

REMARKS OF LOUIS RASMINSKY
GOVERNOR OF THE BANK OF CANADA
BEFORE A MEETING OF THE HALIFAX BOARD OF TRADE
FEBRUARY 7th, 1966

Remarks of Louis Rasminsky, Governor of the
Bank of Canada, before a meeting of the Halifax
Board of Trade, February 7th, 1966

I should like to begin by expressing my pleasure at being here tonight and by saying how glad I was to receive the invitation to address this Annual Dinner Meeting of the Halifax Board of Trade. Your Association has a long and honourable history, and over the years it has made a distinct contribution in encouraging the discussion of important economic issues and in furthering the economic advancement of this part of the country.

It is a rather humbling experience to be talking to a body which, in its original incarnation as "The Association for the Benefit of Trade", was organized over two centuries ago, in 1750. This certainly makes the institutions with which I am connected -- the Bank of Canada, organized in 1935, and the Industrial Development Bank, organized in 1944 -- look like newcomers on the scene. I hope that in my remarks tonight I shall not give the impression of being a Johnny-come-lately who knows all the answers -- for I certainly don't. At the same time I hope that I shall indicate that at least I know some of the questions.

When I realized that the body I was to address tonight was organized in 1750, I naturally started to wonder what financial conditions in Halifax might have been like when the Association for the Benefit of Trade started its operations. So I got out the fascinating selection of

Documents relating to Currency, Exchange and Finance in Nova Scotia from 1675 to 1758 for which Dr. Adam Shortt was responsible and spent some pleasant hours going through them. I discovered that many of the documents had a curiously contemporary flavour. For example, the collection of several hundred pages is replete with references to the scarcity of money -- and this long before the days when there was a central bank! I found, moreover, many documents which illuminate the problems involved in the financial relations between different levels of government, though it goes without saying that no outside government would dare to address the provincial authorities in the tone used by Whitehall when Cornwallis, the Governor of Nova Scotia, wrote to complain that the Boston merchants were pushing up the prices of the goods they supplied, to the disadvantage of the Province. The High and Mighty Lords of Trade and Plantations in London replied to Cornwallis in 1750:

"The Merchants of Boston, of whom You complain for their Readiness to take Advantage of the Province upon every Occasion, and their Demand of exorbitant Profit upon every Contract with you, will always be more unreasonable and extravagant in their Offers in Proportion as the Credit of the Colony becomes exceptionable, which again cannot be by any other Method sustained and kept perfect but by keeping the Charges of the Year within the Supply of the Year, so that there may be always in the Treasury a Fund to answer the Bills, and the Bills punctually answered; unless this Rule be observed, Your Demands must always in some Part of the Year exceed the Fund: as often as that happens, the Payment of your Bills will necessarily be postponed, and the many very disagreeable Obstructions you have lately met with will be again to be contended against."

This was a pretty stern lesson in the need for a balanced budget and a good cash balance at all times. Cornwallis's come-back is equally interesting. He starts in a properly humble and contrite frame of mind: "I am honoured with your Lordships' message. You may be assured that I will be as frugal as possible -- not a pound shall be spent by me unnecessarily". Then, having made this formal bow to fiscal rectitude, he eases into what must be one of the first Canadian expositions (and certainly one of the most lucid) of the theory of budgetary deficits as an instrument of national policy:

"But My Lords, without money you could have had no Town no Settlement & indeed no Settlers -- Tis very certain that the public money clear'd the Ground, built the town, secured it, kept both Soldiers & Settlers from starving with Cold or deserting, & has brought down almost one thousand Settlers from the Colonys. Lots in Halifax are now worth 50 Guineas; if there was no public money circulating, lots would be given for a Gallon of Rum. "

I am not completely up to date on the value of first-class real estate in Halifax, but I suspect that it would take quite a few gallons of rum just to make an acceptable down-payment on a good lot today.

