

July 21, 2009



## BANK OF CANADA

### The tone is slightly more positive, but the Bank reiterates its conditional commitment to keep the key rate at 0.25% until mid-2010

#### ACCORDING TO THE BANK OF CANADA (BoC)

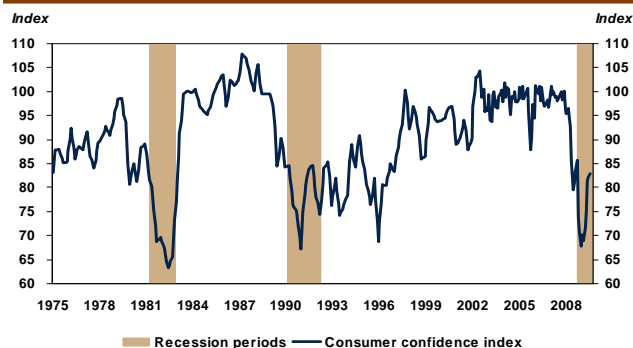
- The target for the overnight rate remains at 0.25%. Conditional on the outlook for inflation, the target overnight rate can be expected to remain at its current level until the end of the second quarter of 2010 in order to achieve the inflation target.
- There are now increasing signs that economic activity has begun to expand in many countries. However, the recovery is nascent. Effective and resolute policy implementation remains critical to sustained global growth.
- A number of factors are spurring domestic demand growth. However, the higher Canadian dollar, as well as ongoing restructuring in key industrial sectors, is significantly moderating the pace of overall growth. The BoC projects that the economy will contract by 2.3% in 2009 and then grow by 3.0% in 2010 and 3.5% in 2011.
- Inflation should trough in the third quarter of this year before returning to the 2% target in the second quarter of 2011. As a consequence of operating at the effective lower bound, the overall risks to its inflation projection are tilted slightly to the downside.

#### COMMENTS

It was clear that the BoC was not going to change its key rate this morning. It is interesting to note, however, that the BoC has taken a slightly more positive stance in its statement. According to the BoC, the economic recovery now seems imminent in both Canada and elsewhere in the world, although many obstacles remain.

In Canada, stimulative monetary and fiscal policies, improved financial conditions, firmer commodity prices and a rebound in business and consumer confidence are spurring domestic demand growth. The Canadian dollar's rise and specific difficulties in key industrial sectors are curbs to the Canadian economy's growth. Compared with April, the BoC has upgraded its growth outlook for Canada's GDP for 2009 and 2010, which is offset by moderating the strong growth forecast for 2011. The BoC's new economic forecasts will

#### Canadian consumer confidence has rebounded



Sources: Conference Board of Canada and Desjardins, Economic Studies

be set out in detail when its *Monetary Policy Report* is published on Thursday.

However, today's statement should not be construed as a signal that key rates will be raised shortly. The BoC judges that the economic recovery is nascent and that stimulative policy is still critical. Moreover, given the substantial excess supply in the economy, inflation could remain below the 2% target until mid-2011. The BoC also continues to think that the risks to this projection are slightly tilted to the downside.

**Implications:** The statement's tone and the BoC's new forecasts rule out the possibility of new non-traditional measures in Canada in the near term. The most likely scenario is still a Canadian key rate that is steady until mid-2010. However, if the economy recovers as strongly as the BoC is forecasting, the door could gradually be opened to slightly faster tightening of the monetary policy.

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**EXCERPT FROM THE BANK OF CANADA PRESS RELEASE**


“[...] There are now increasing signs that economic activity has begun to expand in many countries in response to monetary and fiscal policy stimulus and measures to stabilize the global financial system. However, the recovery is nascent. Effective and resolute policy implementation remains critical to sustained global growth [...] The dynamics of the recovery in Canada remain broadly consistent with the Bank’s medium-term outlook in its April *Monetary Policy Report* (MPR). Stimulative monetary and fiscal policies, improved financial conditions, firmer commodity prices, and a rebound in business and consumer confidence are spurring domestic demand growth. However, the higher Canadian dollar, as well as ongoing restructuring in key industrial sectors, is significantly moderating the pace of overall growth [...] Some of the early strength in domestic demand represents a bringing forward of household expenditures, which modestly alters the profile of growth over the projection period relative to the April MPR. The Bank projects that the economy will contract by 2.3 per cent in 2009 and then grow by 3.0 per cent in 2010 and 3.5 per cent in 2011, reaching production capacity in the middle of 2011 [...] Total CPI inflation declined to -0.3 per cent in June and should trough in the third quarter of this year before returning to the 2 per cent target in the second quarter of 2011 [...] While the underlying macroeconomic risks to the projection are roughly balanced, the Bank judges that, as a consequence of operating at the effective lower bound, the overall risks to its inflation projection are tilted slightly to the downside [...] Conditional on the outlook for inflation, the target overnight rate can be expected to remain at its current level until the end of the second quarter of 2010 in order to achieve the inflation target. Consistent with this conditional commitment [...].”

**Table 1  
Schedule and key rates**

Date	Central Bank	Decision	Rate
<b>April 2008</b>			
29	Federal Reserve	s.q.	0.00 / 0.25
<b>May 2008</b>			
5	Reserve Bank of Australia	s.q.	3.00
6	Bank of Norway	-50 b.p.	1.50
7	European Central Bank	-25 b.p.	1.00
7	Bank of England	s.q.	0.50
15	Bank of Mexico	-75 b.p.	5.25
21	Bank of Japan	s.q.	0.10
<b>June 2008</b>			
2	Reserve Bank of Australia	s.q.	3.00
4	European Central Bank	s.q.	1.00
4	Bank of England	s.q.	0.50
4	Bank of Canada	s.q.	0.25
10	Reserve Bank of New Zealand	s.q.	2.50
10	Bank of Brazil	-100 b.p.	9.25
15	Bank of Japan	s.q.	0.10
17	Bank of Norway	-25 b.p.	1.25
18	Swiss National Bank	s.q.	0.25
19	Bank of Mexico	-50 b.p.	4.75
24	Federal Reserve	s.q.	0.00 / 0.25
<b>July 2008</b>			
2	European Central Bank	s.q.	1.00
2	Bank of Sweden	-25 b.p.	0.25
7	Reserve Bank of Australia	s.q.	3.00
9	Bank of England	s.q.	0.50
14	Bank of Japan	s.q.	0.10
17	Bank of Mexico	-25 b.p.	4.50
21	Bank of Canada	s.q.	0.25

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

**Table 2  
Coming soon**

Date	Central Bank
<b>July 2009</b>	
22	Bank of Brazil
29	Reserve Bank of New Zealand
<b>August 2009</b>	
4	Reserve Bank of Australia
6	European Central Bank
6	Bank of England
10	Bank of Japan
12	Bank of Norway
12	Federal Reserve
21	Bank of Mexico
<b>September 2009</b>	
1	Reserve Bank of Australia
2	Bank of Brazil
3	European Central Bank
9	Reserve Bank of New Zealand
9	Bank of Sweden
10	Bank of England
10	Bank of Canada
16	Bank of Japan
17	Swiss National Bank
18	Bank of Mexico
23	Bank of Norway
23	Federal Reserve
<b>October 2009</b>	
6	Reserve Bank of Australia
8	European Central Bank
8	Bank of England
13	Bank of Japan
16	Bank of Mexico

Source: Desjardins, Economic Studies