Mr. IRVINE: He said that it was not a thing he was discussing at that time. I would like to know how the variation between the value of currencies of the different nations, or as between one nation and another.

The WITNESS: You mean, as to how the exchange rate is fixed?

Mr. IRVINE: Yes, if you would like to put it that way.

Mr. FRASER: It is fixed here in Canada.

The WITNESS: I suppose one could answer that question in the good old fashioned way by saying that it is demand and supply that fixes any price, and that answer would be I suppose an accurate answer as regards the price of foreign exchange over a sufficiently long period of time. Over a long period of time a country's foreign exchange rate has to be such that the demand for foreign exchange on the part of its nationals to pay for imports and to pay for current services and to purchase investments abroad is equivalent to the supply of foreign exchange resulting from its exports of goods and services and from capital inflow. If the price of foreign exchange is fixed at too low a level the supply of foreign exchange will increase relatively to the demand for foreign exchange. In other words, if the currency is under valued exports will tend to be stimulated and imports will be relatively expensive as compared with domestically produced goods, and that condition will tend to raise the domestic level of prices until the equilibrium has been restored; and, conversely, if the exchange is under valued. Now, that answer is extremely theoretical.

Mr. IRVINE: Yes. Thank you.

The WITNESS: That is the theoretical answer. In any concrete case there will be other practical things to take into consideration. I must add this, that if the exchange rate is stabilized that means that there must be a fluctuation in the international reserves the supply and demand over any short period of time will obviously not coincide, and if a fixed rate is maintained then it must be through the use of your international reserve or your accretions to your international reserves to keep supply and demand during that time from exercising normal influences over exchange rates.

Other factors enter over short periods. For example in the case of Canada, a very important factor in determining the exchange rate has been the rate between sterling and United States funds. Traditionally the Canadian dollar has taken a position midway between sterling and the United States dollar. I mean by that if you take the sterling—U.S. average rate at the old parity of $4.86 to the pound, when sterling has been depreciated about 20 per cent below that the rate of the Canadian dollar has been depreciated about 10 per cent below its parity. When sterling has been depreciated about 10 per cent we find a depreciation of about 5 per cent in the relation of Canadian dollars to American funds; and that represents if you like the medial position of the Canadian dollar. It has accurately represented the economic position of Canada as between the United Kingdom and the United States with our surplus of exports to the United Kingdom and our surplus imports from the United States. The surplus of sterling has realized fewer American dollars when sterling has been depreciated in relation to the American dollar rate and we have been less able to protect the value of the Canadian dollar and the Canadian dollar has tended to fall.

By Mr. Stewart:

Q. Following on that, would you say that the present rate is a natural rate?—A. Mr. Chairman, I have two objections to answering that question. One is that it opens up a brand new field and one that would take a lot of time to discuss and is not directly related to this measure. And the second objection is that I am afraid if I embark on a discussion of the exchange rate I might say something which under the provisions of the Exchange Fund Act would make me liable to three years' sentence in prison.