

BANK OF CANADA

ADDRESS BY THE GOVERNOR AT THE THIRD ANNUAL GENERAL MEETING OF SHARE- HOLDERS OF THE BANK OF CANADA, FEBRUARY 22, 1938

As you will remember, under the Bank of Canada Act Amendment Act of June, 1936, we shall by 1940 have a Board composed of three Directors elected by Class "A" shareholders, and six Directors appointed by the holder of Class "B" shares. It is also provided that no Class "A" Director in office at the date of the coming into force of the amending Act shall be replaced so long as Class "A" shareholders are represented on the Board by three or more Directors. We have, I regret to say, lost two of the Class "A" Directors, Mr. R. J. Magor, who resigned in June last, and Mr. W. C. Woodward, whose term of office expires to-day. In accordance with the Act their places will not be filled.

The balance sheet of the Bank as at December 31st last, a copy of which was sent to all shareholders with the notice calling this meeting, shows that there have been certain material changes in the amount of our assets and liabilities during the course of 1937.

At the end of December, our note issue stood at \$165,330,405, an increase of \$29,594,948 on the year. The active circulation, that is, the amount of our notes in the hands of the public, increased by some \$23,558,000, while the notes of the chartered banks decreased by \$7,472,000. Thus the net active circulation rose by about \$16 millions. Using daily averages, the increase was \$18.2 millions, or 10 per cent, as compared with an increase of 7.2 per cent

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between 1935 and 1936. This reflects for the year 1937 as a whole a further increase in business activity and employment, a rise in prices, chiefly wholesale prices, and some increase in wages.

During the year, our investments increased on balance by \$25.8 millions, \$21 millions of which was in the short term category. The change in the amount of our investments, therefore, is of the same order of magnitude as that in the active circulation. The reserves of the chartered banks were increased on the year by \$15 millions, which can be accounted for as follows:—

(Millions of dollars)

	Changes producing a decrease in chartered banks' cash	Changes producing an increase in chartered banks' cash
Increase in sterling and U.S.A. funds		5.8
Increase in investments		25.8
Increase in active circulation	23.6	
Decrease in Dominion Government balances		7.7
Increase in other banks' balances	1.4	
Other net changes		.7
	25.0	40.0
	Deduct	25.0
		15.0
Increase in chartered banks' cash reserves (notes of and deposits with Bank of Canada)		15.0

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PROFIT AND LOSS ACCOUNT

In 1936, after providing for contingencies and reserves, we had available for distribution \$2,008,124. This year the comparable figure is about \$260,000 higher at \$2,268,596. Over the whole year, our investments have averaged about \$39 millions more than in 1936, but from the point of view of earnings, this factor was partially offset by a lowering of the average yield on our holdings of Treasury Bills.

You will remember that our loss on silver in 1935 was \$489,000, and in 1936 some \$135,000; I am glad to say that the loss in the current year has been only \$13,847, silver prices having been relatively stable during the period under review. We shall, of course, continue to value our silver according to the market price; consequently there is no assurance that we shall be immune from losses in the future.

BANK RATE

Bank Rate has remained unchanged throughout the year at 2½ per cent. As in 1936, cash has been plentiful, and no applications for advances or discounts have been received from the banks.

PREMISES

The construction of our new Head Office in Ottawa is being proceeded with rapidly, and we hope to move into it some time during April. Those of you who have seen the exterior will, I think, agree with me when I say that our associated architects, Messrs. Marani, Lawson & Morris and Mr. S. G. Davenport, have been singularly successful in producing a building which is at once simple and dignified, and, we believe, admirably suited to our purposes. I would like also to pay a tribute to the contractors and the workmen who, in the face of some difficulties, will have completed

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their task in scarcely more than a year. Work commenced on March 22nd, and the foundation stone was laid by the Prime Minister on August 10th last.

I referred last year to the inadequacy of our Toronto premises. The remodelling of the interior was completed during 1937, and our staff, who had been housed in temporary premises since the end of August, 1936, returned to Toronto Street in June, 1937.

We have also built an Agency in Regina. The new building was occupied in the middle of December last. We had been in provisional quarters for nearly eighteen months. In appearance, the general character of this Agency somewhat resembles that of our Head Office, though it is, of course, on a small scale. Finally, we have purchased our premises in Vancouver, and we have slightly enlarged our Montreal Agency. We feel that our building programme and its cost have been kept down to a minimum.