I must leave 1750 and Cornwallis now, but not before I refer sympathetically to the anguished cry with which he addressed Whitehall in a letter asking for help. "It is quite indifferent to me who is employed", he wrote. "I wish to God some person you could confide in was sent to transact the affairs of the Colony relating to money matters".

I don't know whether it was the early financial experience of

the province, or the Scottish ancestry of many of its original settlers that was responsible, but it is the case that Nova Scotians have played a very important and constructive part in the development of banking in Canada. Halifax, indeed, was the birthplace of an important part of our Canadian banking system and of the banking practices which have developed in this country. Two of the largest chartered banks operating today had their start in this city, while others absorbed three long-established Halifax banks into their organization early in this century. Banking in Halifax goes back to the 1820's and 1830's when it was a town less than one-tenth its present size. I believe that the principle of double liability made its first appearance in the Maritimes and that the first clearing house in Canada was established in Halifax in 1887. The Maritime banks were active not only in extending their business westward as Canada developed, but also into the United States and Caribbean as well -- connections which have persisted to the present day.

Mr. Chairman, I propose now to adjust my historical sights a little and bring the focus closer to the present day by reviewing very briefly the general economic developments in Canada and in the Atlantic provinces during the past few years. In a few weeks' time, Canada will be entering the sixth year of virtually uninterrupted economic expansion. This is the longest sustained period of economic advance the country has experienced since the first World War. And the magnitude of the advance

has been equally impressive. In real terms, that is after discounting price increases, our gross national product is currently about one-third greater than in the first quarter of 1961. This has been a heartening performance. Since 1961 we have ranked very high on the international growth league tables -- the increase in our real output has substantially exceeded the average of all those leading industrial countries of the world which constitute the membership of the Organization for Economic Cooperation and Development, and there is indeed only one large country in the group, namely Japan, whose growth has been greater than ours. These comparisons are, of course, affected by a variety of factors including differing rates of population growth, but I believe that the general impression they give is accurate enough.

I do not propose to go into the reasons for our good economic performance -- we have had our share of good luck, which we managed to take advantage of, and there may even, one would hope, have been occasional pieces of good management. The luck consisted in a generally expansionist world economic environment which was favourable to our exports, and in the coincidence in two years of large Canadian wheat crops and large Russian needs at times when the foreign exchange came in handy to us. On the international side, once we overcame the exchange crisis of 1962 (which was done by grasping the nettle firmly) the country has managed on the whole pretty well. Our exchange position is inevitably a worrying

preoccupation to those in Canada who have responsibility in this connection, and this is particularly the case when the United States -- the main source of the capital we need to cover our large and increasing current account deficit -- has its own balance of payments problems. I do not propose to comment on this side of things in any detail tonight but I will say that in spite of some difficulties we have in all the circumstances done reasonably well up to the present in reconciling the requirements of the domestic situation with the maintenance of a balanced international position.

Turning now more specifically to this part of the country, I believe that it would be a fair generalization to say that over the past few years economic expansion in the Atlantic Provinces has been proceeding at about as good a rate as in Canada as a whole. In the absence of estimates of output of goods and services on a regional basis, I take employment as being a reasonably good indicator of the progress which has been made. Over the four years from 1961 to 1965 non-agricultural employment in the Atlantic provinces has increased at an average rate of over 4 per cent a year. This is slightly greater than the rate of increase for the Canadian economy as a whole over this period, in spite of the fact that the increase in the labour force of this region has been less than for Canada as a whole. In such important and dynamic areas of the economy as mining, manufacturing and construction the average annual growth of employment in the Atlantic region has been ahead of the national average. The increase

of 4 1/2 per cent per annum in manufacturing employment in the Atlantic region over the past four years is a particularly encouraging development. As important as employment growth, of course, is the question of the income growth which it generates. In this connection the statistics show that the growth in average income of all wage and salary earners in the Atlantic region also compares favourably with the national trend -- 4.1 per cent a year against 3.9 per cent for Canada as a whole since 1961.

