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Bank of Canada Governor reviews Canada's experience with inflation targets and a flexible exchange rate

NEW YORK CITY, N.Y., February 20, 2002 — In a speech to the Canadian Society of New York, Bank of Canada Governor David Dodge said today that Canada's monetary policy framework, based on an explicit inflation-control target and a flexible exchange rate, "has contributed importantly to putting the Canadian economy back on the right path to longer-term prosperity."

The Governor said that, "a credible monetary policy requires a credible anchor." Inflation targets fulfill that role successfully " ... because they make inflation more predictable and firmly anchor inflation expectations well into the future." When expectations are solidly anchored "the real economy works better and is more stable."

Mr. Dodge went on to say that the Bank's focus on the 2 per cent midpoint of the target range underscores the symmetric feature of Canada's inflation-targeting system that "helps to smooth the peaks and valleys of the business cycle and to promote sound, and generally less variable, economic growth."

The Governor also highlighted the role of a flexible exchange rate in Canada's approach to monetary policy. "The inflation target and a floating exchange rate work well together—indeed, they reinforce each other," he said. "This approach has worked extraordinarily well for us over the last decade. And we expect that it will continue to provide the foundation for a prosperous future."

With respect to the short-term economic outlook, Mr. Dodge said that, with encouraging signs of a turnaround in the world economy and strengthening demand at home, "prospects for the Canadian economy are favourable."

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