



BANK OF ENGLAND

Quantitative measures expand slightly

ACCORDING TO THE BANK OF ENGLAND (BoE)

- The official Bank Rate paid on commercial bank reserves remains steady at 0.50%. The asset purchase program financed by the issuance of central bank reserves is extended by £25B to £200B (US\$330B).
- In the United Kingdom, activity has contracted by almost 6% since the beginning of 2008. GDP continued to fall in the third quarter. A number of indicators, however, suggest that a pickup in economic activity may soon be evident.
- At 1.1% in September, the inflation rate should shoot above the 2% target in the near term, reflecting higher petrol price inflation and the reversal of last year's reduction in VAT.
- The Monetary Policy Committee is expecting the economy to post a slow recovery and continue to show a substantial margin of under-utilised resources. This will put downside pressure on inflation over the medium range.

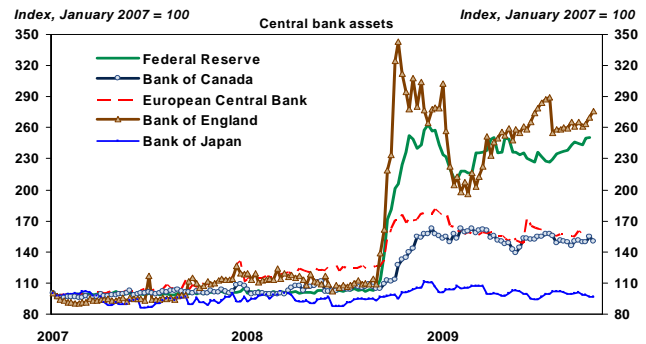
COMMENTS

The financial markets had been eagerly awaiting November's Bank of England meeting. There was no doubt that the key rate would stay at 0.50%. However, as the £175B asset purchase program was completed, a decision as to whether or not to further expand the quantitative easing measures could no longer be put off. The £25B increase in the purchase program is smaller than a slight majority of analysts had expected.

BoE leaders did not have an easy decision on their hands. On one hand, the global economy is showing clear signs of recovery and conditions in the financial markets have shown substantial improvement in the last few months. Britain's economy still has its difficulties, but the quick comeback by home prices in the recent months could have prompted the BoE to take its foot off the gas. By several yardsticks, the BoE can already boast of having been the central bank that took the most muscled action since the financial crisis broke.

However, there were other arguments in favour of expanding the quantitative measures. Following the British economy's annualized 1.6% contraction in the third quarter, the U.K.'s output gap widened even further. Even if it does end shortly,

Before this morning's decision, the Bank of England was already the bank that had taken the most action since the crisis began



Sources: Statistics Canada, Federal Reserve, Bank of Japan, European Central Bank, Bank of England and Desjardins, Economic Studies

this recession is one of the most severe to have ever hit Britain's economy. Beyond short-term movements by inflation, everything thus suggests that inflation pressure will remain very subdued over the medium term. The BoE may also have factored in fiscal policies that could quickly become much less favourable to growth. The consumption tax should go up 2.5 percentage points at the beginning of 2010 and many politicians are arguing for substantial cuts to public spending.

Implications: The BoE made a reasonable decision when it increased its quantitative measures moderately this morning. It will be interesting to find out from the minutes whether all of the committee members rallied behind this decision. The key rate will stay where it is until at least mid-2010, as in the euro zone, where the ECB once again opted for the status quo this morning.

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EXCERPT FROM THE BANK OF ENGLAND PRESS RELEASE


« The Bank of England's Monetary Policy Committee today voted to maintain the official Bank Rate paid on commercial bank reserves at 0.5%. The Committee also voted to continue with its programme of asset purchases financed by the issuance of central bank reserves and to increase its size by £25 billion to £200 billion.

The world economy has shown signs of recovery, with a number of emerging market economies experiencing a strong rebound in growth, although global activity as a whole remains significantly depressed. [...]

In the United Kingdom, output has fallen by almost 6% since the start of 2008. Households have reduced their spending substantially and business investment has fallen especially sharply. GDP continued to fall in the third quarter. A number of indicators of spending and confidence, however, suggest that a pickup in economic activity may soon be evident.

CPI inflation fell to 1.1% in September, having been 5.2% a year earlier. Inflation is likely to rise sharply to above the 2% target in the near term, reflecting higher petrol price inflation and the reversal of last year's reduction in VAT.

[...] On balance, the Committee believes that the prospect is for a slow recovery in the level of economic activity, so that a substantial margin of under-utilised resources persists. That will continue to bear down on inflation for some time to come, offset in the short run by the impact of the past depreciation of sterling. [...] »

**Table 1
Schedule and key rates**

Date	Central Bank	Decision	Rate
September 2008			
2	Bank of Brazil	s.q.	8.75
3	European Central Bank	s.q.	1.00
3	Bank of Sweden	s.q.	0.25
9	Reserve Bank of New Zealand	s.q.	2.50
10	Bank of England	s.q.	0.50
10	Bank of Canada	s.q.	0.25
16	Bank of Japan	s.q.	0.10
17	Swiss National Bank	s.q.	0.25
18	Bank of Mexico	s.q.	4.50
23	Bank of Norway	s.q.	1.25
23	Federal Reserve	s.q.	0.00 / 0.25
October 2008			
5	Reserve Bank of Australia	+25 b.p.	3.25
8	European Central Bank	s.q.	1.00
8	Bank of England	s.q.	0.50
13	Bank of Japan	s.q.	0.10
16	Bank of Mexico	s.q.	4.50
20	Bank of Canada	s.q.	0.25
21	Bank of Brazil	s.q.	8.75
22	Bank of Sweden	s.q.	0.25
28	Bank of Norway	+25 b.p.	1.50
28	Reserve Bank of New Zealand	s.q.	2.50
29	Bank of Japan	s.q.	0.10
November 2008			
2	Reserve Bank of Australia	+25 b.p.	3.50
4	Federal Reserve	s.q.	0.00 / 0.25
5	European Central Bank	s.q.	1.00
5	Bank of England	s.q.	0.50

**Table 2
Coming soon**

Date	Central Bank
November 2009	
19	Bank of Japan
27	Bank of Mexico
30	Reserve Bank of Australia
December 2009	
3	European Central Bank
8	Bank of Canada
9	Reserve Bank of New Zealand
9	Bank of Brazil
10	Bank of England
10	Swiss National Bank
16	Bank of Norway
16	Bank of Sweden
16	Federal Reserve
17	Bank of Japan
January 2010	
7	Bank of England
14	European Central Bank
19	Bank of Canada
25	Bank of Japan
27	Reserve Bank of New Zealand
27	Bank of Brazil
27	Federal Reserve
February 2010	
2	Reserve Bank of Australia
3	Bank of Norway
4	European Central Bank
4	Bank of England
10	Bank of Sweden
17	Bank of Japan

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

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