.50	0.50	0.50	0.50
Angelo Melino University of Toronto	0.25	0.25	0.50	0.50
Douglas Porter BMO Capital Markets	0.50	0.50	0.50	0.50
Nicholas Rowe Carleton University	0.50	0.50	0.50	0.75
Pierre Siklos Wilfrid Laurier University	0.50	0.50	0.75	1.00
David Tulk TD Securities Inc.	0.50	0.50	0.50	0.50
Craig Wright RBC	0.50	0.50	0.50	0.75
Median Vote	0.50%	0.50%	0.50%	0.75%

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 May 19, 2016 prior to the Bank of Canada's interest rate announcement on May 25, 2016.

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