

major changes in supply and demand. The price of credit is the level of interest rates. When the supply of credit is ample or the demand is slack interest rates fall; and when this situation is reversed interest rates rise. But interest rates also reflect the quality as well as the quantity of supply and demand. If lenders or investors develop doubts about the wearing or the lasting quality of the securities they are offered they will be reluctant to buy except at a lower price, that is to say, at higher rates of interest....

"While the Bank of Canada has a broad control over the money supply, it is the chartered banks that decide through their day to day actions how that supply of money is allocated. The overall limit of bank credit is controlled by the statutory requirement that each bank shall maintain a minimum cash reserve equal to 8 per cent of its deposit liabilities, and by an understanding between the banks and the Bank of Canada that each of the chartered banks will maintain in addition a minimum secondary reserve of highly liquid assets (i.e. day loans and Treasury Bills) equal to a further 7 per cent of its deposit liabilities. But beyond that it is for each bank to decide for itself, having regard to prudent banking practice, what proportion of its resources is put into loans, how much is invested in federal, provincial, municipal or corporate securities, or what amounts should be committed to insured mortgages under the National Housing Act. In the allocation of these resources neither the Government nor the Bank of Canada has any authority to direct how the chartered banks shall act.

MONEY SUPPLY

"While the Government has no direct control over money supply and the volume of credit, nevertheless its fiscal and debt management policies unquestionably affect the total credit situation. During the period of the recession the large federal deficit that was deliberately engendered was matched by an increase in the money supply by the Bank of Canada to a degree which the Bank believed to be appropriate to the circumstances. As conditions changed from recession to recovery to expansion, the Government adapted its fiscal policy by moving in the direction of a balanced budget. Concurrently, the Bank of Canada having regard to these changed conditions, and being particularly concerned with the inflation psychosis that appeared to be spreading into Canada from the United States, took steps to stabilize the money supply....

"While the total money supply has remained relatively stable over the past twelve months, except for seasonal variations, may I emphasize that there has been no freezing of the money supply. Fluctuations always occur from month to month.

"It is worth recording that from the beginning of the recession to the present time the proportionate expansion of money supply in

Canada has been significantly greater than in the United States. Over the past two years the United States money supply has increased 10 per cent, while ours has increased 16 per cent.

"...There are those who contend that a measure of inflation would today bring about a reduction in interest rates. This is a fallacy of the deepest dye. Inflation would divert savings into equities and diminish the supply of loanable funds. The result would be to force interest rates upward.

CURRENT CREDIT SITUATION

"I have already drawn attention to the extraordinary demand in 1959 for commercial credit in Canada, and to the fact that the existing shortage is the outcome of the free play of the strong forces of economic growth and is not attributable in any degree to any reduction of supply. Restrictions on credit are never popular. Refusals of credit tend to provoke strong personal resentments. We should have Utopia if every credit-worthy borrower could obtain all the money he requires at reasonable rates of interest, on other terms to his satisfaction, under conditions of full employment, a steadily expanding economy and stable prices. Unfortunately, this is a form of coexistence not yet completely attained in this imperfect world.

"You would expect me to comment on the restrictions which the chartered banks have imposed on their own lending operations.

"I have often declared my belief that the chartered banking system of Canada is as good as any in the world. It enjoys very high respect in other countries. Over the years our banking system has on the whole well served the expanding needs of the dynamic Canadian economy. I have appreciated the co-operation of the chartered banks in many matters of mutual concern. It would be unreasonable to expect perfection of any banking system. In such situations as the present, however, it is essential that the public should clearly understand where responsibility rests.

"Parliament has conferred on the banks valuable charters containing many rights and privileges. I think we will all agree that these should be exercised with due regard for the national interest.

"The banks are not the only source of loanable resources, but they are normally the first-line source. In times of enormous demand as throughout 1959, it is vital that the best possible use be made of the existing available lending resources, for these are not unlimited. I am particularly concerned for the legitimate credit needs of farmers and small borrowers, that their interests may not suffer in the keen competition which exists for large and very profitable accounts....

"The commitments to the larger borrowers have continued greatly to exceed the actual loans, and have obliged the banks to keep

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