
Undertaking #37

CAC to indicate what length of historical data Ms. Sherry used for setting the adverse inflation assumptions.

RESPONSE:

I have extensive experience directing DCATS for two different private firms.

Rather than provide a response specific to the company I currently work for, I have chosen to provide a response reflective of my experience in private industry and my conversations with others from private firms.

It should be recognized that in private industry the DCAT analysis is focused on solvency issues rather than rate volatility.

Given the solvency concern and the desire to test extreme scenarios in the context of that concern DCATs often use 50 years of inflation data. The 99.7% probability level is commonly used in the adverse scenario.

A long inflation history (50 years) ignores significant improvements in anti-inflation (monetary) policy during this period, in particular the institution of inflation targeting in the 1990s. Inflation targeting has been associated with a long period of stable inflation that has settled around 2% per annum for a decade. The continuation of inflation targeting by the Bank of Canada suggests a continuation of relatively low inflation in the 1-3% band for the foreseeable future. The historical data should reflect this and be limited to 20-25 years.