C.D. Howe Institute Monetary Policy Council Calls for Bank of Canada to Hold Overnight Rate at 0.50 Percent until 2017

January 14, 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 January 20, 2016, and maintain it at that level for the rest of the year.

The MPC provides an independent assessment of the monetary stance appropriate for the Bank of Canada as it pursues its 2 percent inflation target. **William Robson**, the Institute's President and Chief Executive Officer, 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, the median results of 0.50 percent for the settings masked marked contrasts in the recommendations of individual members: recommendations included an unchanged rate in the near term with increases thereafter; an unchanged rate at 0.50 through the year; a cut to 0.25 in the near term with increases thereafter; a cut to 0.25 for the next year; while one member recommended 0.50 at the upcoming setting, followed by a cut to 0.25 percent in March (see table below).

Looking at the distribution of recommendations by date: for next week's setting, seven of the 11 members attending the meeting recommended 0.50 percent, and four 0.25 percent; for the March setting, six recommended 0.50 percent and five 0.25 percent; for the July setting, eight recommended 0.50 percent and three 0.25 percent. For January of 2017, four recommended 0.75 percent, four 0.50 percent, and three 0.25 percent.

MPC members generally agreed that indicators of recent economic activity in Canada and expectations of future activity have been disappointingly subdued. The variations among their recommendations, however, reflected key differences in their judgements about the implications of those indicators for inflation, and about such potential influences as the exchange rate, fiscal policy, and confidence among Canadian businesses and households.

The disinflationary output gap spurred lively discussion. Several members highlighted the need to distinguish temporary impacts of falling oil prices and deteriorating terms of trade on the economy's productive capacity as resources move between sectors and regions, on the one hand, from more lasting reductions in potential growth, on the other. Disagreements about the output gap and its likely future development underlay some of the differences in members' recommendations.

The recent sharp decline in the Canadian dollar against the US dollar and other currencies also prompted debate. Members differed about the degree to which the deterioration in Canada's terms of trade justified the dollar's fall, and also about the possibility that damage to public confidence from further precipitous declines might outweigh any beneficial effect to trade-oriented sectors of the economy.

For some members, potential changes in fiscal policy were also a consideration. Two members stressed that their recommendations were contingent on assumptions about the upcoming federal budget and its potentially stimulative economic effects.

The potential effect of a cut in the overnight rate on expectations also featured in the discussion. Some members felt that a cut might feed expectations of further cuts and a possible move into negative territory, emphasizing potential damage to confidence as a result. Others noted that discussion about a negative overnight rate was appropriate in the context of the Bank of Canada's upcoming renewal of its inflation target, and ought not to be seen as signaling the near-term direction of monetary policy.

On balance, the median call from this MPC meeting reflected less desire among members for a higher overnight rate in the coming months – in turn, a reflection of the persistence of inflation below the 2 percent target, and a tendency for forecast updates to postpone its expected return to target.

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	Jan 20	Mar 9	6 months	12 months
Steve Ambler Université du Québec à Montréal (UQAM)	0.50	0.50	0.50	0.75
Paul Beaudry University of British Columbia	0.50	0.50	0.50	0.50
Edward Carmichael Ted Carmichael Global Macro	0.25	0.25	0.25	0.25
Thorsten Koeppl Queens University	0.50	0.50	0.50	0.75
Stefane Marion National Bank	0.50	0.50	0.50	0.50
Angelo Melino University of Toronto	0.25	0.25	0.50	0.75
Douglas Porter BMO Capital Markets	0.50	0.25	0.25	0.25
Nicholas Rowe Carleton University	0.25	0.25	0.50	0.75
Avery Shenfeld CIBC World Markets Inc.	0.50	0.50	0.50	0.50
David Tulk TD Bank	0.25	0.25	0.25	0.25
Craig Wright RBC	0.50	0.50	0.50	0.50
Median Vote	0.50%	0.50%	0.50%	0.50%

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 March 3, 2016 prior to the Bank of Canada's interest rate announcement on March 9, 2016.

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