

Bank of Canada

INTER-OFFICE
CORRESPONDENCE

September 3rd, 1948

To Mr. J. R. Beattie

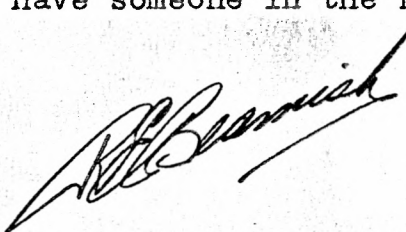
From Royd Beamish

Subject Governor's Vancouver Address

Deal with one subject only. All communications must be signed. Use single spacing for lengthy communications

Mr. Richardson is in Montreal today but before leaving he asked me to pass this fourth draft of the Governor's address to you for further checking. A change is to be made on Page 3, to be based on Mr. Abbott's press statement issued at the time of the market changes at the beginning of the year.

On Pages 5, 6 and 7 there are blanks to be filled in with correct figures. It would be appreciated if you could have someone in the Research Department obtain these.



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GSW Please check figures at bottom of P. 6
" insert nec. figures on p. 7

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Fourth Draft of Vancouver Remarks

I recall that just twelve years ago this month I had the pleasure of speaking to a luncheon meeting ⁱⁿ ~~of the~~ Vancouver ~~Board of Trade~~. The subject of my remarks on that occasion was a very new institution called the Bank of Canada. ^(A) I tried to explain the reasons why the Bank had been created, and to tell something of its objectives and the way in which it would go about its tasks. A great deal has happened in the twelve turbulent and eventful years since 1936. It seems appropriate that I should take this opportunity to say something about what the Bank of Canada has been doing during these years, and add such thoughts on general matters as occur to me at this time.

Pau
(B) → The best way to begin might be to hark back to 1935 when the Bank was created. It will be recalled that Canada was then struggling out of the depression which commenced in 1930. I believe that the decision to have a central bank was materially accelerated by the depression, although I am equally convinced that Canada would have taken this step in due course in any event. It is, I think, fortunate that action to create a central bank was not longer delayed. Although no central bank can by itself prevent a depression if major forces are operating to bring about such a state of affairs, it can ^{provide a} ~~ease the~~ monetary ^{flexibility} ~~rigidity~~ which would have become more and more ^{desirable} ~~urgent~~ as Canada struggled towards recovery in the years following 1934. Moreover, we had a short enough time in all conscience to get ready for the problems which the war brought.

Although there were at the outset some ^{conflict} ~~differences~~ of opinion in regard to the necessity for a central bank in Canada, the events of the last thirteen years have, I think, produced unanimous agreement that this piece of machinery is essential, although there can always be differences of ^{view} ~~opinion~~ in regard to the policies which should be pursued.

The broad policies that have been followed can be considered in relation to three periods of time. The first period would include the years commencing with the creation of the Bank until the beginning of the war. The second period would span the war years and include those early post-war months when

the heaviest demobilization expenses were being met. The third period would embrace our post-war experience.

Between 1935 and the commencement of the war, the Bank each year consistently followed a policy which ensured a moderate increase in the cash reserves of the chartered banks...and thus an increase in the money supply. An increase in production and employment was taking place during that time, but unemployment still remained a serious problem. Our action helped to bring down interest rates, ^{and} to facilitate new issues of securities and ~~made to make~~ ^{to} possible a more liberal attitude on the part of banks, to the extent that they could find suitable borrowers. In this way, we endeavoured, so far as it lay in our power, to remove barriers to recovery which might lie in the financial field.

During the second period, the necessities of war overrode all other considerations so far as the central bank was concerned. During such a time, the best that can be hoped for from a financial point of view is that war expenses will be covered so far as possible by taxation, and the deficit, so far as humanly possible, by voluntary saving on the part of the people. I believe that the general view is...and it is certainly a view which I hold...that the Canadian people did as much in the way of payment of taxes and voluntary saving during the war as anyone could have expected... more than most other countries. What they accomplished in these fields did not, however, fully cover the financing of our long and intensive war effort. Hence, the necessity for an extension of bank credit and money supply perhaps even beyond the point justified by the increase in production. This necessity the Bank had to recognize in framing its policy.

I come now to the post-war period...assuming this to begin after the heavier costs of dismantling the war machine had been met. This has been the period of most substantial increases in prices and cost of living.

So far as our prices depend on prices in other countries,

notably the United States...and they depend very heavily on these external factors...the central bank could obviously not prevent price increase in Canada. Theoretically, it might be done by raising the exchange rate of the Canadian dollar above parity with the U.S. dollar. But I believe that the practical limit to such a policy was reached in July of 1946 when the rate was raised to parity.

