Remarks by Mr. J. E. Coyne, Governor of the Bank of Canada, before the Senate Committee on Manpower and Employment, April 26th, 1961

I understand that this special Committee of the Senate on Manpower and Employment has nearly completed its enquiries. During the past five months the Committee has heard a great many witnesses and advocates, and from them and through the researches of its own staff the Committee has gathered an immense amount of factual information and analysis, of the Canadian economy, of economic growth in Canada, of labour force developments and of employment and unemployment. A very wide range of proposals or suggestions for improving employment and production in Canada, for increasing the rate of growth, and for reducing the deficit in our balance of payments, have been put before the Committee. In addition to information, suggestions and representations from various business interests and labour organizations and others, the Committee has heard from a number of specialists and experts. It is not to be expected that all these individuals and special groups would be in agreement, but they have provided enough interesting and constructive suggestions in sufficient variety to enable a comprehensive programme to be put together by the Committee, or by others interested in assessing the material which has been brought to focus on these important economic problems of today.

I am here today at your request. It is not my desire to come before you as an expert, nor to present any specific new analysis or proposal to you. I have done what I could in my Annual Reports and in public speeches to draw public attention to our economic problems. For what it may be worth, I have given my own analysis of the underlying causes, and have indicated in a broad way the principles which I think should underlie efforts to overcome our present difficulties and reverse certain trends which have become increasingly apparent during the past ten years. Copies of my Annual Report for 1960 were made available to members of the Committee at the time of publication, and I understand extra copies have been distributed this morning. I do not have anything of a specifically new character to add to what I have said in that Report, but would be glad to answer questions and explain points which are dealt with in it if such is your desire.

It may be of interest to the Committee if I first bring up-to-date the facts regarding monetary expansion in Canada. Much of the discussion by proponents of more and easier money seems to proceed on the assumption that there has been no expansion whatever, or indeed even a contraction. In actual fact, we have had over the past year an increase of more than 5% in the total money supply. In the case of the privately-held money supply, that is, excluding Government deposits, the increase has been more than 6%. In each case most of the increase has occurred in the last six or seven months and in each case it has been greater than the degree of monetary expansion in the United States. The same holds true over any longer period that may be chosen going back for many years --- the rate of monetary expansion in Canada has been substantially greater than in the United States.

We have had over the past year a substantial expansion of bank loans, as well as of bank holdings of treasury bills and government bonds. Within the total of bank loans there has been a rise in business loans and a somewhat greater rise in personal loans in the nature of consumer credit. The banks are in a position of substantially increased liquidity and are, in my opinion, well able to take care of all reasonable requirements for an expansion of loans to business enterprises in Canada.

There has also been a good capital market for the issue of securities in Canada whether by the Federal government, provincial governments, municipalities, public utilities or business corporations. We have not had for some months very much in the way of U.S. dollar borrowings in the United States by Canadian governments and corporations. There has been some continued purchase of Canadian dollar securities by foreign investors, but the main part of the capital inflow for nine months or more has been in the field of direct investment. This type of capital inflow is not affected by interest rate differentials between Canada and the United States, nor by interest rate differentials, which often are in the opposite direction, between Canada and certain European countries.

With the banks in a position to expand their business loans, and in fact facilitating the expansion of business loans to the extent that demand makes itself known, and with securities markets providing funds on a large scale for the capital requirements of Canadian governments and businesses, I do not feel that a good case could have been made for substantial further action by the monetary authorities. The action which has been taken has not, in my judgment, been out of harmony or at cross purposes with or less aggressive than action in other fields of public policy.

In assessing levels of interest rates it is important to note that they depend primarily on the degree of demand for borrowed funds and on the willingness of those who hold bank deposits to lend them. Insofar as there is pressure on interest rates continuing in our markets I believe it comes chiefly from the rise in the rate of deficit financing by various levels of government. According to figures recently published by the Dominion Bureau of Statistics in its National Accounts, the combined deficits of all levels of government ran at an average annual rate of $1,144 million in the last half of 1960, exclusive of capital spending by provincial hydro-electric and telephone utilities, toll roads, government-owned railways and the Central Mortgage and Housing Corporation. This total was very much greater than a year earlier ($336 million), for reasons which are understandable, but it has perhaps not been remarked that it was also a slightly higher rate of deficit than that which was being incurred in the last half of 1958. In the case of the federal government, the rate of deficit, as defined, was at the rate of $616 million, not as high as the rate of $822 million in the second half of 1958.

