The Bank of Canada keeps key lending rates unchanged

- The overnight funds rate and bank rate stay put, at 2.75% and 3.00%, respectively.
- Consequently, the prime rate of the Caisse centrale Desjardins and the major Canadian banks will remain at 4.50%.

1) The Bank continues to predict that Canadian economic growth will outpace its potential rate beginning in late 2003.
2) However, the recent appreciation in the Canadian dollar was stronger than expected.
3) A speedier global demand, especially in the United States, should drive our exports, but a rise in the loonie will curb their growth.
4) Furthermore, a number of uncertainties surround the timing and magnitude of ongoing global demand, inflation and exchange rate adjustments in reaction to worldwide economic imbalances.

Excerpts from the BoC Press Release:

[...] Since the Bank lowered policy interest rates on 3 September, indicators of economic activity and inflation in Canada have evolved broadly in line with the Bank’s expectations. Core inflation has remained below the Bank’s 2 per cent inflation target. As well, there has been evidence of gathering economic strength, including firm growth in final domestic demand and positive signs of recovery in the U.S. and overseas economies. Over this period, however, the value of the U.S. dollar has depreciated more than was generally expected against some major currencies, including the Canadian dollar. Taking all these developments into account, the Bank has decided to leave its policy interest rates unchanged at this time.

Looking forward, the Bank continues to expect growth in the Canadian economy to strengthen during the fourth quarter of 2003 and through 2004. On balance, this expansion should be above the rate of potential growth, supported by solid household spending and increased business investment. Stronger economic growth abroad should also boost foreign demand for Canadian goods and services, although this source of strength will be tempered by the higher value of the Canadian dollar. More broadly, there are uncertainties related to the timing and magnitude of ongoing global demand, price, and exchange rate adjustments to economic imbalances. The Bank will closely monitor and assess the implications of these global adjustments for demand and inflation in Canada. An elaboration of the Bank’s views on the economy and the outlook for inflation will be provided in the Monetary Policy Report to be released on 22 October 2003. […]

Conclusion: As expected, the Bank of Canada opted today for the status quo. This means that, despite the recent rally of the Canadian dollar, the Canadian monetary authorities are still banking on an acceleration in economic growth over the quarters ahead. We will learn more in the updated forecasts of the Bank of Canada on economic growth and inflation in next week’s publication of its semi-annual Monetary Policy Report. Nevertheless, its discourse is much less categorical in today’s press release than it was in the release dated September 3rd last. In particular, our central bank clearly indicated that a number of uncertainties are still looming over our economy, including the trend in prices and the exchange rate. According to our most recent scenario, the recent upsurge of the loonie should be short-lived. A slight devaluation in our currency is even possible by the end of the year. Given this context, the Bank of Canada is expected to leave its key lending rates unchanged at its upcoming meeting on December 2nd. However, the possibility of a rate cut should the loonie rise too much and too quickly, in addition to an exacerbation of global imbalances, in particular a degradation in the US current account deficit, cannot be entirely dismissed.

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The US dollar is still following a downward trend

Source: Federal Reserve of Atlanta and Desjardins Economic Studies

The US are expecting foreign financing

Source: International Monetary Fund (IMF)

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