If the inflationary fires were being fanned by a heavy speculation in inventories or securities, the central bank could have made a contribution to stability by preventing or working against such developments. In fact, these have not been present in any significant way in the post-war period.

Finally, to the extent that price increases were being promoted by capital development being undertaken on a scale which outran available supplies of labour and material, the central bank might take action in two different ways...one of which we have done...and one of which we have not.

Minister's statement

The policy which we have not followed is to encourage a material increase in interest rates in order to discourage new capital investment by making it more expensive. ~~Although~~ we have not felt it necessary at this time to assume the full costs which would be entailed in a complete disregard of present tendencies in interest rates. ^{and} I believe that any moderate increase in interest rates would have little or no effect if people feel it is profitable to go ahead with their plans. A really substantial increase might have an effect, particularly as it would have repercussions which would tend to develop a "fear" mentality. But what should be desired is some tapering off in new capital investment, not a major downward change. Action which produces really drastic results in this field must be compared to throwing the baby out with the bath water.

With these things in mind, the central bank has suggested to the chartered banks that financing of new capital development by means of bank borrowing is most undesirable under

existing conditions. One should relate this to other steps that have been taken which will tend to prevent an overall increase in money supply, or, if that proves impossible, to keep the increase down to the lowest practicable amount. I refer to such things as the retirement of government debt ~~which has been the result of~~ ^{the need by the banks}.

I have now discussed all too briefly the broad outlines of central bank policy during the last thirteen years. Before going on to other matters, may I turn for a moment to an institution which is even newer than the comparatively new Bank of Canada...the Industrial Development Bank. This organization was created in 1944 as a result of the feeling of Government and Parliament that there was a certain gap in our financial system, particularly so far as small and medium sized industries were concerned. It was known that the financial requirements of such industries were not usually large enough to make public issue of securities a practical means of meeting them. Commercial banks, ~~particularly at that time~~ ^{up to that} had not been in the habit of financing capital development by making loans repayable over a considerable term of years; and insurance companies, for good and sufficient reasons, were not keen to take mortgages on small factories. Finally, while individuals might be able to get together a reasonable amount of money to purchase stock and thus to ~~finance~~ ^{provide the equity money for} a new concern or the expansion of an existing one, they might have great difficulty in laying their hands on the remaining amount needed.

These are the reasons which underlay the origination of the Industrial Development Bank. It was not intended to compete with other lenders. It was restricted to industrial enterprise because these are the ones in which financing of capital assets in the forms of building and machinery is normally most important; and it was directed in the main to assist small or medium sized enterprises. ~~as will be evident from the legal limitation on the amount of loans which it may make in excess of \$200,000.~~

in Account Times

Although it goes without saying that, ~~latterly~~ the Industrial Development Bank has followed a relatively conservative policy, *because of existing conditions,* it is worth noting that since the commencement of operations a little less than four years ago, the Bank has authorized credits for a total amount of \$. . . Its commitments outstanding at the present time are \$. . . You will see that these figures are not large. What I regard as more important, however, is the number of enterprises which have been assisted. That number is . . . It seems to me of some importance, to put it mildly, that *on reasonable terms* concerns who would not otherwise have been able to obtain financing, have been able to go ahead with their plans during this period of a little less than four years.

It is heartening to see the number of concerns which have already met with success, although I fully realize that the business climate has been abnormally favourable. Even so, I believe it is a good thing that ~~the men or~~ men who are trying to build up a business from a modest beginning should find encouragement for their spirit of enterprise, within the limits of financial reason.

From what I have said of the operations of the Bank of Canada and of the Industrial Development Bank, it will be seen that we have experienced an unusual variety of problems and challenges within the span of a relatively few years.

This, I think, is also typical of the experience of many enterprises in this country and is a reflection of the growth and

Country - dr - age
~~growth~~ of our economy, *this "country - dr - age" is* in part the result of ~~relatively~~ gradual *production methods and capacity* ~~underlying~~ changes in technology and productivity, ~~in part~~ arising *to a great extent* from the extreme pressure of war ~~production~~ *needs* and, more recently, associated with rapid growth in our population from natural increase and from immigration. In 1935 our population was 10.8

millions, to-day it is 12.9 millions, an increase of nearly one-fifth. In 1935 we had ^{probably over} ~~possibly~~ a million unemployed, to-day we have less than 100,000. ^{The number of people} In 1935 ~~a million and a half people~~ ^{is about double} ~~have been~~ at work in industry and ^{service trades} ~~the services~~, to-day the number ^{is about double} ~~is about double~~. Not only have we more hands at work but every where these hands are using better tools to make more goods with less effort. In agriculture the greatly increased production of war and postwar years has been possible with fewer workers than before the war, and in industry the reconversion of wartime productive facilities plus the enormous investment boom of the last three years, are beginning to add to the productivity of the increased labour force.

