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Chair

Mr. Rob Merrifield

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● (1535)

[*English*]

The Chair (Mr. Rob Merrifield (Yellowhead, CPC)): I call the meeting to order.

We want to thank the committee for being here. We have a special guest with us this afternoon: Mr. Mark Carney. Thank you for being here.

We want to make note that cameras will have to leave the room. The meeting is televised, so they'll be able to catch their pictures there. Would the cameras leave the room, please?

Okay, that's half of the room.

We want to welcome you sincerely to our committee. We hope this is the beginning of a long-lasting relationship with the committee and with your future job with the Bank of Canada. We look forward to the time we have here today and to being able to discuss some of what you have in mind for us.

We'll go right to that and ask you to start with your presentation.

Before we do that, we have a question from Mr. Dykstra.

Mr. Rick Dykstra (St. Catharines, CPC): Thank you, Mr. Chairman.

Mr. Carney is here, and I know he's looking forward to his presentation. Certainly I welcome having him here, but this is a review, and as per any OIC appointment that's made, the committee has the right and privilege to call forward the person receiving the appointment.

I thought it might be a little bit helpful if perhaps you or the clerk could clarify the rules of engagement in terms of the bylaw, so to speak, or the parameters for the presentation, and also for the questions that will follow.

The Chair: We'll do that very quickly. I'm not going to go into it in any great depth. The principle is the same as an interview of any individual you would be interviewing for a job appointment. That is the principle I'll be applying to this committee, so the same kind of respect and rules will be applied here.

I'll limit the questioning to those considerations, unless the clerk has anything further than that. Those are the instructions I have, and they're in Standing Order 110(1).

Hon. Garth Turner (Halton, Lib.): Could we have some clarification on that, please? What does that mean? Which questions will you not allow?

The Chair: I'll ask the clerk to just read the standing order on it, and that will help clarify everything here—very quickly, though, because we're wasting time.

The Clerk of the Committee (Ms. Elizabeth Kingston): Standing Order 110(1) states:

> A Minister of the Crown shall lay upon the Table a certified copy of an Order in Council, stating that a certain individual has been appointed to a certain non-judicial post, not later than five sitting days after the Order in Council is published in the *Canada Gazette*. The same shall be deemed to have been referred to a standing committee specified at the time of tabling, pursuant to Standing Order 32 (6), for its consideration during a period not exceeding 30 sitting days.

Hon. Garth Turner: Excuse me, Mr. Chairman, I didn't hear any restrictions on the kinds of questions that can be asked under that standing order. Are you saying there are some?

The Chair: Just hang on a second. I'll consult.

The clerk has informed me, and I will concur with her, that as the chair I'll determine the latitude of the questioning, which is determined on the basis of whether it's appropriate for an interview for a position. That's the criterion I'm going to use.

We're going to continue. Unless this is a point of order, Mr. Crête, I'll continue on that basis.

Go ahead.

[*Translation*]

Mr. Paul Crête (Montmagny—L'Islet—Kamouraska—Rivière-du-Loup, BQ): Mr. Chairman, this is a non-issue. Reading Mr. Carney's presentation, it is clear that it deals with substantive issues. So, what we are talking about now is a non-issue. We have a brief that provides a great many details on important issues. As long as we ask Mr. Carney questions about what he discusses in his presentation, I don't think we will be out of line.

[*English*]

The Chair: Let's carry on.

Mr. Carney, the floor is yours. We look forward to your presentation.

Mr. Mark Carney (Adviser to the Governor, Bank of Canada): Thank you very much, Chair, and I do look forward to discussion of substantive issues.

I would like to begin by saying how pleased I am to be before this committee today to discuss my perspectives on the medium-term policy challenges facing the Bank of Canada. I am looking forward to many future appearances before this committee and its counterpart in the Senate, since a critical component of the bank's accountability to Canadians is having the governor appear periodically before parliamentarians to explain the bank's views on the economy, monetary policy, and the financial system.

I would like, however, to emphasize at the outset that I am not yet the governor of the Bank of Canada. Under the Bank of Canada Act, the current governor, David Dodge, remains very much responsible for Canada's monetary policy until the end of January. In recent years, the bank has operated under a convention whereby monetary policy decisions are taken on a consensus basis by the bank's governing council. I am also not yet a member of the governing council. In answering your questions today, I shall endeavour to comment neither on the current stance of monetary policy nor on the current economic outlook, so as to avoid prejudicing upcoming decisions of the governing council. I trust that all those listening will recognize those important caveats.

