



BANK OF CANADA

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**Bank of Canada releases its semi-annual *Monetary Policy Report***

The Bank of Canada today released its eleventh *Monetary Policy Report* in which it discusses economic and financial trends in the context of Canada's inflation-control strategy. The *Monetary Policy Report* is published every May and November.

In this issue of the *Report*, the Bank notes that the Canadian economy outperformed expectations since last November. Bolstered by vigorous external and domestic demand, Canada's economic expansion strengthened in the second half of 1999 and into early 2000. The trend of inflation in Canada was lower than expected over the past six months and has remained among the lowest in the industrial countries.

The Canadian economy has benefited from greater-than-anticipated strength in the global economy. The strong momentum and high levels of activity in the U.S. economy have also carried into this year, a situation that continues to pose a potential inflation risk. Emerging-market economies have enjoyed significantly stronger-than-expected growth, and prospects are generally bright for 2000. The outlook for Japan remains far more uncertain. In Europe, continued solid growth is expected through the year.

The buoyant U.S. picture, combined with Canada's high levels of business investment and solid employment gains, augurs well for continued strong growth in Canada. Given the strong momentum of demand, the Bank of Canada has raised its projection for growth in 2000 to a range of 4 to 4.5 per cent. At this pace, capacity pressures will likely intensify in 2000 and, as a result, the core rate of inflation is expected to rise gradually to close to the middle of the Bank's 1 to 3 per cent inflation-control target range. To keep the core inflation rate steady near 2 per cent, some deceleration in Canada's economic expansion or a more rapid expansion of productivity and of production capacity would be required during 2001.

The main risks to this outcome are the possibility of continued stronger-than-expected momentum of aggregate demand both from the U.S. economy and from domestic spending, and the possibility of a buildup of inflationary pressures in the United States spilling over into Canada. While capacity output may be also higher than expected, the Bank is taking a cautious approach to projecting potential output growth.

The challenge for monetary policy will be to carefully assess the balance between aggregate demand and supply in the economy, and to adjust monetary conditions in a timely manner. By keeping inflation low, the Bank can work to ensure the viability of the economic expansion in Canada.