Opening Statement by
Gordon Thiessen
Governor of the Bank of Canada
before the House of Commons
Standing Committee on Finance
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Mr. Chairman, my colleagues and I welcome these appearances before your committee following each edition of the Bank of Canada's *Monetary Policy Report*. As you know, we published our latest report yesterday. It touches on a wide range of economic and monetary issues and provides an opportunity for us to account for our policy actions and the results of those actions.

It is important to keep in mind that the objective of monetary policy is to help create and maintain a Canadian monetary climate favourable for improved economic performance over the long haul. The best way for monetary policy to make this contribution is to preserve low and stable inflation. As set out in the jointly agreed inflation-control target of the Bank of Canada and the government, our objective is to keep inflation within a range of 1 to 3 per cent.

In our previous report in May, we highlighted the global economic uncertainties that shrouded the economic outlook. Since that time, economic uncertainties have further intensified. While some stability returned to Asia, instability spread to other regions during the summer, following further evidence of Japan's inability to deal with its problems and Russia's decision to declare a debt moratorium. Many emerging markets were faced with large capital outflows and widening interest rate spreads as investors looked for safe havens. More broadly, spreads between private sector and government bonds also increased, and market liquidity fell.

Throughout this period the conduct of monetary policy has been influenced by these international factors. Problems in Asia and Russia have contributed to a sharp decline in the prices of the commodities we export. The difficulties this has caused in our primary industries were the source of ongoing downward pressure on the Canadian dollar during the summer. In August, financial markets became extremely nervous and uncertain. The Canadian dollar came under intense downward pressure and our medium- and longer-term interest rates began to rise sharply. To forestall a potential loss of confidence in our currency, the Bank of Canada raised its Bank Rate by one percentage point. Subsequently, the Canadian dollar stabilized and medium- and longer-term rates came back down.

In response to the difficult and illiquid financial markets between August and October and some signs of a possible ‘‘credit crunch’’ the U.S. Federal Reserve lowered its interest rate twice by a total of 50 basis points. Because of the importance of the U.S. economy to Canada, and given our ongoing low inflation rate, the Bank of Canada followed these moves with similar reductions in our Bank Rate. Since then, international financial markets have been less volatile.

Looking forward, the economic and financial upheavals in the international area have resulted in downward revisions to the estimates for global economic growth in 1998 and 1999. Nevertheless, economic activity in the major industrial countries, particularly in North America and Europe, is expected to be reasonably well sustained through to the end of 1999.

The Canadian economy is expected to continue expanding over the next year on the basis of the projected sustained domestic demand in the United States and accommodative monetary conditions in Canada. However, the turbulent international developments have created greater-than-usual uncertainty around the economic outlook.

Financial stability is particularly important to household and business confidence. Thus the extent to which growth in Canada’s economy will take up slack over the next year will depend on how quickly international and domestic financial markets stabilize. Preserving confidence among investors in Canadian financial markets will therefore be an important consideration for the Bank over the near term. And I welcome the greater stability we have seen in financial markets in recent weeks.

Let me reaffirm that the fundamental focus of monetary policy over the medium term continues to be on keeping inflation within the target range. Inflation is expected to remain in the lower half of the range of 1 to 3 per cent over the next year.

I will conclude by underlining that the global situation continues to be uncertain and that this will have an effect on Canada. However, we are coping with these international difficulties on this occasion better than before. I believe that is because of the progress we have made in recent years in getting our fiscal house in order, achieving a low and more stable rate of inflation and restructuring our private sector to make it more productive and internationally competitive.