From Paper Presented by Douglas C. Abbott, Minister of Finance of Canada, at the Semi-Annual Meeting of the Academy of Political Science, Held in New York City, April 1, 1948.

"It used to be the orthodox view, and it is a view still held in some quarters, that the solution to the type of situation which exists today is to allow interest rates to rise to increase the supply of savings and to choke off the demand for them. During 1947, especially in the latter part of the year, interest rates did stiffen in the United Kingdom and the United States, and since the first of this year in Canada the yield on long-term government bonds has risen in two steps to the level on which the Victory Loans were raised during the war--that is to say, 3 per cent. However, I do not think this should be interpreted to mean any conviction on the part of our monetary authorities as to the efficacy of interest-rate changes as an instrument for controlling credit expansion under current conditions. In commenting on the reduction in its bid prices for government bonds on February 27 last, the Bank of Canada used the following words:

> The degree of the change in interest rates does not appear inappropriate in the circumstances. On the other hand the Bank of Canada does not regard the increase in rates which has taken place as one of the most important factors in combatting a general rise in price levels. The bank is not in favor of a drastic increase in interest rates which would be likely to create a situation that might hamper, and might even prevent, essential forms of capital investment which Canada needs and which it is desirable should be proceeded with.

Perhaps I might amplify this statement a little. On the supply side, it is difficult to believe that any reasonable increase in interest rates would persuade the general public to save more and increase on balance its holdings of government bonds, thus making possible effective open market operations by the central bank. During the war the public in all democratic countries was persuaded to increase its holdings of government bonds on a scale far beyond anything previously dreamed of. A rise in interest rates likely to be sufficient to induce the public to increase its savings materially under present conditions would cause so drastic a fall in the prices of such bonds and so chaotic a condition in the money market and among institutional as well as individual investors that I doubt whether any responsible person would recommend it as deliberate policy. Even if the public should increase its purchases of government bonds, this would not be anti-inflationary unless the purchasers, in doing so, increased their current savings. A switch from idle savings deposits to bonds would not be enough, and it is difficult to believe that most of the small savers are likely to reduce their living expenditures under current conditions merely because they can obtain a slightly higher interest rate on the money they save.

Analysis of the demand side of the market leads to a similar conclusion. From the point of view of the industrial borrower, demand is so intense that it would take a really substantial change in interest rates to dampen his enthusiasm

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and make him defer his capital project. Difficulty in obtaining loans or in floating securities would be a much more effective deterrent than higher rates. It would, of course, be comparatively easy for the central bank to produce such chaotic conditions in the money market that even the largest and strongest corporations would have difficulty in raising money. But as I have already indicated, what we need is a slowing down, not a sudden cessation, of capital development.

In general I would expect this to be substantially the philosophy which animates the monetary authorities in your country and in the United Kingdom."

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