Bank of Canada governor Stephen Poloz spoke today at Western University in Ontario on the topic of "reinventing central banking". Looking back through the history of central banking, Mr. Poloz suggested that we are at a new turning point, as inflation targeting alone has failed to ensure growth, by fostering financial stability risks. Low nominal interest rates resulted in increased leverage and risk tolerance, as well as debt-fuelled imbalances, the results of which are still being felt globally.

Governor Poloz also emphasized that low and stable inflation, and the matching low level of interest rates results in less room to maneuver (in terms of cutting interest rates) in the event of a significant negative shock. He further spoke to the risks that emerged via financial intermediation and the increasingly globally interconnected financial system.

As in past speeches, the Governor emphasized that he views monetary policy as an exercise in risk management, pointing to a number of trends, such as increased globalization and demographic shifts which have changed the way that monetary policy interacts with the domestic economy.

Key Implications

Today's speech was particularly important as it is the last public speech that will be made ahead of next week's Bank of Canada interest rate decision. Governor Poloz's emphasis on the financial stability risks of low interest rates, as well as the statement that "[the January rate cut] buys us some time to see how the economy actually responds", indicate that the Bank of Canada may choose to keep rates on hold at next week's meeting.

In addition to the Governor's comments today, crude oil prices have recovered somewhat recently, and are now closer to the level assumed by the Bank of Canada in the January MPR. As well, a number of key indicators will be released before the rate decision is made, including 2014Q4 GDP growth, and the January 2015 inflation figures, both of which are likely to impact the rate decision. On balance, it appears that a rate cut next Wednesday is not set in stone.

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