



BANK OF CANADA
BANQUE DU CANADA

Bank of Canada lowers overnight rate target by 1/2 percentage point to 1 per cent

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The Bank of Canada today announced that it is lowering its target for the overnight rate by one-half of a percentage point to 1 per cent. The operating band for the overnight rate is correspondingly lowered, and the Bank Rate is now 1 1/4 per cent.

The outlook for the global economy has deteriorated since the Bank's December interest rate announcement, with the intensifying financial crisis spilling over into real economic activity. Heightened uncertainty is undermining business and household confidence worldwide and further eroding domestic demand. Major advanced economies, including Canada's, are now in recession and emerging-market economies are increasingly affected. Energy prices have fallen as a result of substantially weaker global demand.

Stabilization of the global financial system is a precondition for economic recovery. To that end, governments and central banks are taking bold and concerted policy actions. There are signs that these extraordinary measures are starting to gain traction, although it will take some time for financial conditions to normalize. In addition, considerable monetary and fiscal policy stimulus is being provided worldwide.

Canadian exports are down sharply, and domestic demand is shrinking as a result of declines in real income, household wealth, and consumer and business confidence. Canada's economy is projected to contract through mid-2009, with real GDP dropping by 1.2 per cent this year on an annual average basis. As policy actions begin to take hold in Canada and globally, and with support from the past depreciation of the Canadian dollar, real GDP is expected to rebound, growing by 3.8 per cent in 2010.

A wider output gap through 2009 and modest decreases in housing prices should cause core CPI inflation to ease, bottoming at 1.1 per cent in the fourth quarter. Total CPI inflation is expected to dip below zero for two quarters in 2009, reflecting year-on-year drops in energy prices. With inflation expectations well-anchored, total and core inflation should return to the 2 per cent target in the first half of 2011 as the economy returns to potential.

Against this background, the Bank today lowered its policy rate by 50 basis points, bringing the cumulative monetary policy easing to 350 basis points since December 2007. Guided by Canada's inflation-targeting framework, the Bank will continue to monitor carefully economic and financial developments in judging to what extent further monetary stimulus will be required to achieve the 2 per cent target over the medium term. Low, stable, and predictable inflation is the best contribution monetary policy can make to long-term economic growth and financial stability.

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 *Monetary Policy Report Update* on 22 January 2009. The next scheduled date for announcing the overnight rate target is 3 March 2009.

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