NEW BANK NOTES

The Bank of Canada Act Amendment Act, 1936, provided that, as soon as practicable after the coming into force of the Act, each note of the Bank should be printed in both the English and the French languages. The production of a high quality bank note is necessarily a lengthy and expensive process. Not only does it call for detailed engraving work by highly skilled plate engravers, but the printing processes, and the seasoning of the notes before they are ready for issue to the public, mean in all a lapse of a year from the time a new note issue is designed. Our new notes began to be issued in July last. I think the general opinion is that in design they are an improvement on the previous issue. When a change of this kind is first made, however,

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some inconvenience is bound to be felt by the public until they become familiar with the new notes and any risk of confusion with the old issue has been eliminated by its retirement from circulation.

In our new notes, a strongly distinctive colour has been used for each denomination. In the lower corners of the face of each note the amount is shown in words instead of figures. This is because words present greater difficulties than figures to anyone attempting to alter the note.

STATISTICAL SUMMARY

Our monthly Statistical Summary was first issued in January, 1937. Judging by the comments which we have received, this publication of the Bank has been found to be of considerable assistance to students, and more generally to all those who have occasion to seek information concerning the current development of the main items in the Canadian economy. Certain tables in the Summary appear every month, others come quarterly, half-yearly or annually. Occasionally there will be tables which are not periodical. There is a greater diversification in the charts. Naturally, in the first year there must be more new material than in any other year, but you may be interested to hear that during 1937 we published 59 different tables and 137 different graphs. We distribute the Summary free to a number of institutions and libraries, and any member of the public can obtain it on payment of a subscription of \$3 per annum. Annual binders are supplied at the cost of \$1 each.

TREASURY BILLS

The amount of Dominion Government Treasury Bills outstanding at the end of December, 1937, was \$150 millions, unchanged from the figures of December 31st, 1936. The

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weighted average tender rate during the year was .715 per cent for Bills of three months' currency. The rate ranged from .628 per cent on September 1st to .816 per cent on November 15th. The last offering of the year sold at .744 per cent.

Our holdings of Treasury Bills varied widely during the course of the year. An indication of the extent of these fluctuations is given by the figures of our weekly and month-end statements under the heading of "Dominion and Provincial Government short term securities", the bulk of which at the present time consists of Dominion Government Treasury Bills. Investments in the category to which I have referred rose from \$63.3 millions at the end of September to \$82.5 millions as at October 31st, and \$94.8 millions at November 30th. By December 31st, there was a reduction to \$82.3 millions.

There are two reasons for the increase in our security holdings during the closing months of each year. For one thing, it has been our policy to provide additional cash to offset the seasonal increase in the amount of notes in the hands of the public; and we have implemented this policy by the purchase of securities. The second reason is connected with the fact that this is the time of year when the chartered banks desire to build up their cash reserves. When year-end movements of this character are taking place, the short term investments of the Bank of Canada tend to rise, since the market for Treasury Bills and other short term securities would not be capable of absorbing the holdings which the chartered banks may desire to part with temporarily, unless support were given by the central bank. In the absence of such support, considerable and quite unnecessary dislocation in the capital market would result.

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SECURITY MARKETS

Soaring prices and speculative activity in stock and commodity markets in the spring of 1937, gave rise to the belief that there was bound to be a much heavier demand for credit, and that interest rates would move upwards. High grade bonds reflected this belief in a fall which brought the average price of two typical long term issues in Canada from a high of \$107.26 in January, 1937, to a low of \$101.22 in April. Since that time, the drastic decline in share values, and a reversal of the upward movement in commodity prices, have resulted in a change of attitude towards the gilt edged market. The two issues to which I have already referred sold at an average price of \$104.34 during January of this year. It will be noted that the recovery up to that time had not carried prices back to the level of the preceding January.

The movements of Government bond prices in the United Kingdom and the United States have been closely akin to those experienced in Canada.

There have been indications during the last six or eight months of an improvement in the demand for high grade bonds on the part of smaller investors throughout the country. With the object of promoting better distribution, the Dominion Government is allowing a longer period to elapse between the announcement of the offering of its new issues, either direct or guaranteed, and the opening of the books for receipt of subscriptions. This procedure gives small investors, particularly those who are distant from the large centres, a better chance of participating in a new issue. It can be understood, however, that the number of days during which it is practical to allow an offering to remain

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outstanding is limited, and that the limit may vary from time to time, depending on circumstances. I judge from comments which have been made that the change has been found helpful.