Reflecting my current position, I would like to focus on the principal medium-term policy challenges facing the bank. As set out in the preamble to the Bank of Canada Act, the bank's objective is “generally to promote the economic and financial welfare of Canada”. The bank achieves this objective by, first, conducting monetary policy to maintain a rate of inflation that is low, stable, and predictable; second, promoting the safety and soundness of Canada's financial system; third, acting as the Government of Canada's fiscal agent to provide efficient and effective funds management; and, fourth, supplying quality bank notes that are readily accepted and secure against counterfeiting. This last point, if I may, is very important to the bank, and we have worked closely with our partners in law enforcement, particularly the RCMP, and the retail sector to deter counterfeiting through bank-note-related education, communication, and compliance. These efforts have yielded important results, and they will continue.

With that introduction, I will concentrate the balance of my remarks on the bank's work in monetary policy and the financial system.

● (1540)

[*Translation*]

With respect to monetary policy, I am in the fortunate position of inheriting an exceptionally sound and robust policy framework. Over time, it has become clear that the best contribution monetary policy can make to the promotion of the economic and financial welfare of Canada is to keep inflation low, stable and predictable. Put another way, inflation control is not an end in itself; rather, it is the means whereby monetary policy can best contribute to solid economic performance. Specifically, the Bank aims to keep the annual rate of consumer price inflation at the 2 per cent midpoint of a 1 to 3 per cent control range. By doing so, monetary policy helps to keep the economy as a whole operating at full capacity and promotes sustainable economic growth.

Canada has been served extremely well by its inflation-targeting policy framework, which has been widely emulated. The Bank's exemplary record of inflation control has meant that we have avoided the destructive effects of high inflation prevalent in earlier decades—effects that were disproportionately felt by poor Canadians, and which reduced our output and increased our unemployment. Despite all the shocks that Canada has faced since inflation targets were introduced, Canada's real output since that time has expanded at an average rate of 3 per cent per year and the unemployment rate has fallen to levels not seen in more than three decades. As in countries where inflation targeting has been adopted, inflation and interest rates have generally been lower and less volatile.

An explicit inflation target was first formalized in a joint agreement between the Bank and the Government of Canada in 1991. Given its initial success, this agreement has been extended four times with small modifications; most recently, until the end of 2011. This agreement sets out one clear objective—the inflation target—and creates a transparent accountability framework for the Bank of Canada. The Bank supports that framework through frequent and open communication with Canadians. If inflation deviates from its target, the Bank will explain the reasons why, what it will do to return it to target, and how long the process is expected to take. It is important to underline that the Bank approaches inflation control in a symmetric way.

[*English*]

A floating exchange rate is a key element of our monetary policy framework. It allows Canada to pursue an independent monetary policy appropriate to our own economic circumstances. Although there is no target exchange rate for the Canadian dollar, the bank does care why the exchange rate is moving and what the potential impact will be on output and inflation.

The exchange rate is an important relative price in our economy. Movements in the exchange rate influence the levels of imports and exports, which can help keep total demand and supply in balance. Further, exchange rate movements act as a signal to shift resources into sectors where demand is strongest. A floating exchange rate helps to smooth that process and to minimize the adjustments in other areas of the economy.

The challenge for the bank is to understand the reasons behind currency movements, to incorporate those with our assessments of other data, and to set a course for monetary policy that works to keep total demand and supply in balance and inflation on target. This means that the bank has to make judgments about the causes and likely persistence of exchange rate movements, the speed and degree at which exchange rate changes pass through to domestic prices, and the possible impact of exchange rate movements on confidence, and through confidence, on consumption and investment.

It is true that exchange rate movements can be, and have been recently, rather volatile. In these circumstances, it is not surprising that some have called for Canada to fix its currency to the U.S. dollar. In my opinion, it would be a mistake to do so. It would mean that, de facto, Canada would adopt U.S. monetary policy despite the reality that the structures of our economy are very different and, as a consequence, often require different types of adjustments in response to global developments.

We cannot avoid adjustment. The question is simply how we adjust to global economic forces. With a fixed exchange rate, the adjustments would have to come through movements in overall output and in all wages and prices. History has shown that these adjustments are more protracted and more difficult than exchange rate adjustments. Again, however, I stress that this position does not mean the bank is indifferent to movements in the exchange rate.

Another important aspect of our policy framework is the need to be forward looking given the lags between policy actions and their effect on the economy. Indeed, a forward-looking perspective is essential to the success of inflation targeting. The joint agreement between the Government of Canada and the Bank of Canada on the inflation target has helped concentrate inflation expectations at around 2%.

