BANK OF CANADA

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Bank of Canada Governor speaks to the Greater Charlottetown Area Chamber of Commerce

CHARLOTTETOWN, P.E.I. -- The Bank of Canada expects a positive economic picture going into next year, Bank of Canada Governor Gordon Thiessen told the Greater Charlottetown Area Chamber of Commerce today. Nonetheless, the Bank is very sensitive to the increased risks of inflation arising from stronger foreign and domestic demand.

In a speech that reviewed two important challenges that may face Canadian monetary policy next year, Mr. Thiessen discussed the ongoing extraordinary strength of the U.S. economy and, in particular, the implications for Canada of further increases in U.S. interest rates to cool that economy.

The Governor stressed that there is no automatic rule as to how the Bank of Canada should respond if the U.S. Federal Reserve raised interest rates. But he said that, if it looked as though the underlying economic momentum and price pressures in the United States would lead to upward pressures on prices here, the Bank would certainly respond.

“Let me be as clear as I can on this,” Mr. Thiessen emphasized, “our current healthy economic expansion will continue only if we sustain a low and stable inflation environment.”

Mr. Thiessen also discussed a possible scenario of a serious flare-up of inflation in the United States and how Canada could resist a spillover here.

The second challenge that the Governor considered was how monetary policy should operate as the Canadian economy gets close to full use of its production capacity. Mr. Thiessen said that “given the current momentum in our economy and the high levels of activity that we are seeing, and because of the uncertainty surrounding the conventional estimates of potential output, monetary policy-makers must be on guard . . . [and] be very alert to early warning signs of accumulating price and cost pressures.”

Governor Thiessen said the Bank will “respond promptly and firmly if any such signs emerge.”

On the year-2000 changeover, Mr. Thiessen reiterated his earlier message that the Canadian financial sector is well prepared and that Canadians can expect “business as usual” as we head into the year 2000 and beyond. In fact, said Mr. Thiessen, the financial sector is “so well prepared that the major issue is no longer one of potential technical problems. Rather, it is a matter of dealing with a possible overreaction to year-2000 fears that could be more disruptive than the year-2000 problem itself.”

That is why financial sector participants, including the Bank of Canada, have put contingency arrangements in place, such as a much larger-than-usual inventory of bank notes and a special liquidity facility for financial institutions. These arrangements should “bolster the confidence of Canadians in the financial sector’s ability to operate normally, . . . ease year-2000 fears, and reduce the likelihood of an overreaction.”