As you know, a notable feature of Canada's recent economic history has been the great rise in public and private capital investment expenditures. The increase in the Atlantic region on a per head basis has been about the same as the national average, 9 per cent per year, and in Nova Scotia it has exceeded this. The recent strength of capital expenditures in this region is reflected in the growth of important new secondary manufacturing industries which are helping to broaden and diversify the economies of this province and New Brunswick, including such technologically advanced projects as the heavy water plant at Glace Bay and the chemical industry complex at Dorchester Cape. They are reflected also in major new resource development projects in New Brunswick and Newfoundland, and in a considerable expansion of fish and other food processing facilities in all four provinces.

Perhaps just as important, in the long run, as these recent gains to which I have been referring has been the accumulating evidence of a

widespread determination of the Atlantic region to come to grips effectively with its own problems in a thoughtful, purposeful way. There have been the important studies sponsored by the Atlantic Provinces Economic Council and the Atlantic Provinces Research Board -- for example the recently published APEC report entitled "Toward a Strategy for the Economic Development of the Atlantic Provinces", which provides valuable guidelines for policy planning over the balance of the decade. In this province there is the interesting experiment embodied in the organization of the Voluntary Economic Planning committees. In these and several other organizations, I am particularly impressed to see how much of the initiative rests with the private citizen -- that is, with local businessmen, labour leaders and members of the universities. Such activities deserve and, of course, are receiving the support of governments, but I am sure they would be much less fruitful without such extensive participation and concern on the part of the private citizen in the Atlantic provinces.

It is beyond doubt that real progress is being made and that an impressive increase in employment, production and living standards has been achieved in recent years. On the other hand, no sensible person would minimize the problems which still face this province and this region. At the national level there is certainly a growing concern with regional problems, and a growing recognition that measures to promote regional prosperity are essential to the achievement of our national goals of high

levels of employment and sound, balanced growth. Federal Agencies now operating directly in these fields include such organizations as the Atlantic Development Board, the Agricultural Rehabilitation and Development Agency, and the Area Development Agency, which were not even in existence ten years ago. The experience with, and deeper understanding of, regional problems which is being acquired through these and other activities at both the national and regional levels should help greatly in finding more effective ways of dealing with these problems.

I would like to turn now to the question of monetary policy and try to give you some impression of the considerations guiding the Bank of Canada at the present time. The high level of economic activity that we have achieved in Canada after almost five years of uninterrupted expansion represents the attainment of one of the most important goals of economic policy. It has confronted us with a new set of challenging problems -- welcome problems which we have not had to face for a decade. The economy is now operating sufficiently close to its effective limits that we must be alert to the dangers that total monetary demand in the economy may move ahead more rapidly than the economy's capacity to grow. It is true that we can accommodate -- and indeed require -- a sizeable increase in the call on our resources year by year; we have what is by international standards an unusually high rate of annual growth in our labour force, and in the last year or two we have been adding to physical plant capacity at a

rapid rate. The problem of achieving just the right amount of increase in demand, however, is never an easy one in a free economy where the course of future spending decisions cannot be predicted with any exactitude. The consequences of a failure of demand to grow adequately are, of course, obvious and immediate -- rising levels of unemployment and widening margins of unused capacity. The consequences of excessive growth in demand, on the other hand, are not so readily recognized but the danger of overshooting the mark obviously increases as the slack in the economy gets taken up. Initially, if this happens, there may be some acceleration in imports and some upward creep in costs and prices which one is sometimes tempted to overlook or to ascribe to special factors. The more lasting and ultimately painful consequences may not become evident until the process has reached an acute stage and inflationary pressures are giving rise to pronounced increases in prices and costs. If one refuses to face the problem until this point has been reached, the damage will already have been done. The distortions that arise in such periods, the problems associated with the inevitable let down in activity that follows, and the loss in international competitiveness which accompanies any serious inflationary tendencies, can place the economy under a handicap which endures long after the pressures have subsided.

