economy at a rate of inflation lower than that in the United States, though the margin of improvement over the U.S. rate of inflation is probably not much better than 1%. For instance, if the United States economy is inflating at a rate of 5% it is unlikely that the Canadian rate of inflation could be much lower than 4%. The Economic Council of Canada, in its evidence of October 6, 1969, stated:

> The Council also notes that the overheating of the U.S. economy has contributed to a much more marked "inflationary psychology" in both the United States and Canada. In the words of the *Sixth Annual Review*—Expectations of continuing substantial price increases are currently being taken increasingly into account in the markets for some goods and services (for example, in such fields as construction and land purchases), as well as in the markets for labour and capital. In these circumstances, resistance to price and cost increases tends to be reduced." This has complicated the difficulties of restoring reasonable price and cost stability in Canada.
>
> ....
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> In approaching the policy setting appropriate to achieving good performance in the economy, the Council has based its approach on an essential premise since the *First Annual Review*. This is the premise that it will be very difficult indeed to achieve high standards of performance in relation to our basic economic and social goals under conditions in which there is poor performance in the world economy—and in particular, in the U.S. economy. We have made it clear that the Canadian economy cannot be effectively insulated from major price movements abroad. The scope for unilateral action within Canada to contain inflation is limited.

For further evidence on this subject, see Appendix A.

In this connection the Committee has noted recently published U.S. figures showing a rate of increase in 1969 consumer prices of slightly over 6% and D.B.S. figures for Canada of an increase in consumer prices of slightly over 4.5%. For further illustration, see Appendix B.

Canadian policy options, therefore, are limited first by international interest rate levels, and secondly by the state of the U.S. economy.

Our trade and capital transactions with other countries take place under generally free market conditions. If interest rates are low in Canada relative to the U.S. and other countries, money will flow out of the country precipitating a foreign exchange crisis. Our fixed exchange rate may have the effect of reducing the opportunities for more independent action by the Bank of Canada, though there may be crucial offsetting disadvantages in a flexible exchange rate.

We also noted the comment of Mr. Rasminsky who singled out our chronic deficit on international current account transactions in these words "There may be a tendency for our need for capital to outrun our own savings and for us to have to rely to some extent on American or other foreign capital markets. Recently we have been relying relatively more on European markets and less on the American market for our long term capital requirements. Looking ahead I think that in recognizing this we will have to also keep in mind the danger of vulnerability of the Canadian economy to the extent that it is dependent on foreign capital imports and that it should be an objective of our policy to reduce this vulnerability, to reduce our dependence on foreign capital by moving towards a balance rather than a deficit in our Current Account."

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