At the time of our last annual meeting, I referred to the growing volume of speculation on the stock markets, and to the steps taken by the leading Canadian Stock Exchanges to enforce a greater degree of conservatism by raising margin requirements. At the end of January, 1937, borrowings of members of the Toronto and Montreal Exchanges on Canadian collateral amounted to \$79.5 millions. They did not rise appreciably at any time during the year, the maximum month-end figure being \$82 millions in August. By December 31st, borrowings were reduced to \$45 millions.

It is, of course, the case that the figures of member borrowings do not give the complete story; bank loans to individuals against stocks and bonds must also be taken into consideration. During the twelve months which ended on October 31st, 1937, bank loans in this category rose from about \$111 millions to \$142 millions, an increase of approximately \$31 millions. Stock Exchange member borrowings decreased \$13 millions during the same period. The chartered banks' figures naturally include many loans which were made for business purposes and have no connection with speculative activities. Nevertheless, the published information leads one to suppose that reductions of clients' liabilities to brokers between October, 1936, and October, 1937, were offset by increased borrowings from banks, although it does not necessarily follow that the bank loans were to the same individuals who were reducing their commitments in brokerage accounts.

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The experience of the last two years shows again that there should be a careful scrutiny of the influence of credit facilities upon speculative buying, and evidences the desirability of prompt action when the first danger signals appear. I do not suggest that even the most conservative policy in regard to margins will ensure any degree of stability in prices: experience elsewhere has given proof to the contrary. But caution in the use of credit does mean that there is much less likelihood of those concerned finding themselves in extreme financial difficulties, with all that this involves in the way of an extended period of liquidation and damage to public confidence.

CANADIAN DOLLAR IN 1937

Turning to the foreign exchange situation, it should be noted that fluctuations of the Canadian dollar against both the United States dollar and sterling, were narrower even than in 1936. The entire range of fluctuations against the former was $37/64$ per cent as compared with $1\frac{1}{4}$ per cent in the preceding year. Against the pound sterling, the range of fluctuations was approximately $3-1/16$ per cent compared with 4 per cent in 1936.

The range in the sterling-U.S. dollar rate during the year was about $3\frac{1}{8}$ per cent. The volume of international trade which is conducted directly or indirectly, in terms of these currencies, is such that their relative stability during 1937 was a helpful factor of great importance, for which credit must be given to the operation of the Tripartite Agreement. Had there been no machinery of this kind in operation, it is probable—perhaps one might say certain—that the disturbing developments which have taken place from time to time during the past year, would have been quite sufficient to cause wide fluctuations in rates.

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BALANCE OF INTERNATIONAL PAYMENTS

Preliminary estimates of Canada's balance of international payments for 1937 show a reduction in our favourable balance on current account from \$324 millions in 1936, to \$217 millions. The drop of about \$100 millions occurs in the merchandise item, and is almost entirely attributable to a fall in the export of grain. This is partly due to the fact that the wheat crop last year was the smallest since 1914, and partly to the fact that in 1936 we were liquidating heavy wheat stocks.

After very favourable balances, such as we had in 1935 and 1936, one would, in any case, expect a tendency towards their reduction, even if our exports continued to grow, as they have done. On *a priori* and historical grounds, one would expect imports, after a certain time-lag, to increase more quickly than exports, as a recovery in business progresses; and by the same token, imports may be expected to decrease less quickly than exports in the early stages of a recession in business. It may be, however, that on the present occasion the decline in our exports will be reflected in a downward adjustment of imports more rapidly than usual. We had not reached the stage in our recovery where construction and capital development was taking place on a large scale, and it is the completion of projects of this kind which for a time keeps import figures relatively high, even after a recession in business has commenced.

In 1936, the net retirement of issues payable in currencies other than Canadian was in the neighbourhood of \$230 millions. In 1937, though continuing at a fairly high level during the first half of the year, it is estimated for the whole year at about \$155 millions. By the middle of 1937,

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the refunding operations conducted during the preceding two years had very greatly reduced the number of issues which could be called for redemption. Perhaps it is just as well that the movement has proceeded at a somewhat slower pace, keeping step with the reduced amount available from our balance of international payments. Any considerable reduction in our foreign debt must, in any case, take many years, in view of the magnitude of the task. Considering only Dominion and Provincial Governments' direct and guaranteed debt, and that of the Canadian National Railways, there is still \$1,307 millions payable abroad, and not only that, but an even larger total of debt—\$1,379 millions, to be exact—carries the option of payment in one or more foreign markets as well as in Canada. Our efforts should, of course, be directed first towards a reduction in such optional payment bonds. Certainly it is undesirable that any additions to this class of indebtedness should be made, from the point of view of the Canadian economy as a whole.