More fundamentally, the successful management of monetary policy by my predecessors has created a self-reinforcing process whereby increased policy credibility further anchors inflation expectations, which then contributes to a more stable macroeconomic environment, which in turn enhances policy credibility. We should not underestimate the value of these hard-won gains, and I have no intention of forfeiting them.

Well-anchored inflation expectations help reduce swings in interest rates, lower the cost of borrowing to Canadians, contribute to a more stable, competitive cost of capital for our firms, and ultimately support more sustainable growth in output and employment.

Now, despite our successes, the bank has an obligation to Canadians to continually evaluate possible improvements to its policy framework. As a result, the bank has launched a concerted research program to examine whether and how the monetary policy framework in Canada might be improved. This program is focusing on the potential costs and benefits of targeting a lower rate of inflation and of pursuing a price-level target instead of an inflation target. And it is focusing on the challenges of communicating these potential changes to Canadians.

The bank will conduct this research and publish its findings in an open manner in order to encourage debate and suggestions. I will say that the research would need to uncover compelling evidence in favour of a change before we would want to alter a system that has proven so successful over the past 15 years.

The conduct of monetary policy over the coming years will be challenged by four underlying trends. Their precise speed is difficult to predict, but their influence will be impossible to ignore. These trends are as follows:

First is the globalization of product capital and, increasingly, given outsourcing and technology, labour markets.

Second is the resolution of global imbalances. This requires both stronger domestic demand in countries with large current account surpluses and the move to flexible exchange rate regimes in those systemically important countries that currently actively manage their exchange rates. As the bank has consistently noted, this process may proceed in an uneven manner.

Third is the pace and direction of financial innovation and integration. This has important implications for the degree of financial intermediation, the levels of nominal and real interest rates, and the monetary policy transmission mechanism.

● (1545)

Fourth is the evolution of potential growth in Canada reflecting the balance of profound demographic changes in developments in Canadian productivity.

These underlined economic and financial trends complicate the pursuit of our inflation target, not only because none is likely to proceed at a steady, predictable pace, but also because they are all interrelated. For example, global imbalances, financial integration, and historically low nominal interest rates can all be partially explained by the familiar process of global integration that is currently taking place on an unprecedented scale.

The bank must better understand these forces to effectively meet its responsibilities. It should also continue to share its perspectives on these broader trends so that individual Canadians, companies, and governments have the necessary context when making their savings and investment decisions.

● (1550)

[*Translation*]

The strength of our financial system will help determine the ultimate impact of these trends, since each has the potential to affect asset-price volatility and the stability of growth and employment. Where financial systems are strong and resilient, they cushion shocks, efficiently allocate resources, and help improve the effectiveness of monetary policy. Where they are weak, however, they can amplify the impact of shocks on macroeconomic activity and reduce the effectiveness of monetary policy. As a consequence, the Bank has a fundamental role to play in promoting the safety and stability of Canada's financial system.

The Bank's role in financial stability is at the heart of our legislated mandate to promote the economic and financial welfare of Canada. Before concluding, I would like to make five brief comments in that regard.

First, as Canada's central bank, we have legislative oversight responsibility for the safety and soundness of systemically important clearing and settlement systems.

Second, we play a central role in providing liquidity to facilitate the settlement of financial transactions. The Bank has traditionally undertaken open-market by-back operations only in Government of Canada debt, and offered standing liquidity facilities against high-quality collateral, in order to keep the overnight rate close to the target policy rate. However, recent events have raised questions over the appropriate role for central banks in the provision of liquidity in money markets. As my colleague, Pierre Duguay, noted last month, the Bank is currently examining whether some market failures might be addressed if the central bank had a facility that would provide liquidity at terms longer than overnight, possibly secured with a wider range of securities.

[*English*]

Third, the response to the recent turbulence in financial markets should reaffirm that market participants are fundamentally responsible for their actions. For example, investors must understand the price dynamics and liquidity risks of the products they buy, rather than relying solely on credit-rating agencies. The market is beginning to lead many of the necessary changes, as institutions are improving their liquidity management and credit discipline and as originators and distributors of new loans are beginning to adjust their products to standardize terms and, importantly, align incentives. At the same time, accurate and timely information about underlying risks is essential for the market to differentiate and properly price risk. Thus, as Governor Dodge highlighted in September, enhanced disclosure and transparency remain crucial.