It is for this reason that I am concerned about the signs of some deterioration in the performance in respect of prices and costs which

became apparent in the Canadian economy during 1965. Given the prospect of continued strong economic expansion throughout North America in the present year and the tendency we have observed in the past for such adverse price and cost developments to gather momentum, it would, in my opinion, be dangerous to ignore the warning signals if we wish to avoid bringing the expansion to a premature end and to avoid generating serious balance of payments problems for the future.

In 1965 the total output of goods and services in the Canadian economy increased by more than 9 per cent in value and by about 6 1/2 per cent in volume terms. Such a large and gratifying increase was only possible because of the slack which still remained in the economy a year ago. With this slack virtually eliminated in many parts of the country, it would be imprudent to think that we can expect to see expansion continue at quite such high rates. For this reason I feel that it has been appropriate that as the economy moved closer to full capacity operations, credit conditions should have become less easy. The Bank of Canada has certainly not acted to prevent a reasonable rate of credit expansion. But the continued strong growth of the economy, accompanied in the last year or two by an acceleration in business outlays on plant and equipment, has inevitably led to heavy demands for credit and market rates of interest, including mortgage rates, have increased and the chartered banks have found it necessary to become more selective in their credit policies in recent months. The

extent to which it is appropriate for the monetary authorities to permit credit conditions to tighten in any given circumstances must inevitably be a matter of judgment and I have been very interested to note that in its submission to the Minister of Finance last week, the Canadian Chamber of Commerce expressed the view that in present circumstances it would be appropriate for Canada to pursue "a more vigorous monetary policy and impose more monetary discipline".

A few moments ago I referred to the fact that despite the good rate of economic growth which has been enjoyed in the Atlantic region during the present expansion of the Canadian economy, certain major problems remain. In the fourth quarter of 1965 when the national unemployment rate was down to 3 1/2 per cent of the labour force on a seasonally adjusted basis, unemployment in the Atlantic region was still running at about 6 per cent. This represents a considerable reduction from the very high levels of unemployment prevailing at the start of the expansion, but it is well above the 4 1/2 per cent rate which the Atlantic Provinces Economic Council considered to be a realistic target for 1970 in its recent study. There is no question that a greater margin of slack exists in this part of the country than in most other regions. Moreover, while this region has recently experienced a very good rate of growth, marked disparities remain in terms of per capita income and per capita investment between this region and the rest of the country.

In these circumstances I can readily appreciate and understand the concern sometimes expressed here over the tightening of credit conditions which has developed during the past year. There are several points in this regard which I would like to make.

First, I think there can be no disagreement with the proposition that an essential requisite of growth in the Atlantic provinces is the maintenance of sound and sustainable expansion in the national economy. The monetary policy we have been following has had as its objective the prolongation of expansion on a sustainable basis and the avoidance of overheating in the economy and of strains and imbalances which would lead to a premature end of the expansion.

Secondly, while the cost of credit has risen over the past year and more selective lending policies are now being followed by financial institutions, credit expansion is continuing, and at a substantial rate. It is my impression and certainly my desire that the normal requirements of smaller bank borrowers will be met in this and all other parts of the country.

Finally, though there are some who seem to think that monetary policy can and should do the whole job by itself, I have made it clear on a number of occasions going back to my submission to the Porter Commission in 1962 and my subsequent evidence that I feel that undue reliance on monetary policy to restrain any general tendency towards excessive demand

pressure would not only fail to produce the desired results but would have unfortunate side effects as well. Apart from the effect on international capital flows which in our situation must always be kept in mind, there is the unevenness of the impact of monetary policy on different kinds of businesses and classes of borrowers. Monetary policy is only one part of a whole mix of public policies, including fiscal and other general economic policies, which are designed to influence the total level of spending in the economy, and I hope that it will not be necessary to place undue reliance on monetary policy in attempting to keep the rate of growth of demand in step with the economy's capacity to increase its output.

