



## U.S. FEDERAL RESERVE

### The Fed has cut its key interest rates again, but is trying to close the door on further cuts

#### ACCORDING TO THE U.S. FEDERAL RESERVE (Fed)

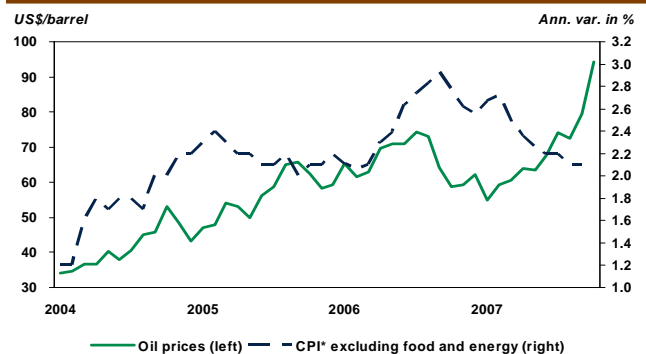
- The interest rate target for federal funds goes from 4.75% to 4.50%. The decision was not unanimous (9 to 1 – the Kansas City Fed's Thomas Hoenig).
- The discount rate has also been decreased by 25 basis points, from 5.25% to 5.00%.
- Economic growth was solid in the third quarter, but the pace of growth should slow in the near future.
- The statistics on core inflation are still showing modest price growth. However, some inflation risks from energy and commodities are intensifying.
- The upside risks to inflation and downside risks to the economy are roughly balanced. The Fed will continue to watch the situation and act as needed.

#### COMMENTS

Fed leaders decided to move ahead with the monetary easing initiated in September. The action was a little more measured this time—a cut of 25 basis points—whereas the Fed's unexpected 50-point cut last month had come as a surprise. Ben Bernanke and his colleagues are still expressing concern about the U.S. economic situation. Their worries seem to be less acute at this point, given the good news from Q3's national accounts and relative calm noted on the financial markets.

The outlook for inflation is still making Fed leaders uncomfortable. They are reiterating that the latest figures on core inflation are encouraging. However, the risks persist. Clearly, the recent increase by oil and commodities prices is a concern for several members of the monetary policy committee. However, long-term inflation expectations are stable and the GDP deflator released this morning showed its weakest quarterly growth since the summer of 1963. The

#### Core inflation is moderating, but the risks associated with the increase in energy prices remain high



\* Consumer price index.  
Sources: Bureau of Labor Statistics, Datastream and Desjardins, Economic Studies

risks associated with inflation thus seem limited to us and we think core inflation will remain low through the end of 2007 and 2008.

**Implications:** The Fed is simultaneously concerned about the outlook for economic growth and inflation risks. Its statement also signals that these risks are roughly balanced. However, in our view, this balance is precarious. Our scenarios and several indicators show that the probability the situation will deteriorate is high. Even though the Fed is emphasizing that its two key rate cuts balance the risks, it seems to us that a further decrease to the target rate for federal funds is possible at the December 11 meeting. However, if further signs of stronger than forecast growth emerge or inflation is less favourable, clearly, the Fed will opt for the status quo.

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**EXCERPT FROM THE U.S. FEDERAL RESERVE PRESS RELEASE  
OCTOBER 31, 2007**


The Federal Open Market Committee decided today to lower its target for the federal funds rate 25 basis points to 4-1/2 percent.

Economic growth was solid in the third quarter, and strains in financial markets have eased somewhat on balance. However, the pace of economic expansion will likely slow in the near term, partly reflecting the intensification of the housing correction. Today's action, combined with the policy action taken in September, should help forestall some of the adverse effects on the broader economy that might otherwise arise from the disruptions in financial markets and promote moderate growth over time.

Readings on core inflation have improved modestly this year, but recent increases in energy and commodity prices, among other factors, may put renewed upward pressure on inflation. In this context, the Committee judges that some inflation risks remain, and it will continue to monitor inflation developments carefully.

The Committee judges that, after this action, the upside risks to inflation roughly balance the downside risks to growth. The Committee will continue to assess the effects of financial and other developments on economic prospects and will act as needed to foster price stability and sustainable economic growth.

**Table 1  
Schedule and key rates**

Date	Central Bank	Decision	Rate
<b>August 2007</b>			
7	U.S. Federal Reserve	s.q.	5.25
15	Bank of Norway	+25 b.p.	4.75
22	Bank of Japan	s.q.	0.50
24	Bank of Mexico	s.q.	7.25
<b>September 2007</b>			
4	Reserve Bank of Australia	s.q.	6.50
5	Bank of Brazil	-25 b.p.	11.25
5	Bank of Canada	s.q.	4.50
6	European Central Bank	s.q.	4.00
6	Bank of England	s.q.	5.75
7	Bank of Sweden	+25 b.p.	3.75
12	Reserve Bank of New Zealand	s.q.	8.25
13	Swiss National Bank	+25 b.p.	2.75
18	U.S. Federal Reserve	-50 b.p.	4.75
19	Bank of Japan	s.q.	3.00
21	Bank of Mexico	s.q.	7.25
21	Bank of Norway	+25 b.p.	5.00
<b>October 2007</b>			
2	Reserve Bank of Australia	s.q.	6.50
4	European Central Bank	s.q.	4.00
4	Bank of England	s.q.	5.75
11	Bank of Japan	s.q.	0.50
16	Bank of Canada	s.q.	4.50
17	Bank of Brazil	s.q.	11.25
24	Reserve Bank of New Zealand	s.q.	8.25
30	Bank of Mexico	+25 b.p.	7.50
30	Bank of Sweden	+25 b.p.	4.00
31	Bank of Japan	s.q.	0.50
30	Bank of Norway	s.q.	5.00
31	U.S. Federal Reserve	-25 b.p.	4.50

s.q.: status quo; b.p. : basis points  
Source: Desjardins, Economic Studies

**Table 2  
Coming soon...**

Date	Central Bank
<b>November 2007</b>	
6	Reserve Bank of Australia
8	European Central Bank
8	Bank of England
12 - 13	Bank of Japan
23	Bank of Mexico
<b>December 2007</b>	
4	Reserve Bank of Australia
4	Bank of Canada
4 - 5	Bank of Brazil
6	European Central Bank
6	Bank of England
6	Reserve Bank of New Zealand
7	Bank of Mexico
11	U.S. Federal Reserve
12	Bank of Norway
13	Swiss National Bank
18	Bank of Sweden
19 - 20	Bank of Japan
<b>January 2008</b>	
9 - 10	Bank of England
10	European Central Bank
18	Bank of Mexico
21 - 22	Bank of Japan
22	Bank of Canada
23	Bank of Norway
24	Reserve Bank of New Zealand
29 - 30	U.S. Federal Reserve
<b>February 2008</b>	
5	Reserve Bank of Australia
6 - 7	Bank of England

Source: Desjardins, Economic Studies