



# Monetary Policy Report Summary

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April 2014

*This text is a commentary of the Governing Council of the Bank of Canada.*

## Highlights

- **Inflation in Canada remains low. Core inflation is expected to stay well below 2 per cent this year due to the effects of economic slack and heightened retail competition, and these effects will persist until early 2016. Total CPI inflation is forecast to be closer to 2 per cent over the coming quarters and remain close to target thereafter.**
- **The global economic expansion is expected to strengthen over the next three years, as headwinds that have been restraining activity dissipate.**
- **In Canada, the fundamental determinants of growth and inflation continue to strengthen gradually, as anticipated.**
- **The Bank continues to expect Canada's real GDP growth to average about 2 1/2 per cent in 2014 and 2015 before easing to around the 2 per cent growth rate of the economy's potential in 2016.**

Inflation in Canada remains low. Core inflation is expected to stay well below 2 per cent this year due to the effects of economic slack and heightened retail competition, and these effects will persist until early 2016. However, higher consumer energy prices and the lower Canadian dollar will exert temporary upward pressure on total CPI inflation, pushing it closer to the 2 per cent target in the coming quarters. The Bank expects total CPI inflation will remain close to target throughout the projection, even as upward pressure from energy prices dissipates, because the impact of retail competition will gradually fade and excess capacity will be absorbed.

The global economic expansion is expected to strengthen over the next three years as headwinds that have been restraining activity dissipate. The economic recovery in the United States appears to be on track, despite soft readings in the last few months largely due to unusual weather. Indeed, private demand could turn out to be stronger than anticipated. Europe's economy is growing modestly, but inflation remains too low and the nascent recovery could be undermined by risks emanating from the Russia-Ukraine situation. In China and other emerging-market economies growth is expected to be solid, although there are growing concerns about financial vulnerabilities. Overall, global growth is expected to pick up to

3.3 per cent in 2014 and increase further to 3.7 per cent in 2015 and 2016—largely unchanged from January.

The Bank continues to expect Canada’s real GDP growth to average about 2 1/2 per cent in 2014 and 2015 before easing to around the 2 per cent growth rate of the economy’s potential in 2016. Competitiveness challenges continue to weigh on Canadian exporters’ ability to benefit from stronger growth abroad. However, a range of export subsectors have been growing in line with fundamentals, which suggests that as the U.S. recovery gathers momentum and becomes more broadly-based, many of our exports will benefit. The lower Canadian dollar should provide additional support. The Bank continues to believe that rising global demand for Canadian goods and services, combined with the assumed high level of oil prices, will stimulate business investment in Canada and shift the economy to a more sustainable growth track.

Recent developments are in line with the Bank’s expectation of a soft landing in the housing market and stabilizing debt-to-income ratios for households. Still, household imbalances remain elevated and would pose a significant risk should economic conditions deteriorate.

In sum, the Bank continues to see a gradual strengthening in the fundamental drivers of growth and inflation in Canada. This view hinges critically on the projected upturn in exports and investment. With underlying inflation expected to remain below target for some time, the downside risks to inflation remain important. At the same time, the risks associated with household imbalances remain elevated. The Bank judges that the balance of these risks remains within the zone for which the current stance of monetary policy is appropriate and therefore has decided to maintain the target for the overnight rate at 1 per cent. The timing and direction of the next change to the policy rate will depend on how new information influences the balance of risks.

#### Projection for global economic growth

	Share of real global GDP <sup>a</sup> (per cent)	Projected growth <sup>b</sup> (per cent)			
		2013	2014	2015	2016
<b>United States</b>	20	1.9 (1.9)	2.8 (3.0)	3.2 (3.2)	3.0
<b>Euro area</b>	14	-0.4 (-0.4)	1.1 (0.9)	1.3 (1.4)	1.6
<b>Japan</b>	5	1.5 (1.7)	1.2 (1.8)	1.3 (1.1)	1.0
<b>China</b>	15	7.7 (7.7)	7.3 (7.2)	7.3 (7.1)	7.2
<b>Rest of the world</b>	47	2.9 (2.9)	3.2 (3.2)	3.8 (3.8)	3.8
<b>World</b>	100	2.9 (2.9)	3.3 (3.4)	3.7 (3.7)	3.7

a. GDP shares are based on International Monetary Fund (IMF) estimates of the purchasing-power-parity (PPP) valuation of country GDPs for 2012. The individual shares may not add up to 100 owing to rounding.

Source: IMF, *World Economic Outlook*, October 2013

b. Numbers in parentheses are projections used for the January 2014 *Monetary Policy Report*.

Source: Bank of Canada

**Summary of the projection for Canada<sup>a</sup>**

	2013	2014				2015				2016			
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<b>Real GDP (quarter-over-quarter percentage change at annual rates)</b>	2.9 (2.5)	1.5 (2.5)	2.5 (2.5)	2.6 (2.5)	2.5 (2.6)	2.5 (2.5)	2.4 (2.5)	2.4 (2.3)	2.3 (2.2)	2.2	2.1	2.0	2.0
<b>Real GDP (year-over-year percentage change)</b>	2.7 (2.3)	2.3 (2.3)	2.4 (2.5)	2.4 (2.5)	2.3 (2.5)	2.5 (2.5)	2.5 (2.5)	2.4 (2.5)	2.4 (2.4)	2.3	2.2	2.1	2.1
<b>Core inflation (year-over-year percentage change)</b>	1.2 (1.2)	1.2 (1.0)	1.2 (1.2)	1.4 (1.3)	1.6 (1.5)	1.6 (1.6)	1.7 (1.7)	1.8 (1.8)	1.9 (1.9)	2.0	2.0	2.0	2.0
<b>Total CPI (year-over-year percentage change)</b>	0.9 (0.9)	1.3 (0.9)	1.6 (1.2)	1.8 (1.4)	1.9 (1.5)	2.0 (1.7)	2.0 (1.9)	2.0 (1.9)	2.0 (2.0)	2.0	2.0	2.0	2.0
<b>Total CPI excluding the effect of the HST and changes in other indirect taxes (year-over-year percentage change)</b>	1.0 (1.0)	1.4 (1.0)	1.5 (1.2)	1.8 (1.4)	1.9 (1.5)	2.0 (1.7)	2.0 (1.9)	2.0 (1.9)	2.0 (2.0)	2.0	2.0	2.0	2.0

a. Numbers in parentheses are from the projection in the January 2014 *Monetary Policy Report*. Assumptions for the price of West Texas Intermediate and Brent crude oil (US\$ per barrel) are based on an average of spot prices over the recent period.

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