It is in the nature of monetary policy that its effects cannot be directed towards particular areas on a pin-pointed basis. Its impact and the criteria on which it is based are necessarily nation-wide. There is no escape from this. The central bank must, however, be very concerned that it has the best possible knowledge and understanding of what is going on in particular sectors and regions. Only in this way can it properly assess developments in the national economy and shape its policy wisely.

In order to avoid undue pressure on our price and cost structure and thus on our competitive position when the economy is operating at very high levels, we need to place greater emphasis on policies which are directed to the supply side of the picture. This means giving greater attention to the education and training of our manpower as well as other efforts to promote our industrial efficiency and our adaptability to changes in demand and technology. The growing recognition of the important role of "supply

policies" in Canada is due in no small part to the attention which has been focused on them by the Economic Council of Canada.

Efforts on the supply side also involve giving increased attention to the problem of matching as best we can our productive resources to the particular kinds of demand which our own economy and our export customers are generating. Such measures can and obviously should in many cases be quite selective as between different parts of the country. An example of selective measures of restraint was provided recently when the Government of Canada took steps to postpone or slow down the pace of certain of its construction expenditures in those parts of the country where the pressure on the construction industry is severe, while maintaining them in other areas. On the more positive side, this approach also means increasing our efforts to make fuller use of the slack which still persists in certain regions such as the Atlantic provinces. It is clear that agencies like the Atlantic Development Board and the Area Development Agency, working in close cooperation with the provincial authorities, have an important role to play in supplementing capital financing in such areas, while other Federal agencies are bringing new drive into the efforts to cope with pockets of high unemployment and rural under-employment.

One of the financial institutions which I think has been and can continue to be helpful, perhaps in even greater measure, in the economic

development of the Atlantic region is the Industrial Development Bank, of which I am President.

The Industrial Development Bank was set up by Parliament in 1944 as a subsidiary of the Bank of Canada. It was set up for a special purpose: to fill a gap in the financial system. Prior to its formation, there were for practical purposes no readily available sources of medium and long term financing for that important group of enterprises consisting of smaller-size businesses, even though they might be well managed and have excellent prospects for growth. Today the gap is narrower than it was twenty or even ten years ago, and other lenders have entered this field. For us this is a gratifying development because we feel that it has come about in part because of the success of our pioneering efforts. However, there is still a gap, and our experience shows that in all parts of the country opportunities exist for sound term financing of well-run, potentially profitable, smaller business enterprises which find it difficult or impossible to obtain financing from conventional sources on reasonable terms and conditions.

In the early years of the Bank's operations, we were pretty well confined under the terms of our Act to the financing of manufacturing enterprises but, following amendments to the Act over a period of years, our terms of reference were broadened so that today the Industrial Development Bank can provide financial assistance to virtually any type of industry or

business, except a few which are regarded as inappropriate for our participation. In addition to manufacturing businesses, the Bank can provide financing to service industries such as those engaged in wholesale and retail distribution, transportation, laundry and dry cleaning, restaurants, professional services, farming and fishing operations, and so on. In fact, at present some 60 per cent of our loans are to businesses engaged in types of activity other than manufacturing.

Besides financing new buildings, machinery and equipment, etc. the Bank will in some circumstances consider applications for loans to strengthen working capital (for example, when it has been depleted by purchases of equipment or other capital expenditures) although loans for this purpose are intended to supplement rather than take the place of normal accommodation provided by a chartered bank or other source of current financing. We are always willing to participate in the initial financing of soundly conceived new businesses, and in some circumstances can assist in financing changes in ownership, mergers, etc. In the course of developing a loan application with a customer, one of the useful functions we can play is in providing guidance on ways in which the prospective borrower can arrive at a sound and suitable mix of financing for his business.

