Bank of Canada Review: September 2020

As anticipated, the BOC held the overnight rate at 0.25% Wednesday (Bank rate at 0.50%, deposit rate at 0.25%), while "continuing its quantitative easing (QE) program, with large-scale asset purchases of at least $5 billion per week of Government of Canada bonds."- "The Governing Council will hold the policy interest rate at the effective lower bound until economic slack is absorbed so that the inflation target is sustainably achieved," BOC Governor Tiff Macklem said at Thursday's press conference.
- Macklem also said "uneven outcomes for some can lead to poorer outcomes for all. Thus, even if monetary policy cannot target specific sectors, it is important for us to understand the uneven impacts of this recession and to make policy decisions that support lasting, broad-based growth."
- National Bank of Canada: "Going forward, there's little more that the Bank is likely to provide in the way of direct monetary stimulus especially with negative interest rates firmly off the table."

Relevant Links :

Policy Announcement:
https://www.bankofcanada.ca/2020/09/fad-press-release-2020-09-09/

Policy Press Conference: Tiff Macklem, Governor Bank of Canada
https://www.bankofcanada.ca/2020/09/supporting-growth-and-greater-opportunity/

BOC interest rate announcements for 2020:
Wednesday, January 22* (steady at 1.75)
Wednesday, March 4 (-0.5 to 1.25)
--- UNSCHEDULED ---
Monday, March 16 (-0.5 to 0.75)
Friday, March 27 (-0.5 to 0.25)

Wednesday, April 15* (steady at 0.25)
Wednesday, June 3 (steady at 0.25)
Wednesday, July 15* (steady at 0.25)
Wednesday, September 9 (steady at 0.25)
Wednesday, October 28*
Wednesday, December 9
*Monetary Policy Report published

Implementation adjustment: According to the Bank of Canada site, "starting in 2021, the target for the overnight rate will take effect on the business day following each rate announcement. This differs from the Bank's current approach, whereby Governing Council rate decisions apply immediately upon release. The Bank is also reviewing the publication time of its interest rate announcements, which is currently 10:00 (ET). Any changes resulting from this review will be communicated in due course.

Sell-Side Analyst Reviews:

CIBIC: The Bank of Canada interest rate decision was largely as expected, though the inclusion of the word 'calibrate' with respect to QE could be meaningful. For months now, we have argued the Bank needs to 'right size' its QE program to allow for more permanency. We continue to expect changes to be announced at the October MPR.
- There were subtle hints of optimism in the statement yesterday, reflecting the stronger pace of growth expected for Q3. But the short-end is already pricing a rate hike a full year ahead of the Fed, meaning little room to reprice.

Citi: "As expected, there was no notable hawkish or dovish lean to the September policy statement. Updated language acknowledged that the rebound in activity has seen stronger than expected in July, but a full recovery of economic activity will still likely be "slow and choppy". It is hard to know exactly what the BoC's outlook for growth is, as updated GDP forecasts were not included in the policy statement and will likely only be provided in the October Monetary Policy Report. However, we suspect that we are likely still more optimistic that the recovery phase will show a persistent, albeit slower, pace of growth, especially after significant new fiscal measures recently announced."

National Bank of Canada: "Going forward, there's little more that the Bank is likely to provide in the way of direct monetary stimulus especially with negative interest rates firmly off the table. This can be demonstrated by the Bank's removal of the pledge to "provide further monetary stimulus as needed".
As we move towards 2021, markets may look for better guidance on the Bank's Government of Canada bond purchases to clarify what the economic recovery being "well underway" looks like in practice. Should term rates move decisively higher, we could see a move to yield curve control à la Japan and Australia though we'd judge this to be premature at this juncture. Overall, today's statement didn't really come with any surprises, reflected in the relatively muted response in rates following the release.”

RBC: "Tempering any optimism about stronger-than-expected data in the re-opening phase, the bank still expects the upcoming recuperation phase will be "slow and choppy." Inflation is expected to remain well below 2% in the near term, and recent slowing in the BoC's core measures was attributed to significant economic slack. The bank maintained its commitment to keep its policy rate at the effective lower bound until that slack is absorbed and inflation is sustainably at 2%—a process that's likely to be measured in years. Governing Council tweaked its previous commitment to "provide further monetary stimulus as needed," instead saying its QE program (set to continue until the recovery is well underway) will be calibrated to provide the necessary stimulus. While that suggests the program could be expanded or tapered if required, we don't think it flags an imminent change in the bank's asset purchases."

Scotiabank: "The Bank of Canada is in a holding pattern pending a handful of major potential developments that may determine next steps into year-end:
- "How they are reading movement toward the Federal Liberal government's throne speech two weeks from today and what it potentially tees up by way of a possible further spending spree."
- "Is the evolution of the pandemic as Canadian cases rise particularly in western Canada. "
- Is the "faster than expected rebound of late is sustainable or results in a future pulled-forward demand vacuum that is reminiscent of what Federal fiscal stimulus and rate cuts did in 2015-17."
- Conclusion: "Until we have further clarity on these matters, the BoC is taking a nap."

TD: There is nothing terribly surprising about the policy decision itself: it would have gravely undermined credibility to make changes to forward guidance so soon after it had been put in place. Similarly, there was never any indication that the BoC was looking at tapering QE at such an early juncture in the recovery process. While the Bank downplayed the upside surprise on Q2 GDP, they did acknowledge that the bounce back in activity looked to be happening more quickly than anticipated. In the text of the communique, the Bank singled out household spending and housing demand as sources of strength.
- The tone fell short of unrestrained glee; clearly concerns remain around business investment, and the strength in household spending was attributed to pent-up demand. Moreover, the Bank emphasized that going forward growth was expected to be slow and choppy. Still, the tone was noticeably more upbeat than the July MPR's.

