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## Canada's central bank – Update from the Investment Division

Erste AM Communications



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### What has occurred since yesterday ?

Canada's central bank left the key interest rate unchanged at 0.25% yesterday. Importantly, the so-called forward guidance, i.e. the verbal guidance of market expectations, was refined: The key interest rate will remain at the effective lower limit until the negative output gap has disappeared (i.e. full employment has been reached), so that the inflation target of 2% can be achieved on a sustainable basis. A similar adjustment of the forward guidance is expected for the US Federal Reserve and subsequently for other central banks.

The introduction of a yield cap for government bonds was also discussed but not implemented. This is probably because such a measure is not necessary at present. The yield on 10-year government bonds has been moving sideways at 0.5% since March. Long-term yields are largely determined by the expected development of short-term interest rates. As long as the (conditional) fixing is sufficient to keep key rates low for a longer period of time, so that long-term yields also remain low, a yield cap is not necessary.

No change in the monetary policy stance is expected at today's meeting of the Governing Council. Monetary policy will remain ultra-expansive for the foreseeable future. This is not a problem as long as there is no conflict of objectives between price stability and the financing of public deficits. In the long run, an inflation problem could arise if the inflation dynamic necessitates a tightening of monetary policy (key rate hikes, no net purchases of government bonds), but the government deficits need the central bank as a provider of liquidity. At least in the medium (cyclical) term, this conflict of goals will (probably) not exist.

At the press conference, questions could be asked about the duration (extension) and size (increase) of the crisis bond purchase program (PEPP), yield caps, monetary financing of government deficits, changes in forward guidance and ESG orientation. President Lagarde could use the forum to put forward a possible next ECB measure for the autumn.

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