The Industrial Development Bank was intended by Parliament to pay its way and to cover its costs of operation, including of course losses incurred in the course of doing business. For this reason, our

lending rates tend to be somewhat higher than those charged by many conventional lenders on prime credit risks. As we have gained in experience over the years we have found it possible to assume greater risks consistent with paying our way and to assist more marginal enterprises onto a sound and fully competitive basis.

The Industrial Development Bank now has twenty-seven branches across Canada and in the past five years has made nearly ten thousand loans for an amount totalling more than \$425 million. Here in the Atlantic region the Bank has four branches -- a supervisor's office in Halifax and branch offices in Saint John, Moncton and St. John's, Newfoundland. In the past five years these four offices have made 886 loans totalling \$30.9 million, of which \$11.3 million was in the province of Nova Scotia. Most of these loans -- in the Atlantic region as elsewhere -- were for amounts of less than \$100,000. In fact the average size of an IDB loan is in the \$40,000 range. You may also be interested to know that the Bank's operations are decentralized to the extent that in the majority of cases -- roughly 75 per cent -- the decision on a loan proposal is taken at local branches or regional offices.

The proportion of the total of IDB loans made in the Atlantic region is roughly consistent with the relative size of the regional economy, but we would be happy to see still more loan proposals received by our offices in this part of the country. It is true, of course, that in line with your historic financial traditions you have developed a number of successful

organizations which contribute in important measure to filling the gap to which I referred earlier. But we stand ready to work with such organizations as Industrial Estates Limited and the Provincial Loan Board here in Nova Scotia and the New Brunswick Development Corporation in that province whenever we can usefully do so.

The provision of better financing facilities to smaller enterprises important as it is -- is, of course, only one of the many things needed to build a stronger basis for faster economic growth in this region. A particularly important and valuable contribution in a different area is that now being made by the Atlantic Development Board, through the provision of supplementary capital assistance for what economists like to call "the economic infra-structure". This covers such basic facilities as hydro-electric power and the creation of industrial sites with the necessary road and dock facilities, adequate fresh water supplies and so on.

In addition, the building of stronger foundations for growth also means giving priority to the development of human resources, as was pointed out in the strategy paper recently prepared by APEC, which commented that "no economic development programme is complete without recognizing the importance of development in human capital". I am convinced that high priority must be given in the years ahead to the improvement of the level of general education and technical skills of our population; it is reassuring to see how much awareness of this there is in the Atlantic region.

Mr. Chairman, I have come to the end of what I have to say. I have tried in these remarks to indicate that while there are grounds for solid satisfaction in the outstanding economic growth we have experienced in Canada during recent years, there are no grounds for complacency or relaxation.

Taking the economy as a whole we are, as we approach the expanding limits of our capacity, faced with a new range of problems. If we ignore some of the warning signs, in the form of price and cost increases, we may find that our competitive position is seriously impaired and that continued expansion is jeopardized. Our international payments situation, requiring as it does continued large inflows of capital in a world which is short of capital, is a constant source of concern.

On the regional front, though all areas of the country have shared in the advance of recent years, some (notably the Atlantic region) still have appreciable amounts of slack and average levels of output well below the national average. This combination of circumstances also presents us with challenges and opportunities. There is no single road to success in accomplishing our objectives of balanced and sustainable economic expansion. The prosperity of the Atlantic region will not be furthered by the adoption of national policies which allow the competitive position of the economy as a whole to be undermined: sustained and sound economic growth on a national basis is indeed a pre-condition for the attainment of the economic goals of this province and this region. On the other hand, appropriate

policies having nation-wide application must be supplemented by others which are better able to deal specifically with the position of particular areas and help them in their efforts to achieve a more dynamic and diversified economy. These are great objectives which all of us share. It is my hope that in the combination of general and specific policies required to achieve them, the two institutions I represent will play a useful part, for the good of Canada as a whole and all its regions.