

# Monetary Policy Report Summary

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July 2013

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

## Highlights

- Global economic growth remains modest. Although the Bank has downgraded slightly its global growth forecast, the global economy is still expected to pick up in 2014 and 2015.
- Economic growth in Canada is expected to be choppy in the near term. The economy is expected to reach full capacity around mid-2015, as projected in April.
- The Bank projects that the Canadian economy will grow by 1.8 per cent in 2013 and 2.7 per cent in both 2014 and 2015.
- Inflation has been low in recent months and is expected to remain subdued in the near term. Both core and total CPI inflation are expected to return to 2 per cent around mid-2015.

Global economic growth remains modest, although the pace of economic activity varies significantly across the major economies. The U.S. economic expansion is proceeding at a moderate pace, with the continued strengthening in private demand being partly offset by the impact of fiscal consolidation. In Japan, fiscal and monetary policy stimulus is contributing to a rapid recovery in economic growth. In contrast, economic activity in the euro area remains weak. While stronger than in the advanced economies, real GDP growth in China and other emerging market economies has slowed, exerting downward pressure on global commodity prices and, as a consequence, the Bank has downgraded slightly its global growth forecast. The global economy is still expected to pick up in 2014 and 2015.

In Canada, economic growth is expected to be choppy in the near term, owing to unusual temporary factors, although the overall outlook is little changed from the Bank's projection in April. Annual GDP growth is projected to average 1.8 per cent in 2013 and 2.7 per cent in both 2014 and 2015, supported by very accommodative financial conditions. Despite ongoing competitiveness challenges, exports are projected to gather momentum, which should boost confidence and lead to increasingly solid growth in business investment. The economy will also be supported by continued growth in consumer spending, while further modest declines in residential investment are expected. Growth in real GDP is projected to be sufficient to absorb the current material excess capacity in the economy, closing the output gap around mid-2015, as projected in April.

Inflation has been low in recent months and is expected to remain subdued in the near term. The weakness in core inflation reflects persistent material excess capacity, heightened competitive pressures on retailers, relatively subdued wage increases, and some temporary sector-specific factors. Total CPI inflation has also been restrained by declining mortgage interest costs. As the economy gradually returns to full capacity and with inflation expectations well-anchored, both core and total CPI inflation are expected to return to 2 per cent around mid-2015.

The outlook balances the many upside and downside risks to inflation. Three of the most important emanate from the external environment, and include the risks of stronger U.S. private

demand, a failure to contain the crisis in Europe, and weaker growth in China and other emerging-market economies. The most important domestic source of risk to the Canadian economy remains the possibility of a disorderly unwinding of household sector imbalances.

Against this backdrop, on 17 July, the Bank decided to maintain the target for the overnight rate at 1 per cent. As long as there is significant slack in the Canadian economy, the inflation outlook remains muted, and imbalances in the household sector continue to evolve constructively, the considerable monetary policy stimulus currently in place will remain appropriate. Over time, as the normalization of these conditions unfolds, a gradual normalization of policy interest rates can also be expected, consistent with achieving the 2 per cent inflation target.

### 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	19	2.2 (2.2)	1.7 (2.0)	3.1 (3.1)	3.2 (3.3)
Euro area	14	-0.5 (-0.5)	-0.8 (-0.6)	0.8 (0.8)	1.3 (1.4)
Japan	6	1.9 (2.0)	1.9 (1.4)	1.3 (1.6)	1.2 (1.4)
China	15	7.8 (7.8)	7.4 (7.7)	7.3 (7.6)	7.5 (7.7)
Rest of the world	47	3.1 (3.1)	2.9 (3.2)	3.6 (3.7)	3.8 (3.9)
World	100	3.0 (3.0)	2.8 (3.0)	3.5 (3.6)	3.7 (3.8)

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*, April 2013

b. Numbers in parentheses are projections used for the April 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
<b>Real GDP (quarter-over-quarter percentage change at annual rates)</b>	0.9 (0.6)	2.5 (1.5)	1.0 (1.8)	3.8 (2.3)	2.5 (2.8)	2.7 (3.0)	2.8 (3.0)	2.8 (3.0)	2.8 (2.8)	2.8 (2.8)	2.5 (2.5)	2.4 (2.3)	2.2 (2.1)
<b>Real GDP (year-over-year percentage change)</b>	1.0 (1.1)	1.4 (1.2)	1.3 (1.2)	2.1 (1.6)	2.4 (2.1)	2.5 (2.5)	2.9 (2.8)	2.7 (2.9)	2.8 (2.9)	2.8 (2.9)	2.7 (2.8)	2.6 (2.6)	2.5 (2.4)
<b>Core inflation (year-over-year percentage change)</b>	1.2 (1.2)	1.3 (1.3)	1.1 (1.2)	1.3 (1.4)	1.6 (1.7)	1.5 (1.7)	1.7 (1.8)	1.8 (1.9)	1.9 (1.9)	1.9 (1.9)	2.0 (2.0)	2.0 (2.0)	2.0 (2.0)
<b>Total CPI (year-over-year percentage change)</b>	1.0 (1.0)	0.9 (0.9)	0.7 (1.0)	1.1 (1.2)	1.4 (1.6)	1.4 (1.6)	1.6 (1.7)	1.8 (1.9)	1.9 (1.9)	1.9 (1.9)	2.0 (2.0)	2.0 (2.0)	2.0 (2.0)
<b>Total CPI excluding the effect of the HST and changes in other indirect taxes (year-over-year percentage change)</b>	0.8 (0.8)	0.9 (0.9)	0.8 (1.1)	1.2 (1.3)	1.5 (1.7)	1.5 (1.7)	1.6 (1.7)	1.8 (1.9)	1.9 (1.9)	1.9 (1.9)	2.0 (2.0)	2.0 (2.0)	2.0 (2.0)
<b>WTI<sup>b</sup> (level)</b>	88 (88)	94 (94)	94 (94)	103 (95)	100 (94)	97 (93)	94 (92)	93 (91)	91 (90)	90 (90)	88 (89)	87 (88)	86 (88)
<b>Brent<sup>b</sup> (level)</b>	110 (110)	113 (113)	103 (106)	106 (106)	105 (104)	103 (103)	102 (102)	100 (101)	99 (100)	98 (99)	96 (98)	95 (97)	94 (96)

a. Figures in parentheses are from the projection in the April 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 12 July 2013.

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