

March 4, 2008



BANK OF CANADA

Carney starts term off with a 50-point rate cut

ACCORDING TO THE BANK OF CANADA (BoC)

- The target for the overnight rate drops 50 basis points, from 4.00% to 3.50%.
- Domestic demand remains robust, with the rise in price of basic products and employment levels continuing to support the growth of income. Canadian net exports fell back again in the fourth quarter due to the slowing of the U.S. economy and the impact of earlier Canadian dollar appreciation.
- There are clear signs that the U.S. economic slowdown will be greater and longer than had been forecast. This situation is due to deterioration of the housing market, which is negatively impacting other sectors of the U.S. economy and contributing to additional tightening of credit conditions.
- Significant downward risks weighing on outlooks for growth of the Canadian economy are taking shape and—in some regards—intensifying.
- There has been a clear shift to the downside in the balance of risks around the Bank's January projection for inflation.
- The degree of monetary easing will probably have to be increased further in the near future.

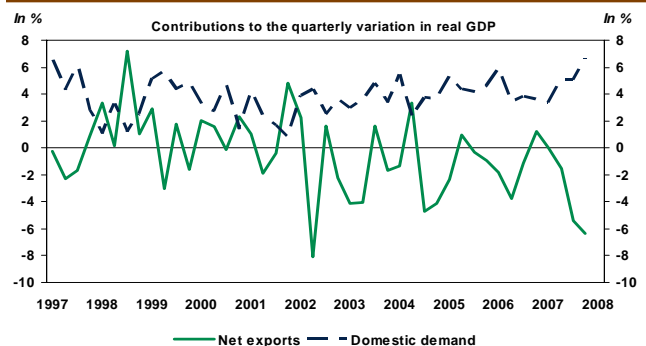
COMMENTS

Their terms succeeded—and resembled—each other. Just like David Dodge on March 6, 2001, Mark Carney lowered key interest rates by 50 basis points during his very first meeting as head of the Bank of Canada. However, the facts show that he had no real choice. Confronted by the increasing risks of a recession in the United States, the volatility of the financial markets, the tightening of credit conditions, the widening gap between key Canadian and U.S. rates and the upward pressure on the loonie, the pace of monetary easing in Canada had to pick up.

The most recent economic data is unequivocal: the Canadian economy has been greatly affected by the convergence of a strong currency and anaemic U.S. demand for products made in Canada. In the fourth quarter, the current account balance dropped into negative territory for the first time since 1999 and the marked drop in net exports sliced 6.7% off real GDP

growth. Canada was able to limit the damage due to the decade's highest growth in domestic demand (6.9%), but the pace seems unsustainable. The year 2007 closed on a fizzle, with a 0.7% drop in GDP per industry and disappointing results in retail sales (excluding automobiles), suggesting that the pace of consumer spending should dip in early 2008.

Canadian economy's external sector is hit by the U.S. slowdown and the loonie's strength



Sources: Statistics Canada and Desjardins, Economic Studies

Implications: The current deceleration of inflation will allow the BoC to pursue its monetary easing policy over the next few months. There is every reason to believe that the key rate could be less than 3.0% by June. Further deterioration of the U.S. economy, and its ricochet effect on the Canadian situation, could signify another 50 basis point drop as of the Bank's April meeting.

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

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**EXCERPT FROM THE BANK OF CANADA PRESS RELEASE
MARCH 4, 2008**


[...] Information received since the January *Monetary Policy Report Update (MPRU)* indicates that economic growth in Canada through the four quarters of 2007 was broadly in line with expectations. Domestic demand has remained buoyant, as rising commodity prices and high employment have continued to support income growth. Canada's net exports weakened further in the fourth quarter, reflecting the slowing U.S. economy and the impact of the past appreciation of the Canadian dollar. Overall, the Canadian economy remained above its production capacity at year-end. Core and total CPI inflation – at 1.4 per cent and 2.2 per cent, respectively, in January – have also been consistent with the Bank's expectations.

At the same time, there are clear signs that the U.S. economy is likely to experience a deeper and more prolonged slowdown than had been projected in January. This stems from further weakening in the residential housing market, which is adversely affecting other sectors of the U.S. economy and contributing to further tightening in credit conditions. The deterioration in economic and financial conditions in the United States can be expected to have significant spillover effects on the global economy. These developments suggest that important downside risks to Canada's economic outlook that were identified in the MPRU are materializing and, in some respects, intensifying.

The Bank now judges that the balance of risks around its January projection for inflation has clearly shifted to the downside, and, as a result, the Bank is lowering the target for the overnight rate. Further monetary stimulus is likely to be required in the near term to keep aggregate supply and demand in balance and to achieve the 2 per cent inflation target over the medium term. [...]

**Table 1
Schedule and key rates**

Date	Central Bank	Decision	Rate
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
February 2007			
4	Reserve Bank of Australia	+25 b.p.	7.00
7	European Central Bank	s.q.	4.00
7	Bank of England	-25 b.p.	5.25
13	Bank of Sweden	+25 b.p.	4.25
14	Bank of Japan	s.q.	0.50
15	Bank of Mexico	s.q.	7.50
March 2007			
3	Reserve Bank of Australia	+25 b.p.	7.25
4	Bank of Canada	-50 b.p.	3.50

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

**Table 2
Coming soon**

Date	Central Bank
March 2008	
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
30	U.S. Federal Reserve
May 2008	
6	Reserve Bank of Australia
8	European Central Bank
8	Bank of England
16	Bank of Mexico
19	Bank of Japan
28	Bank of Norway

Source: Desjardins, Economic Studies