підвищення цінових очікувань споживачів; зниження доходів домогосподарств; формування ажіотажного попиту на товари першої необхідності. Саме тому питання розробки інструментів антиінфляційної політики є найбільш актуальним для сучасних економічних систем.

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A RISK MANAGEMENT APPROACH TO MONETARY POLICY

Introduction

Risk is an uncertainty about outcomes that can be either negative or positive. It cannot be never fully eliminated; it could be only managed prudently. Risk management is an important element in monetary policy. In recognition of the increased uncertainty, the Bank of Canada evaluates and assesses the most important risks, both positive and negative, and strives to balance them while making decisions about monetary policy.

Monetary Policy Formulation

The Bank of Canada’s mandate is to conduct monetary policy to promote the economic and financial well-being of Canadians. The best way to deliver on its mandate is to keep inflation low, stable and predictable. In 1991, the Bank adopted an inflation target and, since 1995, this target has been 2 per cent inflation. And, in more than two decades inflation has been very close to the target.

This has not happened by itself. The Bank sets the policy interest rate with the goal of achieving 2 per cent inflation target. Central to this decision is its view of the most likely path for the Canadian and global economies. However, economic projections are subject to considerable uncertainty and the forecasts represent ranges of likely outcomes.

Assessing Risk through two lenses

The Bank of Canada looks at risks through two lenses:

- the possible impact on the outlook for real economic activity and inflation, and
- the possible impact on the stability of the financial system.

Targeting inflation is informed by the work of economic forecasters who crunch the data and use models to assess the most likely future path of inflation. As inflation target is symmetric, the Bank cares about both the upside and downside risks to inflation. Canada’s inflation-targeting framework is flexible. Typically, the Bank seeks to return inflation to target over a horizon of six to eight quarters. However, the most appropriate horizon for returning inflation to target will vary depending on the nature and persistence of the shocks buffeting the economy. The Bank’s projection for inflation and its assessment of the risks around that projection are published quarterly in *Monetary Policy Report*.

Risks to financial stability are viewed through a separate lens. The Bank considers those that have the potential to disrupt or harm the financial system. Its primary objective is to determine the likelihood that they materialize and, if they were to occur, their impact on financial institutions and the functioning of markets. The Bank examines such risks in depth twice a year in *Financial System Review*.

These two sets of risks are related. The Bank of Canada considers the risks to economic stability and financial stability in an integrated fashion. Both are central complements to each other, not substitutes. The Bank is setting policy with a view to balancing the risks facing both the outlook for returning inflation sustainably to its target, and the risks to financial stability such as those posed by the indebtedness of Canadian households.

The sudden drop in global oil prices has increased both risks. The oil-price shock is an important setback in Canada's progress toward full capacity, full employment and stable inflation because it is a net negative for economic growth. And because lower oil prices mean lower Canadian income, the shock will worsen the debt-to-income ratio of Canadian households, thereby increasing financial stability risks.

The Bank's decision to lower the policy interest rate to 0.75% in January 2015 was intended to take out some insurance against both sets of risks. It gives a greater confidence to get back to full capacity and stable inflation by the end of 2016, and it will cushion the decline in income and employment, as well as the rise in the debt-to-income ratio, that lower oil prices will bring.

Credibility Counts

The Bank of Canada's flexible inflation-targeting framework gives the room to manoeuvre in the face of unusual shocks. This only works if expectations are well anchored: the public has to be confident that the Bank will get to the 2 per cent target. The Bank's commitment to the inflation target must remain credible.

Credibility is earned only through years of sound policy. Without it, low and stable inflation could only be achieved at considerable short-run cost to the economy. The Bank of Canada considers the credibility as an investment. By using credibility to exercise the framework's flexibility, it's working to maintain stable financial conditions that will support the expansion of capacity and return the economy to its full potential. As the process unfolds, there will be a future payoff of enhanced credibility.

Conclusion

The Bank of Canada looks at risks through two lenses. It's concerned with the big risks of runaway inflation and deflation and is acting to keep them remote. As financial stability is a necessary condition for low and stable inflation, it works in Canada and around the world to improve the resilience of the financial system.

Great lesson after crisis is that economic and financial stability are intrinsically linked, and the Bank is integrating the two in its analysis, research, and policy.

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