

January 14, 2021

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

January 14, 2021 – 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 January of 2022. A majority of MPC members also recommends that the Bank of Canada maintain its current quantitative easing purchases of Government of Canada bonds.

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 March 10th, 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 January 20th, while one member called for a setting of 0.10 percent. The recommendations for the settings in March were the same. By July, one member called for a setting of 0.75 percent. By January of 2022, that member called for 1.50 percent, two other members called for 0.50 percent, and the member who wanted 0.10 percent over the next six months raised his recommendation to 0.25 percent (see table below).

The main themes of the Council’s discussion of the outlook for economic activity were greater-than-expected momentum at the end of 2020, the likelihood of flat to negative first quarters in the United States and Canada resulting from the resurgence of COVID-19 and related restrictions, and prospects for a sharp rebound in the second half of the year. Several members cited robust household balance sheets, strong prices for Canada’s commodity exports, and the release of pent-up demand as more of the population gets vaccinated as factors behind their optimistic outlook for growth over the course of 2021.

The Council’s discussion of the outlook for inflation devoted considerable attention to indicators signaling that inflation may return to the 2 percent target earlier than might have been expected in late 2020, among them higher wholesale prices, buoyant financial and housing markets, and a more tolerant attitude toward inflation, notably on the part of the US Federal Reserve. While these and other indicators of inflation and inflationary expectations led some members to recommend a higher overnight rate within 12 months, most members felt that near-term weakness in the economy, and the persistence of a disinflationary output gap under even more optimistic scenarios for aggregate demand, justified the Bank of Canada maintaining the overnight rate target at 0.25 percent.

January 14, 2021

One area of uncertainty probed in the Council's discussion was the extent to which the pandemic and its resurgence would scar the economy and adversely affect productive capacity and demand during the upcoming expansion. Another topic that received considerable attention was the rapid growth in monetary aggregates, and whether prolonging the current combination of deficit-financed government income supports and central bank bond purchases threatened above-target inflation. For the majority of Council members, these concerns did not outweigh the need for continued accommodative monetary policy, resulting in majority votes in favour of an unchanged overnight rate and continuation of the Bank's quantitative easing program.

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

MPC Members	Jan 20, 2021	Mar 10, 2021	Jul 14, 2021	Jan 2022	Vote on QE (\$billions/week)
<b>Steve Ambler</b> Université du Québec à Montréal (UQAM)	0.25	0.25	0.25	0.50	Less than \$4B
<b>Edward A. Carmichael</b> Ted Carmichael Global Macro	0.25	0.25	0.75	1.50	Less than \$4B
<b>Stéfane Marion</b> National Bank of Canada	0.25	0.25	0.25	0.25	At least \$4B
<b>Angelo Melino</b> University of Toronto	0.10	0.10	0.10	0.25	At least \$4B
<b>Jean-François Perrault</b> Scotiabank	0.25	0.25	0.25	0.25	At least \$4B
<b>Douglas Porter</b> BMO Capital Markets	0.25	0.25	0.25	0.25	At least \$4B
<b>Avery Shenfeld</b> CIBC	0.25	0.25	0.25	0.25	At least \$4B
<b>Stephen D. Williamson</b> Western University	0.25	0.25	0.25	0.50	Less than \$4B
<b>Craig Wright</b> RBC	0.25	0.25	0.25	0.25	At least \$4B
<b>Median Vote</b>	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 March 4, 2021 prior to the Bank of Canada's interest rate announcement on March 10, 2021.

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