

David Dodge: Economic and financial trends in the context of Canada's inflation-control strategy

Opening statement by Mr David Dodge, Governor of the Bank of Canada, on the release of the *Monetary Policy Report Update*, 24 July 2002.

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Today, we published our *Update* to the April *Monetary Policy Report*, in which we discuss economic and financial trends in the context of Canada's inflation-control strategy.

Canada's economic recovery, which began in the last quarter of 2001, gathered momentum in the first half of 2002. Over the period to the end of 2003, the Bank projects continued solid economic expansion at an annual rate of 3 to 4 per cent. This will result in growth of close to 3 1/2 per cent on an annual average basis in 2002 and in 2003. Both the total and core rates of inflation are projected to be slightly above 2 per cent in the second half of 2002, before steadying out at close to 2 per cent in 2003.

Given that the Canadian economy grew at a faster pace than anticipated in the first half of 2002, there is now less excess capacity than was projected in our April *Report*. The economy is expected to be operating at full capacity in early 2003 - sooner than previously anticipated.

In light of these developments, the Bank has continued to reduce the amount of monetary stimulus in the economy, raising the target for the overnight interest rate by 25 basis points on three occasions - in April, June, and July - to bring the rate to 2 3/4 per cent.

It remains the Bank's view that the underlying economic situation will require further reductions in the amount of monetary stimulus. The timing and pace of policy adjustments will depend on the strength of the various factors at play and their implications for pressures on capacity, and thus on inflation.

There are both upside and downside risks to the outlook for Canadian economic growth. On the positive side, growth of domestic demand could turn out to be stronger than projected because of the substantial amount of monetary stimulus still in place. On the negative side, there are the uncertainties associated with global corporate and financial market developments and their potential effects on confidence and world economic growth. At this time, the risks to our projected rate of growth of 3 to 4 per cent growth appear to be balanced.

As we go forward, the Bank will remain focused on taking actions to achieve the 2 per cent inflation target. Keeping inflation low and stable is the best contribution that monetary policy can make to sustained economic growth in Canada.