

August 4, 2016

BANK OF ENGLAND

The BoE adopts several measures to support the British economy

ACCORDING TO THE BANK OF ENGLAND (BoE)

- Following the United Kingdom's vote to leave the European Union, the outlook for growth in the short to medium term has weakened markedly.
- The fall in sterling is likely to push up on CPI inflation in the near term, hastening its return to the 2% target and probably causing it to rise above the target in the latter part of the forecast period.
- The reference key interest rate (Bank Rate) is reduced by 25 basis points to 0.25%. A majority of the members of the Monetary Policy Committee (MPC) expect to support a further cut in Bank Rate to its effective lower bound during the course of the year. The MPC currently judges this bound to be close to, but a little above, zero.
- The BoE is launching a Term Funding Scheme (TFS) that will provide funding for banks at interest rates close to Bank Rate.
- The BoE will increase the stock of purchased U.K. government bonds by £60B, to £435B.
- The BoE will purchase up to £10B of sterling non-financial investment-grade corporate bonds.

COMMENTS

The BoE surprised markets during its July meeting by announcing no change to its monetary policy despite the win of the Brexit option. However, it clearly signalled that some easing would be announced at the next meeting. The BoE delivered the goods today, by announcing a series of measures to support the British economy, which will have to make some difficult adjustments and face increased uncertainty.

Before the meeting, the vast majority of analysts forecast a 0.25% decrease in the principal key British rate. An £50B increase in the purchase of British bonds also seemed likely. On these two points, there was not much surprise: the BoE cut the Bank Rate by 0.25% and increased its government bond purchases by £60B. Yet it went even further by also announcing the purchase of corporate bonds and the

implementation of the TFS to provide liquidity to financial institutions.

The TFS announcement is particularly interesting. Its primary objective is to ensure that the cut in key rates is passed on to households and businesses. By directly offering liquidity to financial institutions at a rate close to the Bank Rate, the BoE expects retail rates to follow the movement in key rates. This program also provides an additional source of funding for British financial institutions. The measure will be financed by the issuance of central bank reserves, which will inflate the BoE's balance sheet. We also note that the Financial Policy Committee announced some regulatory easing, which should also support the credit offering by financial institutions.

All the measures announced this morning will not be enough to fully offset the negative effects of Brexit. In May, the BoE was predicting real GDP growth of 2.3% for 2017 and 2018, it now expects just 0.8% growth for next year, and 1.8% in 2018. The unemployment rate should go from 4.9% to around 5.5% in the coming years. These forecasts suggest a recession will be avoided, however.

Implications: Despite upside pressure on inflation resulting from a falling pound, the BoE decided to do everything in its power to support the British economy. It also stated that all the measures announced today could be increased if necessary. One last cut in key rates seems particularly likely, but for now, the BoE does not seem to be considering negative rates. The BoE's aggressive actions suggest that the pound will remain very weak, but they will support the value of other British assets. Theresa May's new government could also announce supporting budget measures in the fall.

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Schedule 2016 of Central Bank meetings