It is difficult to reduce all the developments to a single figure but I think the physical volume of our national output must be ^{about} ~~nearly~~ twice what it was in 1935. This is a measure of the recovery and progress we were able to achieve in 13 years, ^{Part of this} ~~but~~ if we look again we will see that there have been some rather special and somewhat disturbing developments associated with this spectacular recovery. ^{One of these} ~~The principal~~ special factor ^{is} that 1935 was a year of quite pronounced depression, that we now have full employment and that, consequently, further improvement ^{as a result of} ~~resting on~~ further absorption of unemployed workers cannot be expected. The chief disturbing development is the ^{weakness} ~~vulnerability~~ of our principal foreign markets and our continued dependence on expedients such as our loans to the United Kingdom and, more recently, the European Recovery Plan.

It should not escape our attention that our present prosperity and high level of employment has been sustained and indeed made possible by a tremendous increase in the volume of our exports. Whereas in 1935 the dollar value of our exports of merchandise was \$ 738 millions, in 1947 it reached a figure of \$ 2812 millions. It will be recalled that for a long period before the war the traditional pattern of our foreign trade was one which involved a substantial surplus in our dealings with

the U.K. and Western Europe, and a deficit in our dealings with the United States. We used our net cash receipts from our overseas customers to cover our U.S. dollar deficit. That pattern has not changed, although the volume of business is greater than ever before. Since the war, we have had tremendous surpluses in our dealings with Europe, amounting to \$ since (date) and equally large deficits in our trade with the United States in the same period of \$.

It may well be asked how the war-torn countries of Europe have been able to finance such a large excess of imports from Canada. In part they have done so by means of Canadian extension of credit. But a very substantial proportion of their obligations to us have been paid in gold or U.S. dollars. For a time they drew on their gold and foreign exchange reserves to make these payments. To-day, with their resources of this kind reduced to minimum levels, they are enabled to carry on through the operation of the European Recovery Programme. Only the receipts which we get in this way enable us to maintain our present level of imports from the U.S., which, in spite of the Canadian import control programme, are still running at an annual rate of \$.

Just a word in regard to the European Recovery Programme, which was authorized by the Congress of the United States early this year. I think it can be described as the greatest measure of international co-operation ever to be adopted in peace time. It offers hope for those who believe that self-interest and humanitarianism are in the main inseparable - and proof that this idea can command the active support of a large number of people. The programme did not come into being from economic logic alone, but also as the outcome of threats and political possibilities which a democratic people simply could not tolerate. It does not deprecate the farsightedness of the Plan to acknowledge this fact at the same time as one recognizes that this is a great economic adventure inspired by imagination and intelligence.

Too much emphasis cannot be given to the unprecedented

size and complexity of the problems faced by ECA, the organization which has been formed to implement the ERP. Having this in mind, as well as the fact that ECA has ^{not more than} ~~at the most~~ four years to run, it would be a courageous man indeed who would venture at this stage to predict the situation in which the U.K. and Western European countries will find themselves when the Programme comes to an end. Will they be in a position through their dealings with other countries of the world to finance a substantial excess of imports from Canada and thus enable us to preserve the traditional pattern of our foreign trade? I do not pretend to know the answer to this question, but the uncertainties are quite sufficient to warrant anxious consideration of this problem by Canadians. We have been fortunate up to now...we must not be led to assume that good fortune is perennial.

Now let me touch on one or two other matters which claim our attention at this time. As if the possibility of new patterns in our foreign trade were not enough, we find ourselves for the first time in our history physically "on the spot" between two great powers who would be opposed in the event of future conflict. (We also know in advance with which of those powers we should align ourselves in the event of such an unhappy development.) This thrusts upon us a vital role in world strategy, which we dare not ignore for a moment in our contemplation of other problems. It clothes the geography of our vast country with a new meaning and a new perplexity. It makes demands upon our economy and introduces stresses we could well afford to do without.

In addition to our concern with developments in world strategy, we realize that we are becoming more and more exposed to changes of technique in production and manufacturing. We know that the forced draught of war stimulates technological change and that some changes are already evident. Although everyone realizes that more efficient production methods or new products can bring great benefits in the long run -- in the short run they make sudden and drastic demands for adaptation

upon industries, and can affect thousands of jobs.

Now...I think I have said enough to illustrate the nature of things which jiggle our elbows when we try to set our hands to that future which we all hope to see realized during our lifetime. Lest my emphasis on the difficulties be misinterpreted, I want to re-emphasize what none know better than you who live in British Columbia...that given reasonable conditions, we have the means within our grasp to achieve astounding things. We have proved our ability to meet economic jostling in the past. We want to go far and fast but we have learned that we cannot go farther or faster than the total of our resources at any given time permit. We are determined to be alert to opportunity and aggressive in its pursuit.

