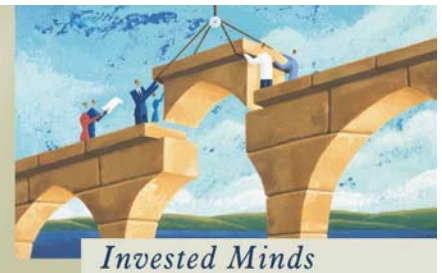




Global Asset Management Inc.

# Market Insight



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## Bank of Canada Cuts Interest Rates To Prod Economic Growth

The Bank of Canada cut interest rates by 25 basis points today bringing the overnight rate down to 2.50%. This is the first change in rates in more than five months. The BoC cited the combined impact of a soaring Canadian dollar, weaker domestic demand and inflation, and that economic growth may not be as strong as originally expected as reasons for its action.

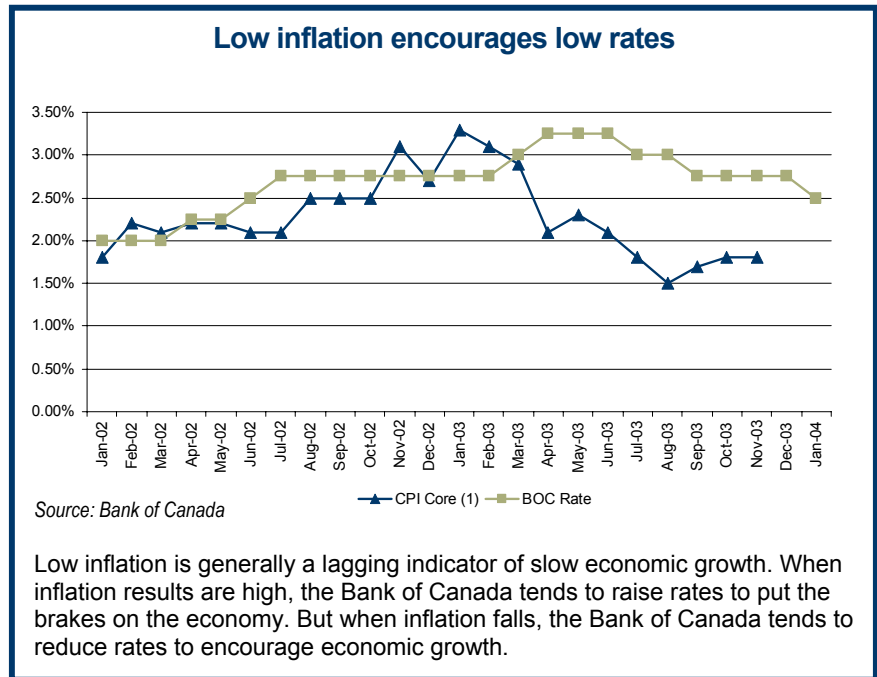
A year ago the BoC had projected that by this point in time, inflation would be above their target because spare capacity would have been used up. The rate cut reverses last year's strategy, which was designed to fight inflation rather than stimulate growth.

"Despite stronger global economic growth, the rapid appreciation of the Canadian dollar against the U.S. currency has cut into the overall growth of aggregate demand for Canadian goods and services through weaker exports and increased imports," the central bank said in its statement.

Almost immediately after the decision, Canada's major banks followed suit, cutting prime lending rate to 4.25 per cent.

"It is good that they cut interest rates by 25 basis points," John Braive, TAL Global Asset Management vice chair and fixed income manager says. "The economy was in need of some stimulus. The effect of a strong Canadian dollar, a weaker Canadian economy, and falling inflation all indicate that the Bank of Canada has to loosen up on monetary policy. The 25 basis points is probably the first cut and there will be another one in March."

That the Bank of Canada would implement this rate cut was no surprise. The appreciation of the Canadian dollar created a lot of buzz about today's statement and economists had been forecasting some central bank monetary action to address the current Canadian economic position.



"TAL's fixed income team forecast the Bank of Canada would cut 50 basis points over two meetings," Mr. Braive says. "If they had done more than we anticipated, that would have shown some panic on their part."

As a result of the rate decrease, the slope of the curve steepens even more, with lower rates at the short end. A steep curve is good for the economy. An interest rate cut would normally have some impact on the Canadian dollar, but since the move was so widely anticipated, the loonie rose versus the U.S. dollar after the announcement.

"It is a change in the Bank of Canada tenor showing that they are willing to use monetary policy if they see weakness and low inflation continuing," Mr. Braive says.

The Bank of Canada hinted that a stagnant economy is likely to persist through this year and into 2005, and the door remains open for more moves if the picture doesn't brighten. The bank's next interest rate decision is slated for March 2.