Tiff Macklem: Release of the Monetary Policy Report

Opening statement by Mr Tiff Macklem, Governor of the Bank of Canada and Ms Carolyn Rogers, Senior Deputy Governor of the Bank of Canada, at the press conference following the monetary policy decision, Ottawa, Ontario, 29 January 2025.

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Good morning. I'm pleased to be here with Senior Deputy Governor Carolyn Rogers to discuss our policy decision and the *Monetary Policy Report* (MPR).

Today, we lowered the policy interest rate by 25 basis points. This is our sixth consecutive decrease and brings our policy rate to 3%.

We also announced our plan to complete the normalization of our balance sheet, ending quantitative tightening. The Bank will restart asset purchases in early March, beginning gradually so that its balance sheet stabilizes this year and then begins to grow modestly in line with economic growth.

We have three main messages this morning.

First, inflation has been close to the 2% target since last summer. Monetary policy has worked to restore price stability.

Second, lower interest rates are boosting household spending, and economic activity is picking up.

Third, the potential for a trade conflict triggered by new US tariffs on Canadian exports is a major uncertainty. This could be very disruptive to the Canadian economy and is clouding the economic outlook.

Since the scope and duration of a possible trade conflict are impossible to predict, the MPR projection we published today provides a baseline forecast in the absence of tariffs. We also provide some discussion of the potential consequences of a major trade conflict.

Let me expand on the first two messages before turning to the threat of tariffs.

First, inflation. A year ago, inflation was 3%, short-term expectations were still elevated and inflationary pressures were broader than normal. In recent months, inflation has remained close to 2%, business and consumer expectations have largely normalized and there is no longer evidence of broad-based inflationary pressures. Shelter price inflation remains elevated, but it is gradually coming down.

While we expect some volatility in CPI inflation due to temporary tax measures, our forecast is that inflation will remain close to the 2% target over the next two years.

Second, growth. There are signs economic activity is gaining momentum as past interest rate cuts work their way through the economy. Lower borrowing costs are boosting activity in the housing market as well as consumer spending on big-ticket

items like automobiles. The pickup in household spending is starting to broaden to other consumer items and is projected to strengthen further. Business investment has been weak, but is forecast to increase gradually. And the outlook for exports is being supported by new export capacity for oil and gas.

Employment has strengthened in recent months. But with job creation having lagged labour force growth for more than a year, the labour market remains soft. The unemployment rate was 6.7% in December, and wage pressures, which have proven sticky, are showing some signs of easing.

The Bank forecasts GDP growth will strengthen from 1.3% in 2024 to 1.8% in 2025 and 2026. Growth in GDP per person is projected to pick up as lower interest rates and rising incomes support spending. The projected increase in overall GDP growth is more modest than it was in October, largely due to lower population growth that reflects new federal immigration policies.

There are risks around our outlook, and Governing Council is equally concerned with inflation rising above the 2% target or falling below it. Absent the threat of tariffs, the risks to the inflation outlook are roughly balanced.

Let me turn now to the question of tariffs. US trade policy is a major source of uncertainty. There are many possible scenarios. We don't know what new tariffs will be imposed, when or how long they will last. We don't know the scope of retaliatory measures or what fiscal supports will be provided. And even when we know more about what is going to happen, it will still be difficult to be precise about the economic impacts because we have little experience with tariffs of the magnitude being proposed. Nevertheless, some things are clear.

A long-lasting and broad-based trade conflict would badly hurt economic activity in Canada. At the same time, the higher cost of imported goods will put direct upward pressure on inflation. The magnitude and timing of the impacts on output and inflation will depend importantly on how businesses and households in the United States and Canada adjust to higher import prices.

Unfortunately, tariffs mean economies simply work less efficiently-we produce and earn less than without tariffs. Monetary policy cannot offset this. What we can do is help the economy adjust. With inflation back around the 2% target, we are better positioned to be a source of economic stability. However, with a single instrument-our policy interest rate-we can't lean against weaker output and higher inflation at the same time. As we consider our monetary policy response, we will need to carefully assess the downward pressure on inflation from weakness in the economy, and weigh that against the upward pressure on inflation from higher input prices and supply chain disruptions.

So let me tell you what we're doing in preparation.

In recent years, we have invested in better information on supply chains, trade links and the connections between sectors. And this is helping us analyze the effects of supply disruptions including tariffs. We have begun assessing the possible consequences of different tariff scenarios, and present an example in this MPR.

We are stepping up our outreach activities across the country to hear directly from those affected by trade uncertainty. This includes augmenting our surveys of businesses and consumers to better understand how trade uncertainty is affecting their decisions and how they would cope in the event of a trade conflict.

We will update you on our analysis and assessments as developments unfold.

Having restored low inflation and reduced interest rates substantially, monetary policy is better positioned to help the economy adjust to new developments. As always, the Bank will be guided by our monetary policy framework and our commitment to maintain price stability over time.

With that, the Senior Deputy Governor and I would be pleased to take your questions.