

BANK OF CANADA

The Bank announces a Canadian recession Key rate cut of 75 basis points

ACCORDING TO THE BANK OF CANADA (BoC)

- The target for the overnight rate is down 75 basis points to 1.50%.
- The outlook for the world economy has deteriorated significantly and the global recession will be broader and deeper than previously anticipated. Global financial markets remain severely strained.
- While Canada's economy evolved largely as expected during the summer and early autumn, it is now entering a recession as a result of the weakness in global economic activity.
- All of these factors imply a lower profile for core inflation than had been projected at the time of the last *Monetary Policy Report*, in October.
- Economic and financial developments will be monitored carefully to judge to what extent further monetary stimulus will be required to achieve the 2% inflation target over the medium term.

COMMENTS

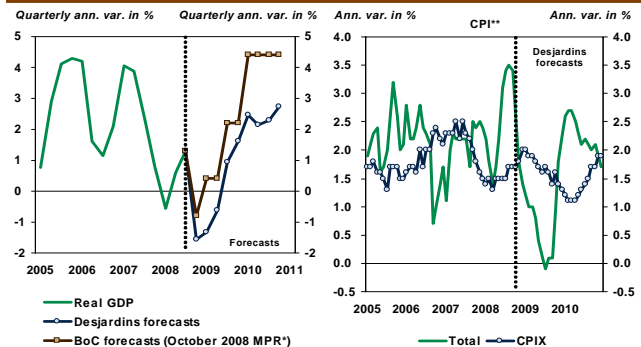
Against all expectations, uncertainty has prompted the BoC to accelerate its monetary policy easing, lowering its key rate by 75 basis points this morning. This takes the key rate cuts over the last three months to 150 basis points.

Most forecasters in the consensus had anticipated a 50 basis point cut, but the latest developments in the economic and financial situation prodded the BoC to be even more prudent. Clearly, due to the risks of a severe global recession, Canada will not avoid a contraction in its economic activity. Moreover, our own forecasts put real GDP growth in the red for three quarters, starting this quarter.

Under the circumstances, the gap between Canada's current production level and potential will continue to widen, which will result in reining in inflation pressure. November's deterioration of the labour market also leans in the direction of easing wage pressure.

With the marked downturn in oil prices (70% since mid-July), the BoC will have to substantially downgrade its inflation projections. In our view, the annual change in total inflation will likely stay below the BoC's target range (1% to 3%) until the fall of 2009, with a potential incursion below 0% in mid-2009.

The BoC will revise its outlook for growth and inflation downward



* Monetary Policy Report; ** Consumer price index.
Sources: Bank of Canada, Statistics Canada and Desjardins, Economic Studies

Implications: In our opinion, the risks are still broadly tilted to the downside. To cushion the Canadian recession's severity and get core inflation back into line with the mean target over the medium term, it seems very likely that more rate cuts will be ordered in the next few months. We are maintaining our scenario for a rate of 1% in the first half of 2009.

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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 BANK OF CANADA PRESS RELEASE


“[...] The outlook for the world economy has deteriorated significantly and the global recession will be broader and deeper than previously anticipated. Global financial markets remain severely strained. Measures taken by major governments are beginning to encourage credit flows, although it will take some time before conditions in financial markets normalize. In addition, a series of recently announced monetary and fiscal policy actions will also support global economic growth [...] While Canada’s economy evolved largely as expected during the summer and early autumn, it is now entering a recession as a result of the weakness in global economic activity. The recent declines in terms of trade, real income growth, and confidence are prompting more cautious behaviour by households and businesses [...] All of these factors imply a lower profile for core inflation than had been projected at the time of the last *Monetary Policy Report* in October [...] Several factors are helping to counterbalance the negative drag from the global economic and financial developments. The depreciation of the Canadian dollar will continue to provide an important offset to the effects of weaker global demand and lower commodity prices. As well, money markets and overall credit conditions in Canada are responding to significant and ongoing efforts to provide liquidity to the Canadian financial system [...] In light of the weakening outlook for growth and inflation, the Bank of Canada lowered its policy interest rate by a total of 75 basis points in October and by an additional 75 basis points today. These monetary policy actions provide timely and significant support to the Canadian economy [...] The Bank will continue to monitor carefully economic and financial developments in judging to what extent further monetary stimulus will be required to achieve the 2 per cent inflation target over the medium term. [...]”

**Table 1
Schedule and key rates**

Date	Central Bank	Decision	Rate
October 2008			
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
15	Bank of Norway	-50 b.p.	5.25
17	Bank of Mexico	s.q.	8.25
21	Bank of Canada	-25 b.p.	2.25
22	Reserve Bank of New Zealand	-100 b.p.	6.50
23	Bank of Sweden	-50 b.p.	3.75
29	Bank of Norway	-50 b.p.	4.75
29	Bank of Brazil	s.q.	13.75
29	Federal Reserve	-50 b.p.	1.00
30	Bank of Japan	-20 b.p.	0.30
November 2008			
3	Reserve Bank of Australia	-75 b.p.	5.25
6	Bank of England	-150 b.p.	3.00
6	European Central Bank	-50 b.p.	3.25
20	Bank of Japan	s.q.	0.30
28	Bank of Mexico	s.q.	8.25
December 2008			
1	Reserve Bank of Australia	-100 b.p.	4.25
3	Reserve Bank of New Zealand	-150 b.p.	5.00
4	Bank of England	-100 b.p.	2.00
4	European Central Bank	-75 b.p.	2.50
4	Bank of Sweden	-175 b.p.	2.00
9	Bank of Canada	-75 b.p.	1.50

**Table 2
Coming soon**

Date	Central Bank
December 2008	
10	Bank of Brazil
11	Swiss National Bank
16	Federal Reserve
17	Bank of Norway
18	Bank of Japan
January 2009	
8	Bank of England
15	European Central Bank
16	Bank of Mexico
20	Bank of Canada
21	Bank of Brazil
22	Bank of Japan
28	Federal Reserve
29	Reserve Bank of New Zealand
February 2009	
3	Reserve Bank of Australia
4	Bank of Norway
5	Bank of England
5	European Central Bank
10	Bank of Sweden
19	Bank of Japan
12	Bank of Mexico
March 2009	
3	Reserve Bank of Australia
3	Bank of Canada
5	Bank of England
5	European Central Bank
11	Bank of Brazil
12	Reserve Bank of New Zealand

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

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