What more can we do at this time to prepare ourselves for anything that may come?

If we would speed the development of Canadian nationhood...if we wish to ensure that the architecture of our future is soundly designed and based...if we wish to render ourselves better able to deal with any adverse development which may arise...I believe there is one field to which our attention ^(could) _(should) be directed at this time. This is the field of economic education.

Despite all the progress that has been made in recent years in understanding the simple fundamentals which underlie our material substance and sustenance, it would help greatly if Canadians as a whole understood more about the source and significance of jobs, the real basis of value, the function of money, the various institutions in our economic system, the difference between ^{the terms/concept} "saving" and "investment" and so on.

It is disturbing to think that every year many young Canadians reach maturity and begin to take part in community affairs with only the sketchiest idea of the facts of economic life. It is perhaps time that we stopped using harsh and repellent word "economics" and referred to it...say...as the study of "the way man earns his living." We should then make it possible

for the many who do not have contact with it in university, and for the great many more who are not even able to attend university, to become acquainted with it.

Now...I am well aware that a great many thoughtful people will agree with this aim immediately but will point to real difficulties in the way. "Public understanding of economic fundamentals is very desirable," they will say, "but how are you going to go about making it possible? Economics is a complex affair at best and many of those who profess understanding differ among themselves. How are you going to get economists to agree? Where are you going to get a simplified text? Who is going to teach it and where?" And so on.

The points made by these thoughtful Canadians call for sensible answers. Before attempting to meet some of them, let me make one statement. If we are agreed that the aim I have outlined is worthwhile, then we can be sure that ways and means will be found sooner or later to accomplish it. We must be careful that we do not let it go by default at this time for the lack of the persistence or energy to accomplish it.

It is true that economics in all its ramifications is a complex study. As a body of knowledge which is relatively new, economics has developed at a remarkable rate, particularly during the past twenty years. But without denying the complexities and notwithstanding the variations that arise in the details of interpretation, it is possible to state categorically that most of the facts and fundamentals are well known and are not in dispute. It therefore follows that these basic elements can be presented simply if we once set our minds to it.

I do not intend to formulate a programme nor would it be appropriate for me to do so. In fact, it will be obvious that any programme of this kind will take time. This in itself urges the importance of making a beginning now. Departments of Education today are aware of their responsibilities and opportunities in this field. But no matter how high their aims,

they cannot move without the support of great numbers of far-sighted citizens.

Some will point to the difficulty of achieving a properly objective approach because economic study unfortunately tends to become charged with emotion. We may all prefer to seek the advice of doctors and lawyers in their professional fields but we are all our own economists in the course of our daily affairs. Most of us develop views which are sometimes held with more warmth than intelligence. Here, I am inclined to make a virtue of a difficulty. The very fact that we are all practising economists can be turned to advantage. After all, despite the high school student's absorption with juke boxes and dates, he or she is also concerned with, and not a little apprehensive of, the approaching need to earn a living in a turbulent world. This, in fact, is the reason why emotion may be stirred. Anything which can contribute to an intelligent solution of that problem and to a removal of the concern which sometimes surrounds it, should be attractive.

For those who have left school, no case need be made. It is obvious from the great number of study and discussion groups which have made economics a feature of their activities, that there is a great hunger for economic understanding. In fact, it may well be that the place to begin is in the vigorous promotion of increased activity of this kind.

I shall not at this time pursue the question further, but shall content myself with making one more observation. It is that these thoughts inevitably come to one who is concerned with ^{restraining} mitigating economic forces that are likely to be harmful... and of helping to harness others which appear likely to be in the general public interest. Because of the reasonable success that has attended efforts in this field during the emergencies of the past few years, there has arisen an all too dangerous belief that any desired economic result can be obtained without much trouble if only the right financial or monetary buttons are

pressed or the levers of arbitrary controls are pulled. Some people appear to believe that economic and technological forces can be halted or reversed at will even though they obviously arise from conditions beyond our control and outside our boundaries. In other cases, possible action is not considered in due relation to the cost or disruption that would result. I suggest to you that this state of affairs makes thoughtful conclusions and decisions by great numbers of people unnecessarily difficult.

No matter how powerful or alert financial institutions and devices may be, they are not of themselves equal to the task of stabilizing, protecting or developing a national economy unaided. Far from it. It is inherent in our conception of life that the preponderance of economic power and influence arises from the decisions of countless thousands of people over a period of time. Indeed, anything that can be done by economic institutions may be entirely offset by what people do as individuals...by the principles and desires which govern the use of their own resources and the management of their private economic affairs.

I leave this suggestion with you, therefore as an *(postscript)* appropriate footnote) to our review of the activities of the Bank of Canada during its first dozen years.