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## Negative Interest Rates

By Clinton Orr

Interest rates in Canada have been low for a while and with rates around the world falling our interest rates could get even lower. Some countries have negative interest rates. Why would interest rates be negative? Could that happen in Canada? We will try to tackle both questions.

In 2012 Denmark's central bank was one of the first to push its overnight rate into negative territory. In 2014 the European Central Bank moved their overnight interest rate to negative territory. In 2016 Japan followed suit. The overnight rate set by the central bank is important, it impacts all the other interest rates in the economy. Fast forward to today, there is now multiple Asian and European countries with negative interest rates.

In August, Deutsche Bank estimated that there were \$15 Trillion worth of government bonds with a negative yield, that means of all the government bonds in the world roughly 1 in 4 has a negative yield. For example, at the moment, the 10-year bond from the German government has a yield of -0.61%, which means you invest your hard-earned money and 10 years later you are guaranteed to have slightly less money than you started. Another example, Jyske, Denmark's third largest bank, recently launched the world's first 10-year mortgage with a negative interest rate.

The rate is -0.5%, which means you take out a mortgage and pay the bank back less than you borrowed. The other side of the coin is that banks charge customers for their deposits, instead of earning interest on the money you have in savings, you pay for privilege of having your money in the bank. This last item has not been fully implemented, financial institutions with negative interest rates have been charging their corporate clients for deposits but are yet to charge their retail clients. As the examples above show negative interest rates completely change our relationship with financial institutions.

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So why do some countries have negative rates? When interest rates are lowered it is supposed to stimulate the economy. The lower rates discourage people from saving and encourage people to spend and invest, which helps move the economy forward. Negative interest rates are an extreme example of that concept.

The economy was sluggish, rates were already near zero, so they were pushed into negative territory to help stimulate the economy. That is the theory anyway, the data so far has been mixed. Despite negative interest rates, deposits at many European banks have actually increased. As well in both Europe and Japan lending has not increased in a material way and both economies remain sluggish. We have not been in this situation before, we do not know the long-term impact of negative rates. In the short and medium term, we are still waiting for data to see if negative rates had the desired impact.

So, could Canada or the US get negative interest rates? The economies of both Canada and the US are slowing and interest rates in the US are starting to drop. The Federal Reserve in the US has already cut rates a few times this year. In fact, in September, President Trump, via twitter, demanded that rates in the US be cut to zero and maybe pushed into negative territory. Despite the President's prompting I do not believe Canada or the US will have negative rates. Interest rates in the US have already been cut, eventually Canada will do the same, so we will have lower interest rates but it is unlikely we will have to deal with negative rates.

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