Most of the larger developing countries, primarily the newly industrialized ones (NICs), also have floating rates, but generally these are closely managed against other economic indicators in order to support monetary, investment or industrial policies[123]. Most other small, open economies maintain fixed or pegged range rates against the currencies of their major trading partners[124].

5.2.2.2 The Canadian Exchange Rate:

Since the demise of the Bretton Woods system in the 1970s, the Canadian dollar has moved through long swings, first rising, then gradually falling against the U.S dollar. From a premium over the U.S. dollar in the mid-1970s, the Canadian dollar declined to its lowest level of U.S. $0.7152 by 1985.

Concurrent with the advent of the Free Trade Agreement with the United States, the exchange rate has risen, first to U.S. $0.7696 when the agreement was signed in December 1987, to U.S. $0.8218 when the 1988 election was called, and to U.S. $0.8450 when the Agreement came in to force. The dollar recently has traded at an average of U.S. $0.8550 with highs of over $0.86, although in the early part of January, 1990 the average rate had fallen off by about two per cent.

Some of the rise in value of the Canadian dollar can be attributed to business confidence in Canada, and a higher demand for Canadian-dollar-denominated investments. But the larger part is attributed to the strong anti-inflationary stance of monetary policy and the resulting high level of nominal and real interest rates in Canada, attracting strong portfolio inflows.

Exchange rate variations have appeared to follow a pattern which supports the allegation of an implicit agreement on the part of Canadian authorities to reduce the competitiveness of Canadian exports. Since the advent of the FTA the dollar has risen and stayed high in terms of the U.S. dollar. There is little if any evidence, however, to support such a contention. Moreover, the Ministers of Finance and Trade have both issued specific denials of such allegations on several occasions. Nevertheless, actions by the Governor of the Bank of Canada to sustain wide interest rate differentials between Canada and the United States -- which have been taken as a defence against inflationary pressures -- have in fact led, through exchange rate appreciation, to a decline in the competitive position of Canadian industry.

While a high rate of exchange may lead to increased competitive pressure to adjust, an overly high rate, coupled with high interest rates, will reduce the capacity of Canadian enterprises to improve productivity and make new investments in order to take advantage of the opportunities and challenges of the FTA and global economic restructuring.

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[123] Brazil, Argentina, India and Korea for example. About twenty five countries have some sort of flexible, but not fully floating exchange rates.

[124] Sweden, Norway, and Austria fit this category, as do most developing countries.