BANK OF CANADA

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OTTAWA — The Governor of the Bank of Canada, John W. Crow, in a joint announcement today with the Minister of Finance, set out targets for reducing inflation and reaching price stability in Canada.

These targets are designed to provide a clear indication of the downward path for inflation over the medium term. The path provides for gradual but progressive reductions of inflation until price stability is reached. The range of public policies besides monetary policy can make a significant contribution. However, since inflation cannot persist over an extended period without monetary accommodation, for price stability to be reached it is essential for monetary policy to work firmly and consistently to that end.

The specific targets for the year-over-year rate of increase in the consumer price index (CPI) are as follows:

- 3 per cent by the end of 1992
- 2½ per cent by the middle of 1994
- 2 per cent by the end of 1995
- Thereafter the objective would be further reductions in inflation until price stability is achieved. A good deal of work has already been done in Canada on what stability in the broad level of prices means operationally. This work suggests a rate of increase in consumer prices that is clearly below 2 per cent. However, a more precise definition is not being specified now, in the event that further evidence and analysis relevant to this matter become available in the next few years. A target path after 1995 also remains to be fixed, but again pending new evidence, the aim would be to continue to make steady progress.

In view of the lags involved in the effect of policies on inflation, no explicit target has been set for inflation in 1991. However, this target path is consistent with a year-over-year increase in the CPI of about 5 per cent (less than 4 per cent excluding the impact of the GST) by the end of the year.

In the actions it takes to implement these targets, the Bank will, for practical reasons, focus on the consumer price index excluding the volatile food and energy components, as published by Statistics Canada. Even abstracting from these volatile elements, a good deal of variability remains in consumer price movements, and the targets should be regarded as the midpoints of a target band of plus or minus one percentage point. Over time, however, movements in the total CPI and the CPI excluding food and energy should be broadly similar.

The Bank will report from time to time on progress in relation to these targets, particularly in the Annual Report published each year under the Bank of Canada Act.

The Governor said that in order to keep to this course the Bank will be carefully monitoring the trend rates of expansion of money, credit and total spending to ensure they are consistent with the targets and will be adjusting its monetary policy actions accordingly. The intention in setting out explicit targets, however, is to encourage Canadians to base their economic decisions on this downward path for inflation so that the lower inflation will be more readily achieved, and this will contribute to lower interest rates.

The emphasis in these targets on reaching price stability reflects the importance for economic performance of ensuring that the confidence of Canadians in the value of money is not subject to chronic erosion by inflation. The economy will not operate fairly or to its full potential unless Canadians can have this confidence. The achievement of price stability will provide the sound monetary basis that is important for durable economic expansion.

The Bank will shortly make available further details on the implementation of the targets in a background technical note.