

# Monetary Policy Report Summary

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October 2013

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

## Highlights

- The global economy is expected to expand modestly in 2013, although the composition of growth is now slightly less favourable for Canada.
- In Canada, the Bank expects that a better balance between domestic and foreign demand will be achieved over time and that economic growth will become more self-sustaining. But this will take longer than previously projected.
- The Bank projects that the Canadian economy will grow by 1.6 per cent in 2013, 2.3 per cent in 2014, and 2.6 per cent in 2015, reaching full capacity around the end of 2015.
- Inflation remains subdued. With well-anchored expectations, both core and total CPI inflation are projected to return slowly to 2 per cent around the end of 2015.

The global economy is expected to expand modestly in 2013, although its near-term dynamic has changed and the composition of growth is now slightly less favourable for Canada. The U.S. economy is softer than expected but as fiscal headwinds dissipate and household deleveraging ends, growth should accelerate through 2014 and 2015. The nascent recovery in Europe, while modest, has surprised on the upside. China's economy is showing renewed momentum, while growth in a number of other emerging market economies has slowed as their financial conditions have tightened. Overall, the global economy is projected to grow by 2.8 per cent in 2013 and accelerate to 3.4 per cent in 2014 and 3.6 per cent in 2015.

In Canada, uncertain global and domestic economic conditions are delaying the pick-up in exports and business investment, leaving the level of economic activity lower than the Bank had been expecting. While household spending remains solid, slower growth of household credit and higher mortgage interest rates point to a gradual unwinding of household imbalances. The Bank expects that a better balance between domestic and foreign demand will be achieved over time and that growth will become more self-sustaining. Real GDP growth is projected to increase from 1.6 per cent in 2013 to 2.3 per cent in 2014 and 2.6 per cent in 2015. The Bank expects that the economy will return gradually to full production capacity, around the end of 2015.

Inflation in Canada has remained low in recent months, reflecting the significant slack in the economy, heightened competition in the retail sector, and other sector-specific factors. With larger and more persistent excess supply in the economy, both total CPI and core inflation are expected to return more gradually to 2 per cent, around the end of 2015.

The outlook for inflation is subject to several risks. The most important ones emanating from the external environment are the risks of stronger growth in advanced economies and a more protracted and difficult euro-area recovery. The most important domestic risks are weaker exports, a quicker rebound in confidence and business spending, and a disorderly unwinding of household sector imbalances.

Although the Bank considers the risks around its projected inflation path to be balanced, the fact that inflation has been persistently below target means that downside risks to inflation assume

increasing importance. However, the Bank must also take into consideration the risk of exacerbating already-elevated household imbalances. Weighing these considerations, the Bank judges that the substantial monetary policy stimulus currently in place remains appropriate and therefore has decided to maintain the target for the overnight rate at 1 per cent.

### Projection for global economic growth

	Share of real global GDP <sup>a</sup> (per cent)	Projected growth <sup>b</sup> (per cent)			
		2012	2013	2014	2015
United States	20	2.8 (2.2)	1.5 (1.7)	2.5 (3.1)	3.3 (3.2)
Euro area	14	-0.6 (-0.5)	-0.4 (-0.8)	1.0 (0.8)	1.3 (1.3)
Japan	5	2.0 (1.9)	1.8 (1.9)	1.5 (1.3)	1.0 (1.2)
China	15	7.7 (7.8)	7.7 (7.4)	7.4 (7.3)	7.2 (7.5)
Rest of the world	47	3.2 (3.1)	2.8 (2.9)	3.4 (3.6)	3.7 (3.8)
World	100	3.1 (3.0)	2.8 (2.8)	3.4 (3.5)	3.6 (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 July 2013 *Monetary Policy Report*.

Source: Bank of Canada

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

	2012	2013				2014				2015			
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real GDP (quarter-over-quarter percentage change at annual rates)	0.9 (0.9)	2.2 (2.5)	1.7 (1.0)	1.8 (3.8)	2.3 (2.5)	2.3 (2.7)	2.3 (2.8)	2.4 (2.8)	2.6 (2.8)	2.7 (2.8)	2.7 (2.5)	2.6 (2.4)	2.5 (2.2)
Real GDP (year-over-year percentage change)	1.0 (1.0)	1.4 (1.4)	1.4 (1.3)	1.7 (2.1)	2.0 (2.4)	2.0 (2.5)	2.2 (2.9)	2.4 (2.7)	2.4 (2.8)	2.5 (2.8)	2.6 (2.7)	2.7 (2.6)	2.7 (2.5)
Core inflation (year-over-year percentage change)	1.2 (1.2)	1.3 (1.3)	1.2 (1.1)	1.3 (1.3)	1.4 (1.6)	1.3 (1.5)	1.5 (1.7)	1.6 (1.8)	1.7 (1.9)	1.8 (1.9)	1.9 (2.0)	1.9 (2.0)	2.0 (2.0)
Total CPI (year-over-year percentage change)	1.0 (1.0)	0.9 (0.9)	0.7 (0.7)	1.1 (1.1)	1.3 (1.4)	1.2 (1.4)	1.4 (1.6)	1.6 (1.8)	1.7 (1.9)	1.8 (1.9)	1.9 (2.0)	1.9 (2.0)	2.0 (2.0)
Total CPI excluding the effect of the HST and changes in other indirect taxes (year-over-year percentage change)	0.8 (0.8)	0.9 (0.9)	0.8 (0.8)	1.2 (1.2)	1.4 (1.5)	1.3 (1.5)	1.4 (1.6)	1.6 (1.8)	1.7 (1.9)	1.8 (1.9)	1.9 (2.0)	1.9 (2.0)	2.0 (2.0)
WTI <sup>b</sup> (level)	88 (88)	94 (94)	94 (94)	106 (103)	102 (100)	101 (97)	99 (94)	97 (93)	95 (91)	93 (90)	91 (88)	90 (87)	88 (86)
Brent <sup>b</sup> (level)	110 (110)	113 (113)	103 (103)	110 (106)	110 (105)	108 (103)	107 (102)	105 (100)	104 (99)	102 (98)	100 (96)	99 (95)	98 (94)

a. Figures in parentheses are from the projection in the July 2013 *Monetary Policy Report*.

b. Assumptions for the price of West Texas Intermediate and Brent crude oil (US\$ per barrel) are based on an average of futures contracts over the two weeks ending 18 October 2013.

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