

November 30, 2017

Bank of Canada Should Hold Overnight Rate at 1.00 Percent Next Week; Hike to 1.50 Percent by December 2018: C.D. Howe Institute Monetary Policy Council

November 30, 2017 – The C.D. Howe Institute’s **Monetary Policy Council** (MPC) called for the Bank of Canada to keep its target for the overnight rate, the very short-term interest rate it targets for monetary policy purposes, at 1.00 percent at its next announcement on December 6, 2017, and keep it there at its January 2018 announcement. By May of 2018, however, the MPC called for the Bank to hike to 1.25 percent, with a further increase to 1.50 percent by the end of 2018.

The MPC provides an independent assessment of the monetary stance consistent with the Bank of Canada’s 2 percent inflation target. **William Robson**, the Institute’s President and CEO, chairs the Council. Council members make recommendations for the Bank of Canada’s upcoming interest-rate announcement, the subsequent announcement, and the announcements six months and one year ahead. The Council’s formal recommendation for each announcement is the median vote of the members attending the meeting.

All nine MPC members attending this meeting called for a target of 1.00 percent next week, and eight of the nine called for the same target in January 2018. Although the group varied in the size and timing of rate increases, all recommended rises by the end of the period. By May 2018, only one member still called for a target of 1.00 percent, with six calling for 1.25 percent, and two for 1.50 percent. By December 2018, only one member called for a target as low as 1.25 percent, and two members called for a target as high as 2.00 percent (see table below).

The consensus in favour of increases in the policy rate over the coming year reflected continued indicators of steady growth overseas and in the United States, robust domestic demand and a firming labour market, and consumer price inflation that is trending, if gradually, back toward the Bank of Canada’s target. While some members emphasized uncertainty about what level of the overnight rate might be “neutral” – consistent with steady growth and inflation at the 2 percent target – under current circumstances, the group generally saw further progress away from post-crisis emergency levels as appropriate during the coming year.



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Reluctance to recommend a rate hike sooner reflected several points of uncertainty. Many members judged that concerns about a termination of the NAFTA were already hurting business investment, and that bad news on this front would do significant economic damage. Several also emphasized the contrast between potentially pro-growth fiscal policies in the United States and less growth-friendly fiscal policies in Canada – which, notwithstanding the positive impacts of faster US growth on Canadian exports and investment, could on balance shift activity south of the border. The group discussed the potential timing of policy interest rate hikes by the US Federal Reserve, with some arguing that a slower pace of increases by the Bank of Canada would let a lower Canadian dollar buffer the impact of reduced Canadian competitiveness.

On the domestic front, the MPC devoted considerable discussion to recent volatility in indicators of activity in the housing sector. Some members pointed to robust measures of sales, building and prices as supporting a higher policy rate. Others emphasized indicators of weakness, in particular a sharp drop in building permits in Ontario, a possible consequence of rent control and other measures that will restrict supply. A third topic of discussion was macroprudential measures, which might be shifting activity forward in time, and complicating attempts to assess their longer-term impacts. These uncertainties reinforce the tendency for MPC members to recommend raising the overnight rate target, not at the upcoming settings, but later in 2018.

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Votes of MPC members and the Council median for each announcement (*percent*)

MPC Members	Dec 6	Jan 2018	May 2018	Dec 2018
Steve Ambler Université du Québec à Montréal (UQAM)	1.00	1.00	1.25	1.75
Beata Caranci TD Bank Group	1.00	1.00	1.25	1.50
Edward A. Carmichael Ted Carmichael Global Macro	1.00	1.00	1.25	1.25
Michael Devereux University of British Columbia	1.00	1.00	1.25	1.50
Thorsten Koepl Queen's University	1.00	1.00	1.50	2.00
Angelo Melino University of Toronto	1.00	1.00	1.00	1.50
Nicholas Rowe Carleton University	1.00	1.00	1.25	1.50
Pierre Siklos Wilfrid Laurier University	1.00	1.25	1.50	2.00
Craig Wright RBC	1.00	1.00	1.25	1.75
Median Vote	1.00	1.00	1.25	1.50

The views and opinions expressed by the participants are their own and do not necessarily reflect the views of the organizations with which they are affiliated, or those of the C.D. Howe Institute.

The MPC's next vote will take place on January 11, 2018 prior to the Bank of Canada's interest rate announcement on January 17, 2018.

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