



BANK OF CANADA
BANQUE DU CANADA

Bank of Canada maintains overnight rate target at 1 per cent

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The Bank of Canada today announced that it is maintaining its target for the overnight rate at 1 per cent. The Bank Rate is correspondingly 1 1/4 per cent and the deposit rate is 3/4 per cent.

The global economic recovery is proceeding at a somewhat faster pace than the Bank had anticipated, although risks remain elevated. Private domestic demand in the United States has picked up and will be reinforced by recently announced monetary and fiscal stimulus. European growth has also been slightly stronger than anticipated. Ongoing challenges associated with sovereign and bank balance sheets will limit the pace of the European recovery and are a significant source of uncertainty to the global outlook. In response to overheating, some emerging markets have begun to implement more restrictive policy measures. Their effectiveness will influence the path of commodity prices, which have increased significantly since the October *Monetary Policy Report* (MPR), largely reflecting stronger global growth.

The recovery in Canada is proceeding broadly as anticipated, with a period of more modest growth and the beginning of the expected rebalancing of demand. The contribution of government spending is expected to wind down this year, consistent with announced fiscal plans. Stretched household balance sheets are expected to restrain the pace of consumption growth and residential investment. In contrast, business investment will likely continue to rebound strongly, owing to stimulative financial conditions and competitive imperatives. Net exports are projected to contribute more to growth going forward, supported by stronger U.S. activity and global demand for commodities. However, the cumulative effects of the persistent strength in the Canadian dollar and Canada's poor relative productivity performance are restraining this recovery in net exports and contributing to a widening of Canada's current account deficit to a 20-year high.

Overall, the Bank projects the economy will expand by 2.4 per cent in 2011 and 2.8 per cent in 2012 – a slightly firmer profile than had been anticipated in the October MPR. With a little more excess supply in the near term, the Bank continues to expect that the economy will return to full capacity by the end of 2012.

Underlying pressures affecting prices remain subdued, reflecting the considerable slack in the Canadian economy. Core inflation is projected to edge gradually up to 2 per cent by the end of 2012, as excess supply in the economy is slowly absorbed. Inflation expectations remain well-anchored. Total CPI inflation is being boosted temporarily by the effects of provincial indirect taxes, but is expected to converge to the 2 per cent target by the end of 2012.

Reflecting all of these factors, the Bank has decided to maintain the target for the overnight rate at 1 per cent. This leaves considerable monetary stimulus in place, consistent with achieving the 2 per cent inflation target in an environment of significant excess supply in Canada. Any further reduction in monetary policy stimulus would need to be carefully considered.

Information note:

A full update of the Bank's outlook for the economy and inflation, including risks to the projection, will be published in the MPR on 19 January 2011. The next scheduled date for announcing the overnight rate target is 1 March 2011.

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