Fourth, recent global events have underscored the importance of continued close cooperation among authorities in Canada. The bank will continue to work collaboratively with its partners, including the Department of Finance, OSFI, the Canada Deposit Insurance Corporation, and provincial securities commissions, to promote the safe and efficient operation of the key elements of our financial system.

Finally, the bank will continue to use its membership in international bodies and its extensive research capabilities to foster the safety, soundness, and efficiency of the international financial system. For example, the bank and the Government of Canada have actively promoted reform of the International Monetary Fund through a strengthened surveillance function. Strengthened surveillance can play an important role in the resolution of global imbalances and the development of a more robust international financial system. As part of the international response to recent market turbulence, the bank is also working through the Financial Stability Forum as that body considers possible changes to accounting and regulatory standards and the extent to which enhanced oversight can improve the management of credit and liquidity risk in global financial institutions.

In conclusion, let me say that it is an honour and a privilege to have been chosen to serve Canadians as the eighth Governor of the Bank of Canada. I am particularly looking forward to leading the bank's talented and dedicated staff as we face the challenges of the years ahead. I will do my best to live up to the very high standards of those who came before me and am confident that my experience in both the public and private sectors will help me contribute to the bank's important work on behalf of all Canadians.

Thank you very much for your time, and I look forward to your questions.

● (1555)

The Chair: Thank you very much for being here. It's an honour and a privilege to have you here.

We'll now start our questioning with Mr. McCallum. You have seven minutes.

Hon. John McCallum (Markham—Unionville, Lib.): Thank you.

Mr. Carney, welcome and congratulations.

My Liberal colleagues will ask some questions about the subprime mortgage crisis, the Montreal accord and income trusts, and I would like to focus on monetary policy, beginning with exchange rates, both the level and the volatility.

As you know, for many companies in manufacturing, the very high exchange rate is something of a killer, but I'd like to focus as much on volatility, because I think when you have the dollar going up by 10% and down by 10% in a matter of two or three months, that's pretty extreme volatility, if not unprecedented. I know from speaking to companies that volatility makes it extremely difficult to plan, and it also increases the number of those calling for some kind of fixed exchange rate system.

Given your fundamental commitment to inflation targeting—which I agree with—are you concerned about volatility? More to the point, is there anything the bank could or should or would do to limit or reduce that volatility compared with what we've seen in recent months?

Mr. Mark Carney: Thank you very much for the question. It's extremely important, and obviously extremely timely.

Certainly, we have seen substantial volatility in exchange rate markets recently, including that for the Canadian dollar. It's important to remember, as you know, that exchange rate markets, like all asset markets, can be volatile and can overshoot, and certainly the volatility we have seen in the Canadian dollar cannot be accounted for purely by changes in fundamentals.

We can discuss, if you wish—although you may not want to use the time—potential reasons behind that volatility, but I'll leave that to the side and go more to the substance of the question, which is what the bank can do.

I'll say, first and foremost, because it bears repeating, that the experience of the bank, the experience of Canadian monetary history, is that the best contribution the bank can make to the economic and financial welfare of the country is to focus on its principal and sole objective, which is to achieve an inflation rate that's slow, stable, and predictable.

In the context of doing that, as I mentioned in my remarks, the exchange rate does play an important role, and certainly exchange rate movements that are detached or somewhat differentiated from fundamental movements need to be considered in the conduct of monetary policy.

How do we consider them? We need to look at the reasons the exchange rate may have moved; we need to think through the persistence of those exchange rate changes. We've obviously seen a very sharp spike up and rapid return. Then we need to think about the consequences of this for the economy, all in the context of achieving the exchange rate target.

What specifically can the bank do? I do not favour a pegged exchange rate. I do not favour a monetary union. We can go into more detail on why, if people wish to later. But I think there is a premium on the bank communicating openly with Canadians, being open with the market about the potential impact of these changes on output and, ultimately on inflation, and providing a sense of stability as its objective function.

The way to inject more volatility into asset markets, whether they're interest rates, exchange rates, or equities, is to be perceived to change between targets. I would submit that at the bank we need to retain focus on the inflation target, explain what we're doing, explain what the potential consequences are of exchange rate movement, differentiate between the potential reasons behind that, and the market will adjust accordingly.

Hon. John McCallum: I totally agree with you on the inflation targets. Given those targets, I think that excessive volatility can be a negative, in terms of business planning and so on. So would you see the use of instruments like intervention or talking the currency up or down, or other things that you can do to enhance currency stability, without sacrificing your basic philosophy of inflation targeting?