The most effective way to reduce the pressure on interest rates would be for governments to reduce their demands upon the capital market. Some provincial governments have taken action to this end by recent increases in various forms of taxation.

Looking ahead over the next year or two all the indications are that economic conditions in North America will improve somewhat. There is, however, little ground for confidence that the improvement (except as augmented by measures of public policy) will do much more than absorb the increase in the labour force during the period. It will not apparently be adequate to make a serious dent in the level of unemployment (allowing for seasonal fluctuations). Members of the Council of Economic Advisers to the President of the United States have recently made this point with reference to conditions in that country and there is no reason to believe that our experience would be any better than that of the United States, except to the extent that public policy in this country is more successful in improving employment opportunities in Canada. Expanding business opportunities will improve employment, and in the process will also increase the flow of potential workers into the active labour force, in addition to the normal annual growth. It will take a very substantial rise in employment indeed to bring about any large reduction in unemployment after allowance for seasonal fluctuations.

Your Committee has been working in a field of the utmost public importance, and I hope that the results of your studies will be valuable in bringing about better public understanding of the nature of our economic problem and possible lines of dealing with them.

One of the main points I have been concerned to set before public opinion in the past half-dozen years is the futility, and indeed danger, of looking for easy, cheap, painless cure-alls for economic problems. A great deal of ingenuity seems to be expended nowadays in devising schemes which have in common the hopeful illusion that they will enable us to get something for nothing. I do not believe anything can be achieved without effort. The willingness to put forth effort must underlie all useful practical proposals, but the mere willingness to make an effort is not enough. It is necessary to provide opportunities or outlets for that effort, and increasingly in the modern world it is found that governments have an important role, and indeed a vital part to play, in creating or encouraging the creation by others, of opportunities for useful employment, and in facilitating the maintenance of a sustained rate of economic growth at a satisfactory level.

In the field of public policy, expansion of the money supply, expansion of bank credit and other forms of credit, and at times deficit financing on the part of governments, have their part to play. This is all but universally recognized today, but the danger is that too much magic power may be thought to reside in monetary expansion and deficit finance and too little attention be paid to other fields of policy or other kinds of measures which in combination I believe are considerably more important. The mere fact that a certain amount of credit or some degree of expansion of credit may be a good thing does not mean that unlimited quantities of credit will confer unlimited benefits. As Professor Samuelson said in his special task force report on economic conditions in the United States presented to President-Elect Kennedy and published on January 6th of this year, "Planned deficits, like penicillin and other antibiotics, have their appropriate place in our cabinet of economic health measures; but just as the doctor carries things too far when he prescribes antibiotics freely and without thought of proper dosage, so too does the modern government err in the direction of activism when it goes all out and calls for every conceivable kind of anti-recession policy."

A further quotation from Professor Samuelson's report may be of interest to this Committee, "Modern stabilization has so many alternative weapons to fight depression as to make it quite unnecessary to push the panic button and resort to inefficient spending devices."

I do not quote these words in order to indicate opposition to government spending as such, and indeed I believe some degree of increased spending in some categories of expenditure is desirable. To rely on deficit finance for such expenditures, however, is to use a very dangerous drug, and I believe its use should be held to a minimum. It is particularly important to emphasize this point since most persons advocating large-scale deficit finance propose or assume that the financing will be carried out by means of large-scale expansion of the money supply.

Approaches to the problems of economic growth and employment appear to fall into four main categories. The first, if it can be called a policy proposal at all, is simply that of laissez-faire or do nothing, let nature take its course, wait for the pressures of hard times to bring about adjustments in the attitude and practices of management and labour, and be content with whatever progress is achieved over whatever period of time. This school of thought is entirely out of harmony with present-day conditions and with what is being done in other countries and, for that matter, what is being done in this country. In the end a policy of laissez-faire would lead to a breakdown of our social and economic system, out of which would come much stricter forms of a managed economy than any of us would care to contemplate.

