

July 31st, 1961.

I have been greatly encouraged by the many public expressions of goodwill which have appeared since the announcement of my appointment as Governor of the Bank of Canada. I have decided to make public at this time my views on certain matters connected with the administration of this office. These views had been made known to the Directors and to the Government in the following form when my appointment was being considered.

I believe that it is essential that the responsibilities in relation to monetary policy should be clarified in the public mind and in the legislation. I do not suggest a precise formula but have in mind two main principles to be established: (1) in the ordinary course of events, the Bank has the responsibility for monetary policy, and (2) if the Government disapproves of the monetary policy being carried out by the Bank it has the right and the responsibility to direct the Bank as to the policy which the Bank is to carry out.

The first principle is designed to ensure that the Bank has the degree of independence and responsibility necessary if it is, in the language of the Bank of Canada Act, "to regulate credit and currency in the best interests of the economic life of the nation". To discharge this duty the Bank must be sufficiently independent and responsible in its operations to be able to withstand day-to-day pressures from any source. But in the longer run, if there should develop a serious and persistent conflict between the views of the Government and the views of the central bank with regard to monetary policy which, after prolonged and conscientious efforts on both sides, cannot be resolved, the Government should be able formally to instruct the Bank what monetary policy it wishes carried out and the Bank should have the duty to comply with these instructions. The exercise of this authority by Government would place on Government direct responsibility for the monetary policy to be followed. If this policy, as communicated to the Bank, was one which the Governor felt he could not in good conscience carry out, his duty would be to resign and to make way for someone who took a different view.

Amendments to the Bank of Canada Act would presumably be required to deal with these points. If, however, it were agreed that the respective responsibilities should be of the general character I have indicated, there should be little difficulty in regard to the precise nature and timing of the necessary changes.

I wish, secondly, to place on record some of my views on the way in which monetary policy fits in to other public policies affecting the economic and financial welfare of the nation. I take it that the broad aim of the community is to attain, to the maximum extent possible, certain generally accepted objectives: high level employment, price stability and sustained economic growth. A flexible monetary policy is an essential element in the total blend of policies directed to these ends. In a situation characterized by large unemployment and unused capacity, monetary policy should be directed to encouraging the use of credit. On the other hand, if the economy is approaching a condition of full stretch, policy should be directed towards discouraging the use of credit.

Too much reliance on monetary policy either as a restraining or a stimulating factor would, however, lead to unsatisfactory self-defeating results. If one were to try to control the excesses of a boom period through monetary policy without adequate support from appropriate fiscal, debt management and other economic policies of Government, one would run the risk of creating great strains in the financial system in the form of intolerably high interest rates and disorganization in capital markets. On the other hand, the precise part that monetary policy can appropriately play in stimulating economic expansion is necessarily influenced by the part being played by the concurrent fiscal, debt management and other economic policies of Government. The central bank has an important part to play in influencing the trend of interest rates in a direction appropriate to the economic situation. But an attempt on its part to impose a level of interest

rates which appeared unrealistic to the market would impair confidence in the value of the currency and present a serious obstacle to the orderly flow of funds through the capital market.

What is said in the previous paragraph is not meant to depreciate the contribution that monetary policy can make towards attaining the broad economic objectives of high-level employment, price stability and sustained economic growth. On the contrary, it is meant to underline the need for a careful and consistent meshing together of all the various aspects of financial policy and general economic policy in the effort to attain these objectives while avoiding undue strains in particular sectors. In particular, since monetary policy, fiscal policy and debt management policy are interdependent and to some extent inter-changeable, there has to be a high degree of coordination to ensure that the blend or "mix" of these policies is purposefully directed towards attaining the over-all economic objectives of the community.

The views expressed above regarding the respective responsibilities of Government and Bank for monetary policy and the need for close coordination of monetary, fiscal, debt management and other economic policies point to the great importance of close and continuous contact between the Bank and the Government. I shall wish to play my full part in achieving the close working relationship with the Minister of Finance which is indispensable if the Bank is to discharge its responsibilities in a satisfactory way. I would hope to have frequent contacts with the Minister of Finance of the same character as I have had over the past years in my capacity of Executive Director of the International Monetary Fund and International Bank. In addition, in order to ensure beyond doubt that continuing high importance is attached to maintaining lines of communication, and even though such precaution may now seem unnecessary, consideration should be given to setting up a routine procedure for regular meetings at fairly frequent intervals between the Minister of Finance and the Governor.