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CONTACT: Jeremy Harrison
613 782-8782

Perceptions of Low Rates Raise Risks,
Bank of Canada Governor Mark Carney Says

TORONTO, Ontario – Cyclical and structural factors have led to a low-interest-rate environment, Bank of Canada Governor Mark Carney said today in a speech that reviewed the implications of such an environment for financial stability and economic growth in Canada and globally. "Very low policy rates in the major advanced economies could be in place for a prolonged period—a possibility underscored by the recent extensions of unconventional monetary policies in the United States, Japan and Europe," he said.

"The crisis is not over, but has merely entered a new phase," Governor Carney told the Economic Club of Canada. "In a world awash with debt, repairing the balance sheets of banks, households and countries will take years. As a consequence, the pace, pattern and variability of global economic growth is changing, and Canada must adapt."

A wrenching adjustment to global demand that is already under way and the impact it is having on the international monetary system are reinforcing the low-interest-rate strategies of major advanced economies, the Governor said, adding that further rounds of quantitative easing may be required.

The Governor reviewed the implications of this trend for countries caught in the middle, like Canada, covering three aspects:

- the effect of the second round of quantitative easing in the United States;
- the implications for Canadian monetary policy; and
- the potential financial stability implications of "low for long" interest rates.

Interest rates at low levels for a long period of time could potentially distort behaviour in the public, financial, corporate and household sectors, the Governor noted. "Experience suggests that prolonged periods of unusually low rates can cloud assessments of financial risks, induce a search for yield, and delay balance sheet adjustments," he said.

The Governor cautioned that "low rates today do not necessarily mean low rates tomorrow. Risk reversals when they happen can be fierce: the greater the complacency, the more brutal the reckoning."

In conclusion, Governor Carney suggested several lines of defence and, above all, urged individuals, companies, market participants and others to resist complacency. "Cheap money is not a long-term growth strategy," he said. "Monetary policy will continue to be set to achieve the inflation target. Our institutions should not be lulled into a false sense of security due to low current rates."