

5.2.2 Exchange Rate Management:

Three issues have brought the Canada/U.S. exchange rate into recent prominence:

- The upward trend in the rate itself, which has, perhaps, focussed more intense pressure on Canadian exporters than any other international influence;
- The fact that fluctuations in exchange rates have a larger and more immediate effect on inflation, employment, investment and locational decisions in Canada than in many other countries because Canada is far more dependent on international trade. Indeed, according to the Governor of the Bank of Canada, John Crow:

the Canadian economy is very open to international exchange and international economic and financial influences. More than a quarter of our total production, of goods and services, is traded internationally. We have no exchange controls of any kind and our two-way flows of capital are large by any yardstick.¹²⁰

- Allegations from some quarters that recent trends in the Canada-United States exchange rate are attributable to the FTA, through a "secret" deal between the two countries' finance ministers in late 1988 made to re-start the stalled FTA negotiations.

The United States, Canada's largest trading partner, is less dependent on both trade in general, and North American trade in particular, than is Canada. This together with the fact that a large proportion of Canada/U.S. trade is priced in U.S. dollars causes exchange rate fluctuations between the two countries to play a greater and more immediate role in effecting the Canadian economy.

5.2.2.1 The Exchange System:

Canada maintains an independently floating exchange rate, one of only fifteen countries which does so¹²¹. While Japan and the United States are in this group, the European Community (with the notable exception of Great Britain) has moved towards stabilizing exchange rates among its members' currencies¹²².

The central virtue of the European "snake" is thought to be the greater encouragement to trade and investment activity brought about by the reduction of exchange-rate risk.

¹²⁰ Speech by John Crow, Governor of the Bank of Canada, 15 May 1989.

¹²¹ INTERNATIONAL MONETARY FUND, 1988. Annual Report 1988
Washington, D.C.: IMF.

¹²² Exchange rates in the European Monetary System (EMS) are maintained within a margin of 2.25 per cent around the bilateral central rates against other participating currencies, with the exception of Italy, where the margin is 6 per cent.