

CANADA-U.S. ARRANGEMENTS

The agreements between Canada and the United States in respect of their international financial relationships were dealt with twice in the course of 1968 by exchanges of letters between the Secretary of the Treasury of the United States and the Minister of Finance of Canada. The first of these occurred on March 7 and the second on December 16....

The exchange of letters of March 7 exempted Canada from all the United States balance-of-payments measures affecting capital flows that are administered by the Federal Reserve System and the Department of Commerce. This action was of prime importance in enabling Canada to surmount its serious exchange crisis. It was matched by two steps on the Canadian side to ensure that the United States balance-of-payments position would not be impaired by the exemption. Canada declared its intention (1) to take any steps necessary to ensure that its exemption from the United States programme did not result in Canada's being used as a "pass-through" by which the purpose of the United States balance-of-payments programme would be frustrated; and (2) to invest its holdings of United States dollars in excess of working balances in United States Government securities which do not constitute a liquid claim on the United States, but with effective safeguards to Canada's position should its reserve levels require.

Steps were subsequently taken to implement the Canadian undertakings. On May 3 the Minister of Finance announced guide-lines that had been accepted by the chartered banks following discussions with the Bank of Canada. On July 24 the Minister of Finance asked all other financial institutions operating in Canada to accept a similar guide-line. On September 19, guide-lines for Canadian incorporated companies other than financial institutions were announced by the Minister of Trade and Commerce....

These various guide-lines were designed within the framework of Canadian practices to provide the necessary protection to the United States payments position, while at the same time causing a minimum interference with the normal activities of Canadian business. Our financial relations with the United States are so important that it is clearly in the national interest that Canadians should manage their affairs within these guide-lines. The Bank of Canada is administering the guide-lines which apply to the chartered banks, whose helpful co-operation it has received in this task.

In connection with the second understanding referred to above regarding the investment of Canada's holdings of United States dollars, Canada held at the end of 1968 \$1,250 million (U.S.) of special United States Government securities, an increase of \$1,050 million (U.S.) over the year.

The exchange of letters on December 16 dealt primarily with that part of the understandings between the United States and Canada which has to do with the level of Canada's official reserves. As reserves recovered during the summer and autumn from the low levels reached during the exchange crisis of the first quarter, increasing concern was expressed in Canada that the flexibility of Canadian monetary policy was in danger of being severely limited by the existence of a "target" level for Canadian exchange reserves under our agreements with the United States. In the December exchange of letters it was agreed that the understandings between the two countries do not require that Canada's reserve level be limited to any particular figure, and recognized Canada's need for flexibility with respect to reserve levels in order to accommodate the adaptation of monetary policy to the changing needs of the domestic economy, seasonal factors and other influences of a temporary nature. I welcome this clarification of our basic arrangements with the United States....