Essentials of the Monetary Policy

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U.S. FEDERAL RESERVE

Monetary Easing Continues Apace

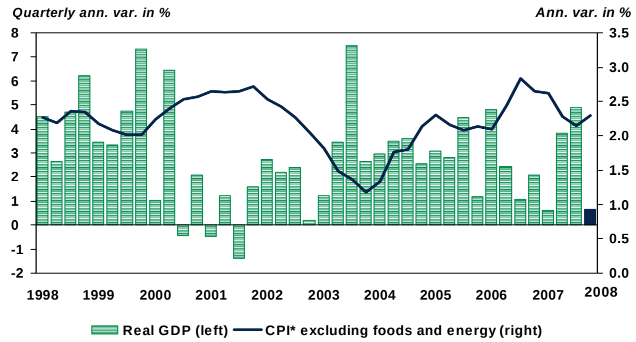
ACCORDING TO THE U.S. FEDERAL RESERVE (Fed)

- One week after its surprise 75 basis point decrease, the Fed used its official meeting to announce another 50 basis point cut to its key rates. The target interest rate for federal funds goes from 3.50% to 3.00%. The discount rate has also been decreased by 50 basis points, from 4.00% to 3.50%.
- Nine members of the monetary policy committee (FOMC) voted for the cut, and one member (the Dallas Fed's Richard Fisher) was in favour of keeping rates steady.
- The financial markets are still under strain and credit conditions are continuing to tighten. The housing market situation is deteriorating further, and the job market is showing signs of weakness.
- The Fed expects inflation to moderate in the coming quarters.
- The downside risks to economic growth remain. The decisions made to date should support moderate economic growth and mitigate the risks to activity. The Fed will continue to watch the situation and act as needed.

COMMENTS

Initiated last September and ramped up last week with a surprise cut, monetary easing continued today. In all, cuts to the target for the federal funds rate total 225 basis points, while discount rate cuts total 275 basis points. The Fed has now taken very strong action, although the official statistics available to date do not indicate an overall decline by employment or a decrease in real GDP. The Fed is thus acting preemptively to support economic growth and eliminate any doubt in investors as to its intention of keeping the situation from deteriorating too sharply and avoid excess pessimism on markets. Today's statement retains a downside bias in terms of the FOMC's future decisions.

Slowing economic growth should cause core inflation to moderate



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

It is now hard to accuse Ben Bernanke and his FOMC colleagues of anti-inflation dogmatism. The key rate cuts are occurring in a situation in which price increases are still above the comfort zones of a number of Fed leaders. As a result, we are now quite far from a central bank that was only focused on its inflation target. Ben Bernanke is betting that price growth will moderate this year. We think so, too. The Fed's projections for the economy and inflation will be published in three weeks, in the minutes of this meeting. In February, Bernanke will also be submitting the Fed's semi-annual report to the U.S. Congress.

Implications: The Fed has already made substantial interest rate cuts, but their work is not done. We expect monetary easing to continue, with the Fed striving to stave off a recession at all costs. The target rate for federal funds could reach 2.25% at mid-year. This movement, and the government's fiscal assistance plan, will help the United States avoid a sharp drop in economic activity.

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EXCERPT FROM THE U.S. FEDERAL RESERVE PRESS RELEASE JANUARY 30, 2008

The Federal Reserve Board

The Federal Open Market Committee decided today to lower its target for the federal funds rate 50 basis points to 3 percent.

Financial markets remain under considerable stress, and credit has tightened further for some businesses and households. Moreover, recent information indicates a deepening of the housing contraction as well as some softening in labor markets.

The Committee expects inflation to moderate in coming quarters, but it will be necessary to continue to monitor inflation developments carefully.

Today's policy action, combined with those taken earlier, should help to promote moderate growth over time and to mitigate the risks to economic activity. However, downside risks to growth remain. The Committee will continue to assess the effects of financial and other developments on economic prospects and will act in a timely manner as needed to address those risks

Table 1
Schedule and key rates

Date	*Central Bank*	*Decision*	*Rate*
October 2007			
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	Reserve Bank of Australia	s.q.	6.75
4	Bank of Canada	-25 b.p.	4.25
5	Reserve Bank of New Zealand	s.q.	8.25
5	Bank of Brazil	s.q.	11.25
6	European Central Bank	s.q.	4.00
6	Bank of England	-25 b.p.	5.50
7	Bank of Mexico	s.q.	7.50
11	U.S. Federal Reserve	-25 b.p.	4.25
January 2008			
10	European Central Bank	*s.q.*	4.00
10	Bank of England	*s.q.*	5.50
18	Bank of Mexico	s.q.	7.50
21	Bank of Japan	s.q.	0.50
22	Bank of Canada	-25 b.p.	4.00
22	U.S. Federal Reserve	-75 b.p.	3.50
17	Bank of Norway	s.q.	5.25
24	Reserve Bank of New Zealand	s.q.	8.25
30	Bank of Brazil	s.q.	11.25
30	U.S. Federal Reserve	-50 b.p.	3.00

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

Table 2
Coming soon

Date	*Central Bank*
February 2008	
4	Reserve Bank of Australia
7	European Central Bank
7	Bank of England
13	Bank of Sweden
14	Bank of Japan
15	Bank of Mexico
March 2008	
3	Reserve Bank of Australia
4	Bank of Canada
5	Reserve Bank of New Zealand
5	Bank of Brazil
6	European Central Bank
6	Bank of England
6	Bank of Japan
13	Bank of Norway
13	Swiss National Bank
14	Bank of Mexico
18	U.S. Federal Reserve
April 2008	
1	Reserve Bank of Australia
8	Bank of Japan
10	European Central Bank
10	Bank of England
16	Bank of Brazil
18	Bank of Mexico
22	Bank of Canada
23	Bank of Norway
23	Reserve Bank of New Zealand
23	Bank of Sweden
29	Bank of Japan

Source: Desjardins, Economic Studies