Economic Commentary

January 24, 2005

Bank of Canada to Stand Pat Tomorrow

The Bank of Canada's rate setting policy committee is meeting tomorrow morning and is widely expected to keep the target for the overnight rate on hold, at 2.5%.

The reasons for standing pat on rates are first, that the rising Canadian dollar is extracting an increasing toll on Canada's manufacturing sector and exports to the rest of the world. Second, inflation remains subdued, averaging 2.1% for the twelve-month period ending in December, 2004 and with the core rate averaging 1.7% for the period, below the central bank's target of 2.0%. Third, a slow down in growth rates in the global economy are also exercising a restraining effect.

Overall, as I forecast in the November three-year economic outlook, rates this year will not rise as much as the market was predicting as late as October, 2004 for the reasons sighted above.

If the US Fed continues on its rate-tightening course, the Fed meets next on February, 2nd, 2005, Canada-USA spreads will narrow further and at some point the Bank of Canada might see the need to raises rates in Canada. However, some forecasters have come out recently to predict that the Bank of Canada, far from raising rates further, might even be forced to cut rates later on this year. We shall see.

Kenneth Matziorinis, Ph.D.
Canbek Economic Consultants Inc.
canbekeconomics@videotron.ca