

Essentials of the Monetary Policy

June 5, 2008



BANK OF ENGLAND



EUROPEAN CENTRAL BANK

Inflation fears notch up

BANK OF ENGLAND (BoE)

To no one's surprise, the BoE kept its key rate at 5.00% this morning. Inflation rose to 3.0% in April and the Inflation Report showed that Britain's monetary authorities now anticipate a more pronounced, sustainable surge by inflation by the end of 2008, taking away all of the BoE's short-term leeway. Yet the economic slowdown, already visible in Q1, seems to be intensifying; the latest statistics point to another drop by consumer confidence and decline by activity in the services sector, while housing is still correcting.

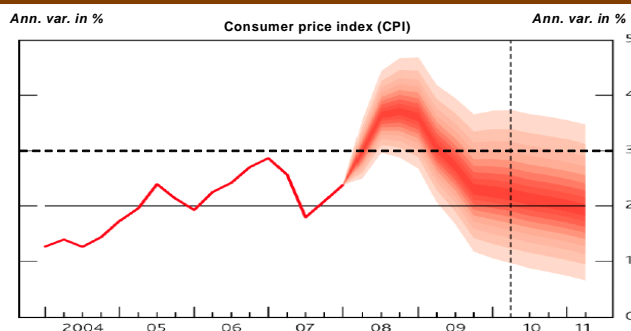
Implications: The BoE is well aware of the problems with the British economy, but it will have to put rate cuts on hold for several months to protect its credibility and keep a damper on inflation expectations. The magnitude of the economic slowdown should convince it to return to monetary easing as of the fall, however.

EUROPEAN CENTRAL BANK (ECB)

As forecast, the ECB kept its key rate at 4.00%. With oil prices persistently high, the ECB is concerned that inflation might impact wage negotiations and lead to an inflation spiral. Note that inflation is showing little sign of flagging. The flash estimate of total inflation picked up to 3.6% in May, well over the ECB's 2.0% ceiling. For now, elevated energy prices' pass-through to the rest of consumer prices is contained. But the risk that the increase in production costs will be passed along to consumers is not giving the ECB any reason to relax. It says it is in a state of heightened alertness.

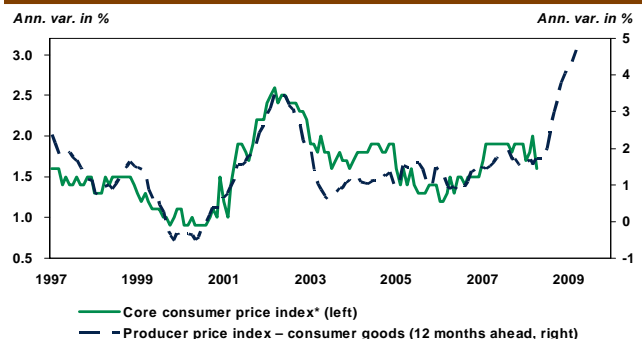
Implications: Given the persistence of inflation pressures, the next interest rate move is much more likely to be upward than downward. At the press conference that followed this morning's decision, Jean-Claude Trichet even said that an increase in rates as early as July was not out of the question.

The BoE expects inflation to remain over 3.0% until early 2009



Sources: Bank of England and Desjardins, Economic Studies

Rising production costs give rise to concern



* Excludes energy, food, alcohol and tobacco.
Sources: Datastream and Desjardins, Economic Studies

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

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**EXCERPT FROM THE EUROPEAN CENTRAL BANK PRESS RELEASE
 JUNE 5, 2008**


« [...] On the basis of our regular economic and monetary analyses, we decided at today's meeting to leave the key ECB interest rates unchanged. At the same time, we noted that risks to price stability over the medium term have increased further. Inflation rates have risen significantly since the autumn of last year, owing mainly to strong increases in energy and food prices. HICP inflation is now expected to remain high for a more protracted period than previously thought. Upside risks to price stability over the medium term are also confirmed by the continuing very vigorous money and credit growth and the absence of significant constraints on bank loan supply up to now. At the same time, the economic fundamentals of the euro area are sound. Against this background, we emphasise that maintaining price stability in the medium term is our primary objective in accordance with our mandate. The Governing Council is monitoring very closely all developments. It is in a state of heightened alertness. By acting in a firm and timely manner, we will prevent second-round effects and ensure that risks to price stability over the medium term do not materialise. It is our strong determination to secure a firm anchoring of medium and long-term inflation expectations in line with price stability. [...] »

**Table 1
 Schedule and key rates**

Date	Central Bank	Decision	Rate
March 2008			
13	Swiss National Bank	s.q.	2.75
14	Bank of Mexico	s.q.	7.50
18	U.S. Federal Reserve	-75 b.p.	2.25
10	Reserve Bank of Australia	s.q.	7.25
April 2008			
8	Bank of Japan	s.q.	0.50
10	Bank of England	-25 b.p.	5.00
10	European Central Bank	s.q.	4.00
16	Bank of Brazil	+50 b.p.	11.75
18	Bank of Mexico	s.q.	7.50
22	Bank of Canada	-50 b.p.	3.00
23	Bank of Norway	+25 b.p.	5.50
23	Reserve Bank of New Zealand	s.q.	8.25
23	Bank of Sweden	s.q.	4.25
29	Bank of Japan	s.q.	0.50
30	U.S. Federal Reserve	-25 b.p.	2.00
May 2008			
6	Reserve Bank of Australia	s.q.	7.25
8	Bank of England	s.q.	5.00
8	European Central Bank	s.q.	4.00
16	Bank of Mexico	s.q.	7.50
19	Bank of Japan	s.q.	0.50
28	Bank of Norway	s.q.	5.50
June 2008			
3	Reserve Bank of Australia	s.q.	7.25
4	Reserve Bank of New Zealand	s.q.	8.25
4	Bank of Brazil	+50 b.p.	12.25
5	Bank of England	s.q.	5.00
5	European Central Bank	s.q.	4.00

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

**Table 2
 Coming soon**

Date	Central Bank
June 2008	
10	Bank of Canada
12	Bank of Japan
19	Swiss National Bank
20	Bank of Mexico
25	Bank of Norway
25	U.S. Federal Reserve
July 2008	
1	Reserve Bank of Australia
3	European Central Bank
3	Bank of Sweden
10	Bank of England
14	Bank of Japan
15	Bank of Canada
18	Bank of Mexico
23	Reserve Bank of New Zealand
23	Bank of Brazil
August 2008	
5	Reserve Bank of Australia
5	U.S. Federal Reserve
7	Bank of England
13	Bank of Norway
15	Bank of Mexico
18	Bank of Japan
September 2008	
2	Reserve Bank of Australia
3	Bank of Canada
4	Bank of England
4	European Central Bank
10	Reserve Bank of New Zealand

Source: Desjardins, Economic Studies