C.D. Howe Institute Monetary Policy Council Calls for Bank of Canada to Hold Overnight Rate at 0.50 Percent until mid-2016; Hike to 0.75 Percent by next November

November 26, 2015 – 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 December 2, 2015. Looking ahead, the Council called for the Bank to hold the target at 0.50 percent until May 2016 and hike it to 0.75 percent by November 2016.

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 calls for the Bank to hold the overnight rate target at 0.50 percent next week and at the following setting in January 2016 were unanimous. By May 2016, five of the nine members attending the meeting still preferred an overnight rate of 0.50 percent, with four wanting a hike to 0.75 percent. By November 2016, four preferred 0.50 percent, four preferred 0.75 percent and one called for a hike to 1.00 percent.

The uniform calls for no near-term change in the overnight rate reflected a widespread view among MPC members that economic activity in the Canadian economy will continue to be subdued. Several members highlighted recent weakness in commodity prices as a concern, with adverse movement in Canada's terms of trade putting continued pressure on Canadian incomes. Members who favoured increases in the overnight rate further out tended to see these negative influences as temporary, with disinflationary slack in the Canadian economy disappearing and inflation returning to target more or less as the Bank of Canada anticipates. Members who favoured an unchanged policy rate for a year

emphasized such indicators as falling profits, weak business investment and decelerating wages, and also noted that the boost a lower Canadian dollar had given inflation will disappear from the year-over-year numbers.

The difference between potential and actual output in Canada was a major topic of conversation at the Council meeting. Many members argued that the output gap remains an important determinant of inflation, but noted that demographic changes and weak capital investment make estimates of potential unusually difficult. Others expressed more fundamental doubts about the significance of the output gap, especially its influence on inflation expectations. A desire for the Bank of Canada to elaborate its own views on the size and significance of the output gap was a strong theme in the discussion.

US monetary policy was another major topic. Several members thought that the widely expected December hike in the Federal Funds rate would push interest rates higher at longer maturities. Some argued that the resulting dampening of housing and other activity in Canada would reduce the pressure for the Bank of Canada to raise the overnight rate; others expressed the opposite concern: that higher interest rates generally would undermine needed growth. Whether a Fed hike would send the Canadian-US dollar exchange rate lower, potentially stimulating Canadian output, was another point of contention. Some members felt the Bank of Canada should also address this topic in its commentary accompanying the upcoming policy rate setting.

The MPC discussed domestic financial imbalances less this time than it typically has in recent meetings. Concerns about the leverage of Canadian households did affect some members' views about the size and timing of potential increases in the overnight rate, however, with those members urging the Bank to proceed more cautiously than it otherwise would.

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	Dec 2	Jan 20	6 months	12 months
Steve Ambler Université du Québec à Montréal (UQAM)	0.50%	0.50%	0.75%	0.75%
Edward A. Carmichael Ted Carmichael Global Macro	0.50%	0.50%	0.50%	0.50%
Thorsten Koeppl Queens University	0.50%	0.50%	0.75%	0.75%
Stéfane Marion National Bank	0.50%	0.50%	0.50%	0.50%
Angelo Melino University of Toronto	0.50%	0.50%	0.50%	1.00%
Nicholas Rowe Carleton University	0.50%	0.50%	0.75%	0.75%
Avery Shenfeld CIBC World Markets Inc.	0.50%	0.50%	0.50%	0.50%
Pierre Siklos Wilfrid Laurier University	0.50%	0.50%	0.75%	0.75%
David Tulk TD Bank	0.50%	0.50%	0.50%	0.50%
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 January 14, 2016 prior to the Bank of Canada's interest rate announcement on January 20, 2016.

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Contact: Kristine Gray – phone: 416-865-1904; e-mail: **kgray@cdhowe.org.**