Stephen S Poloz: Opening statement before the House of Commons Standing Committee on Finance

Opening statement by Mr Stephen S Poloz, Governor of the Bank of Canada, before the House of Commons Standing Committee on Finance, Ottawa, Ontario, 30 April 2019.

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Good morning, Mr. Chairman and committee members. Once again, Senior Deputy Governor Wilkins and I are pleased to be with you to talk about the Bank's *Monetary Policy Report* (MPR), which we published last week.

Six months ago, when we last appeared before this committee, we talked about some very positive developments. The Canadian economy had solid momentum and had essentially completed its journey home—that is to say, it was operating very close to its capacity, and inflation was running near our target. At the same time, we were monitoring the risks posed by protectionist trade measures and elevated levels of household debt.

Unfortunately, since then, there have been a couple of negative developments. These have caused a detour for the economy and are delaying its return home. Our forecast is based on the belief that the impact of these developments will be temporary, and that once the associated adjustments take place, stronger economic growth will resume. So, in the MPR, we marked down our forecast for economic growth this year to 1.2 per cent, and we project growth of near 2 per cent for both 2020 and 2021.

Let me give you some details. First, the global economy slowed toward the end of last year. To be clear, some slowing was expected as the stimulative impact of US fiscal measures fades. But the slowdown was deeper than most forecasters projected and has persisted into 2019.

A major factor behind this global slowdown has been the US-led trade war. This is delaying business investment decisions in many countries around the world. Uncertainty about future trade policies has risen—here in Canada, doubts about the ratification of the Canada-United States-Mexico Agreement have increased, and these remain a downside risk to our outlook for investment.

It is certain that an escalation of trade conflicts would be a blow to the global economy. However, the global economy could receive a significant lift if there were progress in resolving these conflicts. I should emphasize that businesses and economies will ultimately adjust to the heightened level of uncertainty around trade, by adjusting their investment plans lower. Once those adjustments are complete, however, economic growth can pick up again.

The other major development since October was another sharp decline in oil prices late in 2018, which put Canada's oil sector under considerable stress. More recently, oil prices have firmed, including the prices our western producers receive. But transportation constraints on future growth remain a significant source of drag and uncertainty. This has led to another downward revision to investment intentions in the sector. Some of this downgrade is likely more structural than cyclical in nature, as it represents the continued adjustment of the sector to global oil prices of US$50–60 per barrel, rather than the much higher prices of five years ago. This adjustment process is also being reflected in wages and other costs, and in developments in the housing market in Alberta.

It is important to note that as investments in the oil patch are pared back, Canada's growth slows. But when those investment levels stop falling, Canada's growth will pick up again, even if oil sector investment does not, because other areas of growth will come to dominate the data. We saw this same dynamic following the oil price shock of 2014–15.

In addition to concerns about global trade and oil prices, we have continued to watch how the Canadian housing market is adjusting to the combination of provincial and municipal housing policy measures, the revised guidelines for mortgage lending, and past increases in interest rates. The adjustment of the housing market is particularly important given the context of elevated levels of household debt.

Our analysis has been complicated by activity in some previously frothy markets—the greater Toronto and Vancouver areas, in particular. Research by Bank staff shows that the sharp rise in housing resales above fundamental levels in Ontario and British Columbia—and the subsequent fall—correlates strongly with house price expectations. This suggests that provincial and municipal housing policy measures have had a much stronger impact on housing activity than changes to mortgage lending guidelines and past increases in interest rates. Supporting this analysis is the fact that many other markets across the country are seeing solid activity even though they have the same mortgage lending guidelines and interest rates. This is what would be expected in an economy that is growing, with a rising population and strong labour market. The implication is that as the situation in Toronto and Vancouver stabilizes, the Canadian housing sector should return to growth overall later this year.

Finally, I would note that the federal government and several provinces have made fiscal announcements during budget season. Our analysis suggests that the combined impact of adjusted spending plans announced to date would lead to a downward revision for our growth outlook of about 0.2 percentage points in 2020.

In sum, the Canadian economy is currently facing some headwinds, but there is good reason to believe that the economy will accelerate in the second half of this year. In this context, the Bank's Governing Council judges that an accommodative policy interest rate continues to be warranted. We will continue to evaluate the appropriate degree of monetary policy accommodation as new data arrive. In particular, we are monitoring developments in household spending, oil markets and global trade policy to gauge the extent to which the factors weighing on growth and the inflation outlook are dissipating.

With that, Senior Deputy Wilkins and I would be happy to take your questions.