Mark Carney: Bank of Canada's economic overview and monetary policy stance

Opening statement by Mr Mark Carney, Governor of the Bank of Canada, at the House of Commons Standing Committee on Finance, Ottawa, 27 October 2009.

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Good morning, Mr. Chairman and committee members. Paul and I are pleased to appear before this committee today to discuss the Bank of Canada's views on the economy and our monetary policy stance. While conditions in the Canadian economy have improved since we met with you in February and April, many of the basic challenges remain. Before Paul and I take your questions, I would like to give you some of the highlights from our latest *Monetary Policy Report*, released last week.

- Recent indicators point to the start of a global recovery. Economic and financial developments have been somewhat more favourable than the Bank had expected in July, although significant fragilities remain.
- In Canada, as expected, a recovery in economic activity is also under way, following three consecutive quarters of sharp contraction. This resumption of growth is supported by monetary and fiscal stimulus, increased household wealth, improving financial conditions, higher commodity prices, and stronger business and consumer confidence.
- However, heightened volatility and persistent strength in the Canadian dollar are working to slow growth and subdue inflation pressures. The current strength in the dollar is expected, over time, to more than fully offset the favourable developments since July.
- Given all these factors, the Bank now projects that, relative to our July Monetary Policy Report, the composition of aggregate demand will shift further towards final domestic demand and away from net exports.
- We now expect growth to average slightly lower over the balance of the projection period. The Bank projects that the Canadian economy will contract by 2.4 per cent this year and then grow by 3.0 per cent in 2010 and 3.3 per cent in 2011. This projected recovery will be somewhat more modest than the average of previous cycles.
- Total CPI inflation declined to a trough of -0.9 per cent in the third quarter, reflecting large year-on-year drops in energy prices.
- Total CPI inflation should rise to 1.0 per cent this quarter, while the core rate of inflation is projected to reach its trough of 1.4 per cent during the same period.
- Owing to the substantial excess supply that has emerged in the economy, the Bank expects both core and total inflation to return to the 2 per cent target in the third quarter of 2011, one quarter later than we projected in July.
- The main upside risks to inflation relate to the possibility of a stronger-than-anticipated recovery in the global economy and more robust Canadian domestic demand.
- On the downside, the global recovery could be even more protracted than projected. In addition, a stronger-than-assumed Canadian dollar, driven by global portfolio movements out of U.S.-dollar assets, could act as a significant further drag on growth and put additional downward pressure on inflation.

- On Tuesday, 20 October, the Bank reaffirmed its conditional commitment to maintain its target for the overnight rate at the effective lower bound of 1/4 per cent until the end of June 2010 in order to achieve the inflation target.
- The Bank retains considerable flexibility in the conduct of monetary policy at low interest rates, consistent with the framework that we outlined in the April MPR.
- Our focus in the conduct of monetary policy is on achieving the 2 per cent inflation target. The exchange rate should be seen in this context. It is an important relative price, which the Bank monitors closely.
- What ultimately matters is the exchange rate's impact in conjunction with all other domestic and foreign factors on aggregate demand and inflation in Canada. To put it simply, the Bank looks at everything through the prism of achieving our inflation target.

With that, Mr. Chairman and committee members, Paul and I would now be pleased to answer your questions.