A second school of thought is fundamentally that which expects to get something for nothing, and relies heavily on monetary expansion, deficit finance and attempted manipulation of interest rates as the machinery for this purpose. If economic problems could really be solved by massive monetary expansion it is surprising that other countries do not resort to it continually. In fact, of course, excessive reliance on these devices leads in the end to inflation, but most proponents of this school either pooh-pooh that idea or say inflation is far off in the future and not worth worrying about, or in some cases come right out and say they would welcome at least a moderate amount of inflation as an aid to business growth and a necessary feature (as they think) of any programme for maintaining reasonably full employment. I believe that proposals of this character are superficial. They do not go to the root causes of our difficulties either in analysis or in prescription. If carried to the extremes which seem to be contemplated by some of their advocates they too would lead to a breakdown of our financial system and a replacement of the private enterprise system by a combination of government controls and government ownership, of a sort which most of those concerned say they would regard with horror.

A third school of thought, or third category of proposals, does indeed accept the necessity and desirability of controls. Some would put various kinds of direct controls on imports, some people would reintroduce foreign exchange controls, some would take specific action to regulate and control the inflow of capital from abroad, others would set up a system of directing the channels into which investable funds may flow and the quantities and timing of such flows, and some would either immediately or as a second stage in the process be prepared to apply widespread price controls and wage controls.

I do not believe you can safeguard the free enterprise system by applying a set of specific governmental controls to it. Nor can you encourage business enterprise, imagination, initiative and risk-taking by having the government or any government agency give directions to the business interests concerned.

The fourth approach in the field of public policy might be called the free-enterprise incentive system. It is designed to encourage better balanced economic growth, sounder economic growth, more consistent economic growth, the maintenance of Canadian enterprise in Canadian hands, and the reduction of unemployment to minimum levels. This method is one on which we have always relied to a substantial degree in this country, with variations from time to time as circumstances seemed to require. The powers of government are utilized for economic purposes not just in the field of regulation but in the field of government expenditures and in the field of tax adjustments, in order to maximize opportunities for production and employment in Canada and for growth of the Canadian economy. The trend of national economic policy in Canada---and for that matter in all other countries of the Western World, though with variations in degree---has been towards stimulating domestic production for the home market and, if possible for export, improving opportunities for profitable operation of domestic enterprises and providing them with incentives to expand. In addition, of course, like all other countries in the world, Canada exercises some control over its foreign trade by various methods which are subject to continuous adjustments, both on the export side and more importantly on the import side.

I have not mentioned one specific proposal which is advanced by some people, namely, devaluation of the currency or depreciation of the international exchange value of the Canadian dollar. This to my mind comes definitely within the group of inflationary or "something for nothing" proposals with its appearance of sleight-of-hand and painless benefits. If it were such a sovereign remedy it would be in frequent use, not just in Canada but in every country in the world. In fact, most countries have come to foreswear this dangerous drug, having learned to their cost how much harm it can do. At best it is a confession of failure, a recognition that the whole cost-price structure of the country has got so far out of harmony with the rest of the world that there is no use trying to conceal the fact any longer. We are not in that position in Canada, and in my view we would do great damage to the Canadian economy as a whole and to many persons and enterprises in Canada by engaging in deliberate exchange devaluation or by utilizing the presumed powers of monetary policy with the definite object of putting the Canadian dollar to a discount.

I do not suggest that it is desirable to maintain a premium on the Canadian dollar, and indeed would hope to see such a change in our economic arrangements as would prevent a premium from developing again, but this is quite a different matter from attempting to bring about the inflation of all prices and all costs which is the chief effect and avowed objective of deliberate depreciation of the national currency.

In the views which I have put forward on a number of occasions I have emphasized the close connection between the deficit in our balance of payments---the large excess of imports over exports---and the trend towards large-scale unemployment in Canada. I believe we can only effect a fundamental change in our economic condition by learning to get along with a smaller excess of imports, and if possible restoring the balance in our balance of payments. To do this does not require a retreat into isolationism, economic or otherwise. It is a matter of degree, not of shutting off all imports or blocking trade channels. It is not a question of refusing to buy from those to whom we sell, but of holding our expenditures within our earnings. No country of our degree of development can be expected to go on indefinitely importing vastly more than it can pay for from the net proceeds of its exports. The familiar saying that you must import in order to export should apply to other countries as much as to Canada. It is possible indeed that we (in Canada) shall have to import more from certain countries in the world if we are to continue our exports to them, and more particularly if we desire to achieve an increase in those exports. On the other hand, we must by some means increase our own production of some kinds of goods and services which will compete with and displace some volume of imports, and particularly imports from the United States. I believe we will come up against insuperable obstacles to overcoming our unemployment problem in Canada if we cannot give our own producers adequate opportunities to provide goods for the Canadian market and bring about a reduction in our excessive imports from the United States. We likewise cannot put an end to the growing extension of foreign ownership and control of Canadian industry, and set about increasing the share of Canadians, and the ability of Canadians to increase their share in Canadian industry, except by somehow reducing the inflow of capital from the United States.

