

Essentials of the Monetary Policy



Desjardins
Economic Studies

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August 7, 2008



BANK OF ENGLAND



EUROPEAN CENTRAL BANK

Economic difficulties offset inflation's rise

BANK OF ENGLAND (BoE)

To no one's surprise, the BoE opted to keep its key rate at 5.00% this morning. The Bank's officials are still in a very difficult position. On one hand, the annual inflation rate (at 3.8% in June) could remain very high over the next few months. For another, the British economy's outlook is worsening steadily, to the point that a recession is becoming a real possibility. The latest statistics confirmed that May's spectacular rebound of retail sales was just an illusion—sales collapsed in June.

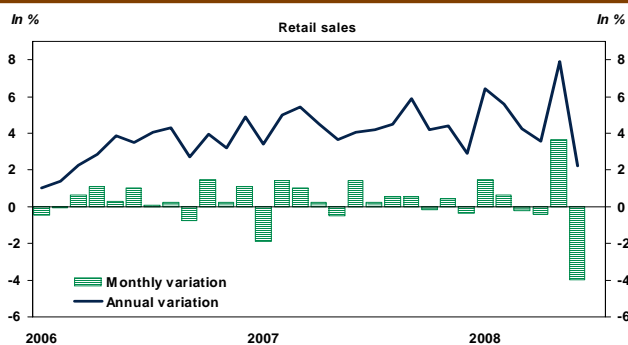
Implications: As usual, this morning's statement does not contain any new information. However, the quarterly Inflation Report, slated for release on August 13, and the minutes of today's meeting, to be published August 20, will provide a better understanding of the BoE's position. The latest developments, including the easing of commodity prices, support our projection that the BoE will relax its monetary policy this fall.

EUROPEAN CENTRAL BANK (ECB)

The ECB kept its key rate at 4.25% this morning, after having raised it 0.25% on July 3. It does not currently have a bias. The euro zone's annual inflation rate, which was 4% in June, should stay above the ECB's 2% target for quite a while, and the risks to price stability are still tilted to the upside. However, the Bank is starting to change its economic scenario, as it had only partially anticipated the disappointing statistics that have been released recently. It therefore judges that downside risks to growth are materializing.

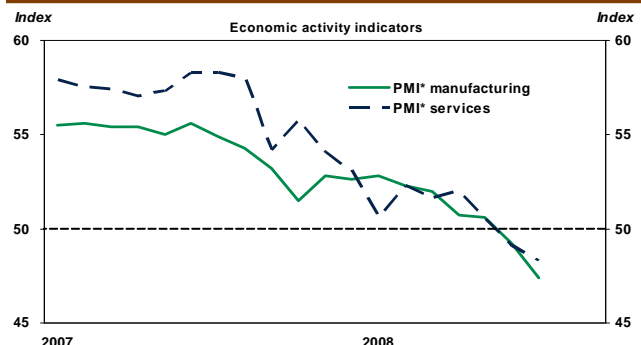
Implications: The ECB is still very concerned about surging inflation and continues to proclaim its determination to combat pass-through effects and rein in rising inflation expectations. However, the deterioration in the euro zone's economic situation and moderating commodities prices over the last few weeks tend to confirm that further rate hikes will not be needed. The ECB should keep its key rate stable for several months, then start to ease its monetary policy next year.

UK: Biggest one-month drop in retail sales ever recorded



Sources: Datastream and Desjardins, Economic Studies

Euro zone: The economy is slowing more sharply



* Purchasing Managers' Index.
* Sources: Bloomberg 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
AUGUST 7, 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. The information that has become available since our previous meeting has further underpinned the reasoning behind our decision to increase interest rates in July. It has confirmed that annual inflation rates are likely to remain well above levels consistent with price stability for a protracted period of time and that risks to price stability over the medium term remain on the upside. This assessment is underpinned by continued vigorous money growth, with so far no signs of significant constraints on bank loan supply. In such a context, it remains crucial to avoid broadly based second-round effects in wage and price-setting. The latest economic data point to a weakening of real GDP growth in mid-2008, which in part was expected after the exceptionally strong growth in the first quarter. Against this background and in full accordance with our mandate, we emphasise that maintaining price stability in the medium term is our primary objective and that it is our strong determination to keep medium and long-term inflation expectations firmly anchored in line with price stability. This will preserve purchasing power in the medium term and support sustainable growth and employment. On the basis of our assessment, the current monetary policy stance will contribute to achieving our objective. We will continue to monitor very closely all developments over the period ahead. [...]

**Table 1
Schedule and key rates**

| Date | Central Bank | Decision | Rate |
|--------------------|-----------------------------|----------|-------|
| May 2008 | | | |
| 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 |
| 10 | Bank of Canada | s.q. | 3.00 |
| 12 | Bank of Japan | s.q. | 0.50 |
| 19 | Swiss National Bank | s.q. | 2.75 |
| 20 | Bank of Mexico | +25 b.p. | 7.75 |
| 25 | Bank of Norway | +25 b.p. | 5.75 |
| 25 | Federal Reserve | s.q. | 2.00 |
| July 2008 | | | |
| 1 | Reserve Bank of Australia | s.q. | 7.25 |
| 3 | European Central Bank | +25 b.p. | 4.25 |
| 3 | Bank of Sweden | +25 b.p. | 4.50 |
| 10 | Bank of England | s.q. | 5.00 |
| 15 | Bank of Canada | s.q. | 3.00 |
| 15 | Bank of Japan | s.q. | 0.50 |
| 18 | Bank of Mexico | +25 b.p. | 8.00 |
| 23 | Reserve Bank of New Zealand | s.q. | 8.00 |
| 23 | Bank of Brazil | +75 b.p. | 13.00 |
| August 2008 | | | |
| 5 | Reserve Bank of Australia | s.q. | 7.25 |
| 5 | Federal Reserve | s.q. | 2.00 |
| 7 | Bank of England | s.q. | 5.00 |
| 7 | European Central Bank | s.q. | 4.25 |

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

**Table 2
Coming soon**

| Date | Central Bank |
|-----------------------|-----------------------------|
| August 2008 | |
| 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 |
| 4 | Bank of Sweden |
| 10 | Reserve Bank of New Zealand |
| 10 | Bank of Brazil |
| 16 | Bank of Japan |
| 16 | Federal Reserve |
| 18 | Swiss National Bank |
| 19 | Bank of Mexico |
| 24 | Bank of Norway |
| October 2008 | |
| 2 | European Central Bank |
| 6 | Bank of Japan |
| 7 | Reserve Bank of Australia |
| 9 | Bank of England |
| 17 | Bank of Mexico |
| 21 | Bank of Canada |
| 22 | Reserve Bank of New Zealand |
| 23 | Bank of Sweden |
| 29 | Bank of Norway |
| 29 | Bank of Brazil |
| 29 | Federal Reserve |
| 30 | Bank of Japan |

Source: Desjardins, Economic Studies