BUSINESS CONDITIONS

Had it not been for the disastrous drought which affected wide areas of the West, I believe that the volume of business in Canada last year would have risen above the 1926-29 level. In fact, however, the volume was probably somewhat lower than the 1926-29 average. Nevertheless, for the country as a whole, 1937 was a good year.

In view of what has happened during the last six months, we should not expect business activity in the first half of 1938 to compare favourably with the same period of last year. I think that the situation is pretty generally understood, and has been discounted in most people's minds. Their interest is, therefore, directed towards the probable

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course of events later in the year. It is well to recall that a satisfactory crop in western Canada should represent a distinct gain over 1937, both from a psychological and a material point of view. As regards general business, much depends upon the situation in the United States. That country and Great Britain are the two greatest markets in the world, purchasing some 30 per cent in value of all goods entering international trade in 1937. The stimulus which these countries have given to world recovery is indicated by the fact that retained imports by Great Britain during 1937 were about \$1,500 millions larger than in 1932, while U.S. statistics for the same years show that their imports increased by some \$1,759 millions. I should note that the import figures to which I have referred do not include purchases of gold and silver. If these were included, the proportion of world imports taken by Great Britain and the United States would probably be close to 33 per cent. Recovery in Great Britain started earlier than in the United States, and has been more extensive. It is not reasonable to count on fresh stimulus from that source, so that one must conclude that developments in the United States may have a decisive influence on the course of business elsewhere.

RELATIONS WITH PROVINCES

Last year I took occasion to define rather carefully the nature of the relationship which it is possible for the Bank of Canada to have with provincial governments. I have nothing to add to what I said on that occasion, except to refer to the three reports on the financial position of Manitoba, Saskatchewan and Alberta, which the Bank of Canada made last spring in response to invitations from the Premiers of these provinces and the Minister of Finance of the Dominion Government. The reports were made public

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on February 15th, March 15th and April 7th respectively, and copies can be obtained from the Head Office of the Bank.

In our reports, we expressed the opinion that the problems of the prairie provinces could not be dealt with in isolation. The difficulties which they face are not in all cases peculiar to the western economy, for some of them are being experienced in varying degree by other sections of the country. In these circumstances, we did not see any solution other than that which might be provided by a comprehensive enquiry into the financial powers and responsibilities of all our governing bodies.

A Royal Commission is now engaged on a re-examination of the economic and financial basis of Confederation. To quote in part from the Order in Council dealing with this matter, the Commissioners are asked to express what in their opinion will best effect a balanced relationship between the financial powers and the obligations and functions of each governing body, subject to the retention of the distribution of legislative powers essential to a proper carrying out of the federal system in harmony with national needs and the promotion of national unity. No study of this scope has ever before been attempted in Canada. The Commission's report may be expected to have a vital bearing on our affairs.

STAFF

In my last two annual speeches, I made no reference to a Staff Pension Fund. This was not because we had not given the matter consideration. We began to work on a scheme almost as soon as the Bank was established, but in our case some of the factors in any such scheme presented

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special difficulties. I am now glad to be able to call your attention to the fact that the Fund has been instituted, under By-laws which were approved by Order in Council, as required by our Act, on December 9th last, and were published in the Canada Gazette of December 18th.

The year has been a heavy one for the staff. In the last two years the number of permanent employees has only increased by six, or 2.8 per cent. It is difficult to establish with absolute accuracy the expansion in the Bank's activities over the same period, but, having reference to routine items only, I would estimate the increase to be from 15 to 20 per cent.

In September, we temporarily lost the services of the Chief of our Research Department, who was appointed Secretary to the Royal Commission on Dominion-Provincial Financial Relations. We cannot expect that he will be able to return to us for some time yet.

As I have indicated on previous occasions, we have reason to be highly satisfied with the work of our staff colleagues, both in their day to day routine and during times of extra strain.

NOTE: The report of the proceedings of the Annual Meeting of the Shareholders of the Bank of Canada can be obtained from the Head Office of the Bank or from any of its Agencies.