I should like to emphasize again, as I have in the past, the elementary point that you cannot have a continued net inflow of capital without a continued inflow of goods and services in excess of exports, and you likewise cannot have a continued large net inflow of capital, particularly of capital for direct investment which is the major element in our capital inflow now, without finding that Canadian enterprise is bought out or pushed aside in a wide range of endeavours by foreign enterprise.

We naturally wish to increase our exports, and indeed some increase is sure to be achieved, but the increase in exports will be matched by an increase in imports to the detriment of Canadian industry and employment in Canada unless the net inflow of capital declines.

One of the ways in which Canadian investment could be stimulated and Canadian enterprise encouraged to expand is by the provision of additional or expanded facilities for the flow of Canadian savings into Canadian industry. The Industrial Development Bank, which is a subsidiary of the Bank of Canada, is greatly expanding the number and volume of its loans for this purpose and is making a special effort to provide financing for Canadian-owned business enterprises. It is mainly operative in the field of small business, but there is no specific limit on the size of any investment by the Industrial Development Bank, the governing consideration being whether the applicant company is unable to obtain funds elsewhere on reasonable terms and conditions. We interpret this to mean that whenever a Canadian business, or a company owned and controlled to a major degree by Canadians, is unable to obtain funds from Canadian investors on reasonable terms and conditions, the Industrial Development Bank should be prepared to make a loan or to invest in the equity of the company or to guarantee its obligations to others, or to assist in the underwriting of public issues in Canada of the securities of such a company. From 1955 to 1960 our volume of new loans to new borrowers per annum multiplied four times and in the 1961 fiscal year the number of new loans and investments is running 40% to 50% above the level achieved during the same period in 1960. I hope to see a very considerable further expansion in the volume of financing undertaken or assisted by the Industrial Development Bank. It may be that other institutions and other methods of assisting the mobilization of capital within Canada for Canadian enterprises could also be utilized on an expanding scale.

Some may question the desirability of operations such as those of the Industrial Development Bank, on theoretical grounds of antipathy to government participation in capital financing. It is my personal view that it is essential in the conditions facing us in Canada today to provide public capital to various sectors of Canadian private enterprise in order to keep private enterprise Canadian, and enable it to expand under Canadian ownership and control. Public capital under private management, Canadian management, can strengthen private enterprise in Canada.

As I have said before, however, the mere provision of capital or making borrowing easier is not enough. You do not do a man a good turn by encouraging him to borrow money or invest his own money in a business unless that business has a good chance of profitable operation. There are many ways, some of which have from time to time been dealt with by legislation in Canada, by which governments at all levels can remove difficulties in the way of Canadian business enterprises, assist them to carry on research and product development, enlarge market opportunities for them, provide subsidies in some cases, at least on a temporary basis, and give tax concessions, depreciation allowances and so on, on a selective basis calculated to improve the profit-making possibilities of Canadian-owned businesses, encourage and enable them to expand production in Canada, increase employment opportunities in Canada and reduce our dependence both upon foreign capital and upon foreign-produced goods and services. Incentives can be given also to encourage saving in Canada and the investment of those savings in Canadian economic growth.

It is not necessary to contemplate any reduction in the average Canadian standard of living. Indeed, overcoming the slack in our economy and drawing unemployed resources into production, particularly those human resources which are now unemployed or underemployed, together with the expanding application of modern technology by Canadian industry can provide us with a continuously rising standard of living for decades to come. By concentrating our efforts on increasing Canadian production, particularly in the field of capital equipment, machinery and the more advanced technical processes of secondary industry, we can also provide to our own people a wider variety of employment opportunities, and increase the volume of employment of the more productive and more satisfying kinds. We have had a most unbalanced industrial structure, an unbalanced economic growth in the postwar period, leading to a situation where those fields which once seemed most profitable and most eligible for rapid growth have suffered setbacks which are now made evident in excess capacity and under-employment. In the meantime, developments in other fields of industry have been handicapped. More balanced growth and more stable growth from year to year would enable us to avoid those splurges of excessive spending followed by periods of relative stagnation, which do not even average out to a reasonably satisfactory rate of growth or percentage of employment, let alone provide satisfactory conditions at the extremes of boom and slack.