

ESSENTIALS OF THE MONETARY POLICY

Bank of Canada (BoC)

Liftoff Begins

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ACCORDING TO THE BOC

- ▶ The BoC announced today an increase in the target overnight rate from 0.25% to 0.50%.
- ▶ The BoC is continuing its reinvestment phase, keeping its overall holdings of Government of Canada bonds on its balance sheet roughly constant until such time as it becomes appropriate to allow the size of its balance sheet to decline.
- ▶ The unprovoked invasion of Ukraine by Russia is a major new source of uncertainty. Prices for oil and other commodities have risen sharply. This will add to inflation around the world, and negative impacts on confidence and new supply disruptions could weigh on global growth. Financial market volatility has increased.
- ▶ Global economic data has come in broadly in line with projections in the BoC's January *Monetary Policy Report*. Economies are emerging from the impact of the Omicron variant of COVID-19 more quickly than expected, although the virus continues to circulate and the possibility of new variants remains a concern.
- ▶ Economic growth in Canada was very strong in the fourth quarter of last year at 6.7%. This is stronger than the BoC's projection and confirms its view that economic slack has been absorbed. Overall, first-quarter growth is now looking more solid than previously projected.
- ▶ [...] inflation is now expected to be higher in the near term than projected in January. Persistently elevated inflation is increasing the risk that longer-run inflation expectations could drift upwards.
- ▶ As the economy continues to expand and inflation pressures remain elevated, the Governing Council expects interest rates will need to rise further.

COMMENTS

Today's interest rate hike was widely expected. The target for the overnight rate has been at its effective lower bound of 0.25% since the start of the pandemic in March 2020, and it was becoming increasingly difficult to justify that degree of monetary easing. The economic recovery is well underway, with real GDP surpassing its pre-pandemic level last fall. Inflation has been picking up speed since early last year. The consumer price index rose 5.1% on a year-over-year basis in January, well above the 3% upper limit of the BoC's target range.

But there's still a lot of uncertainty. As the BoC mentioned in its statement, disruptions from the crisis in Ukraine could further drive up inflation. High household debt means Canadians could be especially sensitive to interest rate hikes, though how much is unclear. And of course there's a chance a new variant will emerge, triggering additional rounds of public health measures. Add it all up, and it's likely the BoC will take a gradual approach to monetary tightening.

IMPLICATIONS

The BoC will need to make additional rate hikes over the coming months to normalize monetary policy and bring inflation down to the 1% to 3% range. It will look to increase the target for the overnight rate to what it considers a neutral level—between 1.75% and 2.75%. Based on our projections, it may take until late next year to hit that target. In the meantime, the BoC will also need to start reducing its holdings of Government of Canada bonds, which will further tighten monetary conditions.

Schedule 2022 of Central Bank Meetings

Date	Central banks	Decision	Rate
January			
13	Bank of Korea	+25 b.p.	1.25
17	Bank of Japan	s.q.	-0.10
20	Bank of Norway	s.q.	0.50
26	Bank of Canada*	s.q.	0.25
26	Federal Reserve	s.q.	0.25
31	Reserve Bank of Australia	s.q.	0.10
February			
2	Bank of Brazil	+150 b.p.	10.75
3	European Central Bank	s.q.	0.00
3	Bank of England	+25 b.p.	0.50
10	Bank of Sweden	s.q.	0.00
10	Bank of Mexico	+50 b.p.	6.00
22	Reserve Bank of New Zealand	+25 b.p.	1.00
23	Bank of Korea	s.q.	1.25
28	Reserve Bank of Australia	s.q.	0.10
March			
2	Bank of Canada	+25 b.p.	0.50
10	European Central Bank		
16	Bank of Brazil		
16	Federal Reserve		
17	Bank of England		
17	Bank of Japan		
24	Bank of Norway		
24	Bank of Mexico		
**	Swiss National Bank		
April			
5	Reserve Bank of Australia		
12	Reserve Bank of New Zealand		
13	Bank of Korea		
13	Bank of Canada*		
14	European Central Bank		
27	Bank of Japan		
28	Bank of Sweden		
May			
3	Reserve Bank of Australia		
4	Bank of Brazil		
4	Federal Reserve		
5	Bank of England		
5	Bank of Norway		
12	Bank of Mexico		
24	Reserve Bank of New Zealand		
25	Bank of Korea		
June			
1	Bank of Canada		
7	Reserve Bank of Australia		
9	European Central Bank		
15	Bank of Brazil		
15	Federal Reserve		
16	Bank of England		
16	Bank of Japan		
23	Bank of Norway		
23	Bank of Mexico		
30	Bank of Sweden		
**	Swiss National Bank		

Date	Central banks	Decision	Rate
July			
5	Reserve Bank of Australia		
12	Reserve Bank of New Zealand		
13	Bank of Korea		
13	Bank of Canada*		
20	Bank of Japan		
21	European Central Bank		
27	Federal Reserve		
August			
2	Reserve Bank of Australia		
3	Bank of Brazil		
4	Bank of England		
11	Bank of Mexico		
16	Reserve Bank of New Zealand		
18	Bank of Norway		
24	Bank of Korea		
September			
6	Reserve Bank of Australia		
7	Bank of Canada		
8	European Central Bank		
15	Bank of England		
20	Bank of Sweden		
21	Bank of Brazil		
21	Bank of Japan		
21	Federal Reserve		
22	Bank of Norway		
29	Bank of Mexico		
**	Swiss National Bank		
October			
3	Reserve Bank of Australia		
4	Reserve Bank of New Zealand		
13	Bank of Korea		
26	Bank of Brazil		
26	Bank of Canada*		
27	European Central Bank		
27	Bank of Japan		
31	Reserve Bank of Australia		
November			
2	Federal Reserve		
3	Bank of England		
3	Bank of Norway		
10	Bank of Mexico		
22	Reserve Bank of New Zealand		
23	Bank of Korea		
24	Bank of Sweden		
December			
5	Reserve Bank of Australia		
7	Bank of Brazil		
7	Bank of Canada		
14	Federal Reserve		
15	European Central Bank		
15	Bank of England		
15	Bank of Norway		
15	Bank of Mexico		
19	Bank of Japan		
**	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. * Monetary Policy Report published; ** To be determined.