	<u>Decision</u>	<u>Rate</u>		<u>Decision</u>	<u>Rate</u>		
JANUARY			JULY				
13	Bank of Korea	s.q.	1.50	5	Reserve Bank of Australia	s.q.	1.75
14	Bank of England	s.q.	0.50	6	Bank of Sweden	s.q.	-0.50
20	Bank of Brazil	s.q.	14.25	13	Bank of Korea	s.q.	1.25
20	Bank of Canada	s.q.	0.50	13	Bank of Canada	s.q.	0.50
21	European Central Bank	s.q.	0.05	14	Bank of England	s.q.	0.50
27	Federal Reserve	s.q.	0.50	20	Bank of Brazil	s.q.	14.25
28	Reserve Bank of New Zealand	s.q.	2.50	21	European Central Bank	s.q.	0.00
29	Bank of Japan	s.q.	-0.10	27	Federal Reserve	s.q.	0.50
FEBRUARY			AUGUST				
1	Reserve Bank of Australia	s.q.	2.00	2	Reserve Bank of Australia	-25 b.p.	1.50
4	Bank of England	s.q.	0.50	4	Bank of England	-25 b.p.	0.25
4	Bank of Mexico	s.q.	3.25	10	Bank of Korea		
11	Bank of Sweden	-15 b.p.	-0.50	10	Reserve Bank of New Zealand		
15	Bank of Korea	s.q.	1.50	11	Bank of Mexico		
17	Bank of Mexico	+50 b.p.	3.75	31	Bank of Brazil		
29	Reserve Bank of Australia	s.q.	2.00	SEPTEMBER			
MARCH			OCTOBER				
2	Bank of Brazil	s.q.	14.25	6	Reserve Bank of Australia		
9	Bank of Korea	s.q.	1.50	7	Bank of Sweden		
9	Reserve Bank of New Zealand	-25 b.p.	2.25	7	Bank of Canada		
9	Bank of Canada	s.q.	0.50	8	European Central Bank		
10	European Central Bank	-5 b.p.	0.00	8	Bank of Korea		
14	Bank of Japan	s.q.	-0.10	15	Bank of England		
16	Federal Reserve	s.q.	0.50	15	Swiss National Bank		
17	Bank of England	s.q.	0.50	20	Bank of Japan		
17	Bank of Norway	-25 b.p.	0.50	21	Reserve Bank of New Zealand		
17	Swiss National Bank	s.q.	-0.75	21	Federal Reserve		
18	Bank of Mexico	s.q.	3.75	22	Bank of Norway		
APRIL			NOVEMBER				
5	Reserve Bank of Australia	s.q.	2.00	3	Reserve Bank of Australia		
13	Bank of Canada	s.q.	0.50	12	Bank of Korea		
14	Bank of England	s.q.	0.50	13	Bank of England		
18	Bank of Korea	s.q.	1.50	19	Bank of Brazil		
21	European Central Bank	s.q.	0.00	19	Bank of Canada		
21	Bank of Sweden	s.q.	-0.50	20	European Central Bank		
27	Reserve Bank of New Zealand	s.q.	2.25	27	Bank of Norway		
27	Bank of Brazil	s.q.	14.25	27	Bank of Sweden		
27	Bank of Japan	s.q.	-0.10	31	Reserve Bank of Australia		
27	Federal Reserve	s.q.	0.50	31	Bank of Japan		
MAY			DECEMBER				
3	Reserve Bank of Australia	-25 b.p.	1.75	5	Reserve Bank of Australia		
5	Bank of Mexico	s.q.	3.75	7	Bank of Canada		
12	Bank of England	s.q.	0.50	8	European Central Bank		
12	Bank of Korea	s.q.	1.50	14	Bank of Korea		
12	Bank of Norway	s.q.	0.50	14	Federal Reserve		
25	Bank of Canada	s.q.	0.50	15	Bank of England		
JUNE			NOVEMBER				
2	European Central Bank	s.q.	0.00	2	Federal Reserve		
7	Reserve Bank of Australia	s.q.	1.75	3	Bank of England		
8	Bank of Korea	-25 b.p.	1.25	9	Reserve Bank of New Zealand		
8	Reserve Bank of New Zealand	s.q.	2.25	10	Bank of Korea		
8	Bank of Brazil	s.q.	14.25	17	Bank of Mexico		
15	Bank of Japan	s.q.	-0.10	30	Bank of Brazil		
15	Federal Reserve	s.q.	0.50	DECEMBER			
16	Bank of England	s.q.	0.50	5	Reserve Bank of Australia		
16	Swiss National Bank	s.q.	-0.75	7	Bank of Canada		
23	Bank of Norway	s.q.	0.50	8	European Central Bank		
30	Bank of Mexico	+50 b.p.	4.25	14	Bank of Korea		
				14	Federal Reserve		
				15	Bank of England		
				15	Bank of Norway		
				15	Bank of Mexico		
				15	Swiss National Bank		
				19	Bank of Japan		
				21	Bank of Sweden		

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.