MNI Policy Reviews

BOC Watches Strong C$, May Curb QE Before Rates Up

By Greg Quinn

OTTAWA (MNI) - Bank of Canada Governor Tiff Macklem said Thursday he will account for strength in his native currency against the U.S. dollar, adding that over the long comeback from Covid-19 it's logical to dial back QE before lifting near-zero interest rates.

"Over the last month we have seen a broad-based depreciation of the U.S. dollar," Macklem said at a press conference following a speech. "It has appreciated a little bit less than some others, and that is certainly something that we will take into account as we assess the amount of monetary stimulus required in the economy."

"Our next decision, which will come with a Monetary Policy Report, and with that a revised central scenario, we will be taking into account any movements in the Canadian dollar in our assessment of how much monetary stimulus is needed," he said. The MPR reports often simply take the recent average exchange rate as an assumption used to build an economic forecast, and the BOC gave up solo currency intervention in 1998.

Still, the BOC view adds to concerns already voiced by the ECB about the U.S. dollar's weakness as the Federal Reserve also seeks easy monetary policy to sustain economic growth during the global pandemic. Fed officials have said their prime focus is the domestic economy.

In response to a question from MNI, Macklem also gave more detail on the main change in yesterday's decision to hold a 0.25% rate until inflation is sustainably at the 2% goal-- a reference to calibrating QE instead of being ready to offer more stimulus as needed. Investors have speculated the BOC could move to QE if the economy stumbles again, or slow the pace of QE if the purchases already worth about 25% of GDP create shortages of some federal bonds.

--What to Buy

"When we say we're going to calibrating going forward, what that means is we will be assessing what to buy, as well as how much to buy. Could be more, could be less," Macklem said.

The recovery still has a long way to go so it's premature to consider any real exit strategy, he said. Macklem said the potential timing is evident in the BOC's pledges to buy at least CAD5 billion a week of federal bond purchases until the recovery is well underway, along with holding rates until slack is absorbed and inflation holding on target. "Logically, the recovery very being well underway comes before slack is absorbed," Macklem said.

He downplayed the policy significance of balance sheet growth stalling out after hitting a record CAD547 billion at the end of July, saying that reflects a decline in repo purchases when markets froze earlier this year while federal bond purchases continue. The focus of purchases has shifted to aiding the recovery with a move into longer-term debt more closely linked to consumer and business borrowing costs, he said.

"I don't know what else they can do-time is what's going to recover this economy, it's not going to be more or less asset purchases by the Bank of Canada, it's not going to be the introduction of yield curve control," Ryan Goulding, fixed income analyst at Leith Wheeler Investment Counsel in Vancouver, said in a phone interview. The firm manages CAD20 billion.

Macklem isn't a fan of Modern Monetary Theory, saying it has a long history of "ending badly" in response to an audience question after his speech.

--Long Recuperation

The economy will slow in coming months after a burst tied to the re-opening, and restoring the last million or so jobs lost will be much more difficult, he said. "We're moving into the recuperation phase," he said, and "we still have a very long way to go."

His earlier speech made several references to full employment, a sign he may be looking at expanding the BOC's single inflation mandate to add something on jobs, TD Bank senior economist Brian DePratto wrote in a research note.

The BOC is due to renew an inflation targeting deal with the government next year, and Macklem said there is no clearly superior alternative to the 2% target, which Canada has been using for decades now. The Fed's embrace of flexible average inflation targeting in some ways mimics latitude the BOC already has, Macklem said, adding "this is an interesting evolution of inflation targeting, and it's certainly something we will be looking at closely."

MNI POLICY REVIEW: BOC Says QE Will Be Calibrated to Support Recovery

By Greg Quinn

OTTAWA (MNI) - The Bank of Canada said Wednesday it could adjust QE to support the long and choppy recovery following the Covid-19 reopening, a slightly more even-handed approach than in its the July statement when it said it would offer more stimulus if needed.

The Ottawa-based bank also affirmed a plan to keep its key lending rate at the lower bound of 0.25% until inflation is sustainably back at the 2% target. The pace of QE was also confirmed at at least CAD5 billion a week of federal bond purchases.

"This QE program will continue until the recovery is well underway and will be calibrated to provide the monetary policy stimulus needed to support the recovery and achieve the inflation objective," policy makers led by Governor Tiff Macklem wrote in a one-page statement. The change in wording to calibrated was one of the only real shifts from the July statement that "the Bank is prepared to provide further monetary stimulus as needed."

The BOC's balance sheet reached 27% of second-quarter GDP or CAD537 billion last week, and some investors have speculated yield curve control may become an option if the economy weakens or QE creates shortages of some bond issues. A repeated phrase today about holding down yields across the curve may signal that curve control isn't happening. Such a move would be difficult anyways with Canadian bonds often driven by trends in U.S. Treasuries.

--Wobbly Recovery

While third-quarter growth may be faster than policy makers expected, they also stressed potential weaknesses in exports, business investment and a shaky jobs recovery. The economy's 13% contraction in the first half is about what the BOC expected. Private economists see a 40% third-quarter expansion to match the second-quarter's historic decline, thought that still won't bring the economy back to where it was before.

"The Bank continues to expect this strong reopening phase to be followed by a protracted and uneven recuperation phase, which will be heavily reliant on policy support," the statement said.

Inflation will remain well below target in the near term and core price measures are consistent with a "large degree of economic slack," the BOC said. There were no specific updated economic projections for coming quarters or for 2020 GDP.

All 13 economists surveyed by MNI predicted no change in the policy rate on Wednesday, and several see the rate on hold through all of next year at least. In July the BOC projections showed inflation won't return to 2% through 2022.