

Essentials of the Monetary Policy

October 8, 2008

CENTRAL BANKS

Central banks all lower key rates!

ACCORDING TO THE CENTRAL BANKS

- The Federal Reserve (Fed), the Bank of Canada (BoC), the European Central Bank (ECB), the Bank of England (BoE) and the Bank of Sweden have all cut their key rates by 50 basis points while the Swiss National Bank trimmed its rate by 25 basis points. Although it did not follow suit, the Bank of Japan came out in favour of this policy.

Banks	Previous Rate	New Rate
Canada	3.00%	2.50%
United States	2.00%	1.50%
Euro zone	4.25%	3.75%
United Kingdom	5.00%	4.50%
Sweden	4.75%	4.25%
Switzerland	2.75%	2.50%

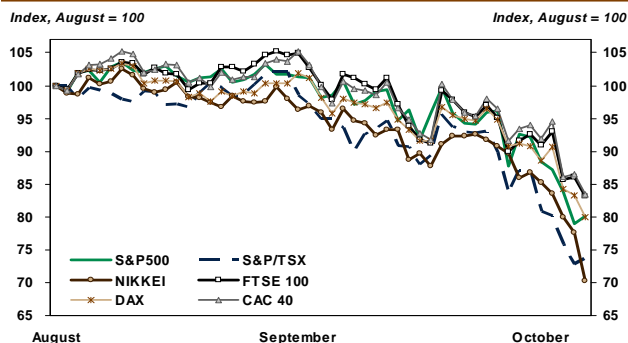
- The worsening financial crisis has augmented the downside risks to growth and further diminished the upside risks to price stability.
- The decrease in oil prices has eased inflationary pressures in many countries. Inflation expectations have also fallen.

COMMENTS

When you have a global crisis, you need a global solution. The central banks have finally decided to strike hard together by cutting their key rates. The credit market and the stock market turmoil that is sapping consumer confidence day after day are a major threat to the global economy. In fact, the Fed said that economic data suggests that the pace of economic activity has slowed markedly and the intensification of financial market turmoil is likely to exert additional restraint on spending. In Canada, the BoC stated that credit conditions have tightened substantially. All these activities, particularly those associated with credit availability, are what prompted this rare joint action. The last time this occurred was on September 17, 2001, when the U.S. markets reopened after 9/11.

Will this joint effort be enough to restore confidence in the markets? It's one more step in the right direction following the more direct action taken by the monetary authorities (injection of liquidity, bigger loans to banks and businesses) and to the government bailouts. The fact is that the financial

Stock market – Freefall prompts central banks to work together



Sources: Datastream and Desjardins, Economic Studies

markets were hoping for and even expecting this monetary easing. That said, credit conditions are still so tough that the stimulative effect of the rate cuts may be very minimal in the near term. Does this mean that these cuts are too little and too late?

Implications: The central banks have taken a big step. However, the easing may not be over for some of those that participated today. With rates at 1.50%, the U.S. does not have much latitude left but given the magnitude of their problems, further cuts are not impossible. In countries where rates are higher, more and bigger cuts are almost a given. The BoC may well shave another 75 b.p. off its key rate before the year is out, while the ECB and BoE are expected to announce major reductions at their next meetings. We can also expect more liquidity injections from the central banks and other government bailout plans.

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EXCERPT FROM THE JOINT STATEMENT BY CENTRAL BANKS

“Throughout the current financial crisis, central banks have engaged in continuous close consultation and have cooperated in unprecedented joint actions such as the provision of liquidity to reduce strains in financial markets.

Inflationary pressures have started to moderate in a number of countries, partly reflecting a marked decline in energy and other commodity prices. Inflation expectations are diminishing and remain anchored to price stability. The recent intensification of the financial crisis has augmented the downside risks to growth and thus has diminished further the upside risks to price stability.

Some easing of global monetary conditions is therefore warranted. Accordingly, the Bank of Canada, the Bank of England, the European Central Bank, the Federal Reserve, Sveriges Riksbank, and the Swiss National Bank are today announcing reductions in policy interest rates. The Bank of Japan expresses its strong support of these policy actions.”

**Table 1
Schedule and key rates**

Date	Central Bank	Decision	Rate
August 2008			
7	Bank of England	s.q.	5.00
7	European Central Bank	s.q.	4.25
13	Bank of Norway	s.q.	5.75
15	Bank of Mexico	+25 b.p.	8.25
18	Bank of Japan	s.q.	0.50
September 2008			
2	Reserve Bank of Australia	-25 b.p.	7.00
3	Bank of Canada	s.q.	3.00
4	Bank of England	s.q.	5.00
4	European Central Bank	s.q.	4.25
4	Bank of Sweden	+25 b.p.	4.75
12	Reserve Bank of New Zealand	-50 b.p.	7.50
19	Bank of Brazil	+75 b.p.	13.75
16	Bank of Japan	s.q.	0.50
20	Federal Reserve	s.q.	2.00
25	Swiss National Bank	s.q.	2.75
25	Bank of Mexico	s.q.	8.25
24	Bank of Norway	s.q.	5.75
October 2008			
2	European Central Bank	s.q.	4.25
6	Reserve Bank of Australia	-100 b.p.	6.00
6	Bank of Japan	s.q.	0.50
8	European Central Bank	-50 b.p.	3.75
8	Bank of England	-50 b.p.	4.50
8	Bank of Sweden	-50 b.p.	4.25
8	Bank of Canada	-50 b.p.	2.50
8	Swiss National Bank	-25 b.p.	2.50
8	Federal Reserve	-50 b.p.	1.50

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

**Table 2
Coming soon**

Date	Central Bank
October 2008	
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
November 2008	
3	Reserve Bank of Australia
6	Bank of England
6	European Central Bank
20	Bank of Japan
28	Bank of Mexico
December 2008	
1	Reserve Bank of Australia
3	Reserve Bank of New Zealand
4	Bank of England
4	European Central Bank
9	Bank of Canada
10	Bank of Brazil
11	Swiss National Bank
16	Federal Reserve
17	Bank of Sweden
18	Bank of Japan
January 2009	
8	Bank of England
15	European Central Bank
20	Bank of Canada

Source: Desjardins, Economic Studies