



Laurentian Bank Securities **ECONOMIC RESEARCH AND STRATEGY**

BoC responds to coronavirus threat with a 50 basis points cut

Echoing the Federal Reserve with a short [statement](#), the Bank of Canada cut its overnight rate target by 50 basis points to 1.25%. Similar to the [OECD](#)'s message sent earlier this week, the BoC says that *"the COVID-19 virus is a material negative shock to the Canadian and global outlooks, and monetary and fiscal authorities are responding"*. The Governing Council easily justifies today's decision by citing the public health threat, global supply chain disruptions, the decline in commodity prices, the deterioration in consumer and business confidence and the repricing of risk in financial markets.

In our view, it was preferable for the BoC to match yesterday's move by the Fed. Easing by 25bps would have increased the risk of falling behind the curve, particularly if Chairman Powell eases at the next scheduled meeting on March 18th. The BoC and the Fed policy decisions can differ during industry-specific shocks. For instance, the plunge in crude oil prices prompted the BoC to cut in early 2015. In 2008, the U.S. housing crisis pushed the Fed to bring down its benchmark rate closer to zero than the BoC. This time, Canada's greater dependence on China for trade, commodities and tourism makes it hard for the BoC to be gentler than the Fed. This being said, Ottawa has more room to come up with an expansionist fiscal response than Washington.

Where do we go from here? The door is clearly open to more BoC easing, at or before the April 15th fixed announcement date. Future actions will depend on how the virus, financial markets and the economy progress: *"As the situation evolves, Governing Council stands ready to adjust monetary policy further if required to support economic growth and keep inflation on target"*. The range of possibilities is very large. If covid19 is contained within the next month, the BoC may not need to ease further to support the economy. But even under this scenario, a V-shaped global recovery would be very surprising due to the long lasting impacts on the highly-integrated global supply chain. Thus, we do not see how the BoC could be in a position to bring back the policy rate at 1.75% before 2021. During the very brief economic slowdown of late 2001 following 9/11, the BoC was able to cut by a cumulative 200bps before hiking by 25bps 7 months later in April 2002. Finally, under the extreme severe scenario of a broader contagion resulting in a global economic meltdown, the BoC may have to bring down its policy rate at the zero lower bound. Bond yields across Canadian and U.S. curves could fall to zero as well.

Governor Poloz will explain today's decision in his speech tomorrow at 12:45PM.

Sébastien Lavoie | Chief Economist
514 350-2931 | lavoies@vmbi.ca

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