

December 4, 2007



BANK OF CANADA

The BoC lowers its key rate to 4.25% due to the proliferation of downside risks

ACCORDING TO THE BANK OF CANADA (BoC)

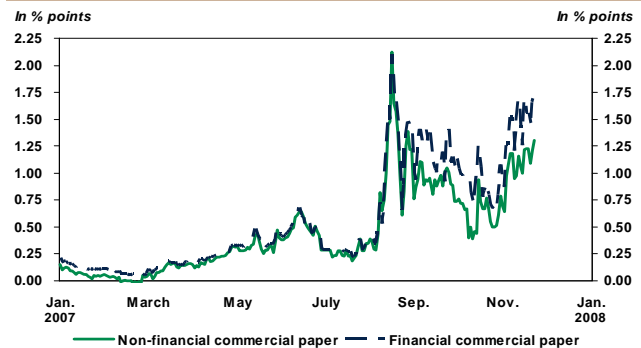
- The target for the overnight rate has been lowered 25 basis points to 4.25%.
- Increased competitive pressures related to the strong loonie led to slower than forecast progress by inflation.
- The Canadian economy continues to operate above its production capacity.
- However, the difficulties facing global financial markets have worsened and should persist for a longer period of time than expected, and credit conditions have tightened.
- The Bank judges that the balance of risks associated with the inflation projection has shifted to the downside.

COMMENTS

Taking action that is clearly preventive, the BoC kept pace with the U.S. Federal Reserve and cut its key rate by 25 basis points this morning. Note that this first decrease since April of 2004 comes at a time when Canadian domestic demand is going strong. The action should please those who have been asking the BoC for monetary easing for some time.

Surely, the darkening outlook held the most weight in the BoC decision, and the Bank seems to have taken advantage of it to avoid being out of synch with market expectations. Specifically, the troubles associated with the liquidity crisis have worsened, causing bank financing costs to increase and credit conditions to tighten further. Parallel to that, the risks to the outlook for demand for Canadian exports have intensified due to the ongoing American housing sector correction. The loonie's recent correction is welcome, but it remains at a high level and its adverse impacts on Canada's foreign trade will continue to be felt. Canadian consumers and businesses have already taken advantage of their increased buying power, with imports advancing almost eight times faster than exports this summer.

The widening of credit spreads is a concern



Sources: Datastream and Desjardins, Economic Studies

In the end, it was good performance by inflation that allowed the BoC to outstrip our projection and lower its key rate prior to January of 2008. Total and core inflation were weaker than forecast in October, due to heightened competitive effects associated with our currency's vitality. With the loonie settling in above parity in November, downside pressure on consumer prices are likely to continue. This should allow the BoC to further ease its monetary policy in the next few months to keep the economy from slowing sharply.

With the ongoing U.S. slowdown, downward pressure on Canada's net exports and the unsustainable pace of stockpiling here, we now expect two more rate cuts, in January and March. This would take the target for the overnight rate to 3.75%.

Martin Lefebvre
Senior Economist

François Dupuis
Vice-President and Chief Economist

Yves St-Maurice
Director and Deputy Chief Economist

Mathieu D'Anjou
Economist

Martin Lefebvre
Senior Economist

Hendrix Vachon
Economist

514-281-2336 or 1 866 866-7000, ext. 2336
E-mail: desjardins.economics@desjardins.com

NOTE TO READERS: The letters **k**, **M** and **B** are used in texts and tables to refer to thousands, millions and billions respectively.

IMPORTANT: This document is based on public information, obtained from sources that are deemed to be reliable. Desjardins Group in no way guarantees that the information is complete or accurate. The document is provided solely for information purposes and does not constitute an offer or solicitation for purchase or sale. The document may under no circumstances be construed as a commitment by Desjardins Group, which takes no responsibility for the consequences of any decision made based on the information herein. The prices and rates shown are for information purposes only as they may change at any time based on market conditions. Past returns are no guarantee of future performance, and Desjardins Group does not hereby purport to provide any investment advice. The opinions and forecasts contained herein are, unless otherwise indicated, those of the document's authors and do not represent the official position of Desjardins Group. Copyright © 2007, Desjardins Group. All rights reserved.

**EXCERPT FROM THE BANK OF CANADA PRESS RELEASE
DECEMBER 4, 2007**


[...] However, both total CPI inflation and core inflation in October, at 2.4 per cent and 1.8 per cent respectively, were below the Bank's expectations, reflecting increased competitive pressures related to the level of the Canadian dollar. The Bank now expects inflation over the next several months to be lower than was projected in the MPR. In the context of exceptional volatility in global financial markets, the Canadian dollar spiked well above parity with the U.S. dollar in November, but it has recently traded closer to the 98-cent-U.S. level assumed in the October MPR.

Overall, the Canadian economy continues to operate above its production capacity. Given the strength of domestic demand and weak productivity growth, there continue to be upside risks to the Bank's inflation projection.

However, other developments since October suggest that the downside risks to the Bank's inflation projection have increased. Global financial market difficulties related to the valuation of structured products and anticipated losses on U.S. sub-prime mortgages have worsened since mid-October, and are expected to persist for a longer period of time. In these circumstances, bank funding costs have increased globally and in Canada, and credit conditions have tightened further. There is an increased risk to the prospects for demand for Canadian exports as the outlook for the U.S. economy, and in particular the U.S. housing sector, has weakened. [...]

**Table 1
Schedule and key rates**

Date	Central Bank	Decision	Rate
September 2007			
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
October 2007			
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
November 2007			
6	Reserve Bank of Australia	+25 b.p.	6.75
8	European Central Bank	s.q.	4.00
8	Bank of England	s.q.	5.75
8	Bank of Japan	s.q.	0.50
23	Bank of Mexico	s.q.	7.50
December 2007			
4	Bank of Canada	-25 b.p.	4.25

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

**Table 2
Coming soon**

Date	Central Bank
December 2007	
4	Reserve Bank of Australia
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
January 2008	
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
February 2008	
5	Reserve Bank of Australia
6 - 7	Bank of England
7	European Central Bank
12	Bank of Sweden
14 - 15	Bank of Japan
15	Bank of Mexico
Mars 2008	
4	Reserve Bank of Australia
4	Bank of Canada

Source: Desjardins, Economic Studies