

BANK OF CANADA

Key interest rates ultimately remain unchanged Despite uncertainties, the BoC is fairly confident

ACCORDING TO THE BANK OF CANADA (BoC)

- The target for the overnight rate stays at 0.50%.
- The dynamics of the global economy are broadly as anticipated in the Bank's October *Monetary Policy Report* (MPR), with diverging economic prospects and shifting terms of trade. China continues its transition to a more sustainable growth path and the expansion in the United States is on track, despite temporary weakness in the fourth quarter of 2015.
- Prices for oil and other commodities have declined further and this represents a setback for the Canadian economy. GDP growth likely stalled in the fourth quarter of 2015, pulled down by temporary softness in the U.S. economy, weaker business investment and several other temporary factors.
- The Bank now expects the economy's return to above-potential growth to be delayed until the second quarter of 2016. The protracted process of reorientation towards non-resource activity is underway, helped by stronger U.S. demand, the lower Canadian dollar, and accommodative monetary and financial conditions.
- The Bank projects Canada's economy will grow by 1.4% in 2016 and 2.4% in 2017. The complex nature of the ongoing structural adjustment makes the outlook for demand and potential output highly uncertain.
- The Bank expects inflation will rise to about 2% by early 2017.

COMMENTS

While nearly half of forecasters expected a new decrease in key rates, the Bank of Canada ultimately opted for the status quo, a decision consistent with our forecast. Further, the statement and the *Monetary Policy Report* that accompanied the Bank's decision are fairly reassuring overall.

The authorities nonetheless note that uncertainties abound, particularly with oil prices declining sharply in recent weeks. According to the BoC, a sustained drop in energy

prices could even drive certain businesses to cease activities, thereby impacting production, investment and employment. In contrast to the looming uncertainty, monetary authorities have not yet factored in the positive impact of additional budgetary recovery measures in their economic forecasts.

Ultimately, the BoC is confident that the adjustments the Canadian economy is experiencing will gradually continue in the coming quarters. In addition, the vitality of U.S. demand and the depreciation of the loonie should continue to be a boon to non-energy sectors. Following almost no growth in real GDP in the fourth quarter of 2015, the BoC forecasts that economic growth will accelerate, particularly as of the second quarter of 2016. Accordingly, monetary authorities expect Canadian real GDP to increase 2.4% in 2017. This projection is higher than the consensus forecast (2.2%) and our most recent forecast (1.8%), attesting to some optimism among BoC leaders.

Implications: While uncertainties abound, the *Monetary Policy Report* is fairly reassuring. Under these conditions, it is likely that the BoC will stay the course in the coming months and leave the target for the overnight rate at 0.50%. That said, the possibility of another reduction in key rates in the spring cannot be ruled out should oil prices continue to fall, should Canadian output be further impacted by difficulties in the energy sector or should the recovery in non-energy exports become lacklustre.

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Schedule 2016 of Central Bank meetings

	<u>Decision</u>	<u>Rate</u>		<u>Decision</u>	<u>Rate</u>
JANUARY			JULY		
14	Bank of England	s.q.	0.50	4-5	Bank of Sweden
14	Bank of Korea	s.q.	1.50	5	Reserve Bank of Australia
20	Bank of Brazil			13	Bank of Canada
20	Bank of Canada	s.q.	0.50	14	Bank of England
21	European Central Bank			14	Bank of Korea
27	Federal Reserve			20	Bank of Brazil
28	Reserve Bank of New Zealand			21	European Central Bank
28-29	Bank of Japan			27	Federal Reserve
FEBRUARY			28-29 Bank of Japan		
1	Reserve Bank of Australia			AUGUST	
4	Bank of England			2	Reserve Bank of Australia
4	Bank of Mexico			4	Bank of England
10-11	Bank of Sweden			11	Bank of Korea
16	Bank of Korea			11	Reserve Bank of New Zealand
29	Reserve Bank of Australia			11	Bank of Mexico
MARCH			31 Bank of Brazil		
2	Bank of Brazil			SEPTEMBER	
9	Bank of Canada			6	Reserve Bank of Australia
10	European Central Bank			7	Bank of Canada
10	Bank of Korea			8	European Central Bank
10	Reserve Bank of New Zealand			9	Bank of Korea
14-15	Bank of Japan			15	Bank of England
16	Federal Reserve			15	Swiss National Bank
17	Bank of England			20-21	Bank of Japan
17	Bank of Norway			21	Federal Reserve
17	Swiss National Bank			22	Bank of Norway
18	Bank of Mexico			22	Reserve Bank of New Zealand
APRIL			29 Bank of Mexico		
5	Reserve Bank of Australia			*	Bank of Sweden
13	Bank of Canada			OCTOBER	
14	Bank of England			3	Reserve Bank of Australia
19	Bank of Korea			13	Bank of England
20-21	Bank of Sweden			13	Bank of Korea
21	European Central Bank			19	Bank of Brazil
27	Bank of Brazil			19	Bank of Canada
27	Federal Reserve			20	European Central Bank
27-28	Bank of Japan			27	Bank of Norway
28	Reserve Bank of New Zealand			31	Reserve Bank of Australia
MAY			31-1 Bank of Japan		
3	Reserve Bank of Australia			*	Bank of Sweden
5	Bank of Mexico			NOVEMBER	
12	Bank of England			2	Federal Reserve
12	Bank of Norway			3	Bank of England
13	Bank of Korea			10	Reserve Bank of New Zealand
25	Bank of Canada			11	Bank of Korea
JUNE			17 Bank of Mexico		
2	European Central Bank			30	Bank of Brazil
7	Reserve Bank of Australia			DECEMBER	
8	Bank of Brazil			5	Reserve Bank of Australia
9	Bank of Korea			7	Bank of Canada
9	Reserve Bank of New Zealand			8	European Central Bank
15	Federal Reserve			14	Federal Reserve
15-16	Bank of Japan			15	Bank of England
16	Bank of England			15	Bank of Korea
16	Swiss National Bank			15	Bank of Norway
23	Bank of Norway			15	Bank of Mexico
30	Bank of Mexico			15	Swiss National Bank

NOTE: Certain banks may decide to change rates in-between the scheduled meetings. The abbreviations s.q. and b.p. correspond to status quo and basis points respectively. * To be determined.