● (1600)

Mr. Mark Carney: Terms such as “talking the currency up and down” or “verbal intervention” are not terms we use at the Bank of Canada—I'll make that clear—again keeping to the framework.

You asked about intervention. As you know, and other members would be aware, the bank has not intervened in the exchange rate market—in the exchange rate market for the Canada dollar, to be more precise—since 1998, since the Asian crisis. That does not mean the bank will never intervene in exchange rate markets.

We have a clear policy, which is on our website, that specifies the occasions when the government—the bank, as agent on behalf of the government—might intervene in exchange rate markets. They're twofold: one is a breakdown in the actual market—gapping, lack of liquidity in the exchange rate market.... Interestingly, we saw an example of that in the Australian dollar during the summer. We haven't seen it in the Canadian dollar. The other is if, in the judgment of the governor—in the judgment of the bank—an excessive move has the potential to seriously undermine the economic prospects for the country.

I'll make one other point. Intervention is a joint decision. Intervention implicates the exchange fund account of the government, which is the property of the people of Canada, and so would be made jointly with the Minister of Finance.

Hon. John McCallum: Thank you.

I would say there's a cyclical element in Canada in calls for a monetary union or a fixed exchange rate or a North American common currency. They tend to become more intense when the dollar is extremely high or extremely low or extremely volatile.

I think it's fair to say that Quebec separatists always want a monetary union because it becomes easier to separate. But we have other respected people today calling for a monetary union.

My question for you, very quickly, is this. It seems to me that Europe is not North America and that the notion that we would have a North American common currency called an “amero” is totally out to lunch. I wonder whether you'd agree with that.

Mr. Mark Carney: It's a big question, so I welcome it being asked again.

Very quickly, I agree with the point, and I would love to go through the reasons why I agree with the point, but in the interests of time, I'll pass to the chair.

The Chair: Thank you very much.

We'll now go to Monsieur Crête. You have seven minutes.

[*Translation*]

Mr. Paul Crête: Thank you, Mr. Chairman.

Thank you, Mr. Carney.

I want to thank you for that substantial presentation. I believe some ministers would do well to follow your lead in terms of the presentation you made. However, that does not mean that we agree with everything you said.

In your presentation, for example, you said:

> The Bank's role in financial stability is at the heart of our legislative mandate to promote the economic and financial welfare of Canada.

Given the current reality in Canada, with the surge in energy prices, there are, in a way—although you probably would not put it this way—two economies in Canada: the western economy, where there is a significant inflationary trend, and the central economy, in Québec and Ontario, whose situation is completely different.

Do other mechanisms need to be developed for there to be appropriate consideration given to these two sides, which may seem contradictory?

Mr. Mark Carney: Thank you for that question.

If I understood you correctly, you are talking, in a way, about a two-tiered economy—a manufacturing economy, on the one hand, and an energy economy, on the other. It is absolutely fundamental that the Bank of Canada manage monetary policy for the Canadian economy as a whole. In order to do that, it closely follows the different sectors of our economy. I am well acquainted with the problems in the manufacturing sector, and particularly the forest industry in Canada. I know CEOs and individuals who work for these companies. Indeed, I have just met with representatives of forestry workers.

We look at the details, but we manage the two economies together.

● (1605)

Mr. Paul Crête: I understand. I would like to come back to the question of volatility, because business is telling us it's very difficult to predict what the dollar's value will be when the time comes to sign contracts. I asked your predecessor, when the dollar was worth 85¢, at what point it becomes more costly to manage volatility, when you have an independent Canadian currency.

However, I would rather ask you to tell me what elements of volatility require special consideration to ensure there is no negative impact on the economy.

Mr. Mark Carney: I would like to repeat one important point. The recent volatility of the Canadian dollar cannot only be explained by the fundamentals. That is very clear, as I stated in my answer to Mr. McCallum. The best thing the Bank of Canada can do is manage the inflation rate and try to ensure that it is low, stable and predictable. Trying to attain that goal is the most useful thing the Bank of Canada can do to reduce that volatility. As I said in my answer to the last question, it is important that the Bank of Canada continue to talk about and raise awareness of that particular point and its goal of stability.

Mr. Paul Crête: That's fine, but how can that be achieved? If more Canadians understood all the fine points, we might indeed end up with better results and all the different factors would adjust in a more nuanced fashion. But how can we achieve that?

Mr. Mark Carney: That's a very good question. First of all, we have to attend meetings such as this one, and discuss these points with Members of Parliament and Canadians. That is one of the responsibilities of the Governor of the Bank of Canada. His job, in a sense, is to explain to Canadians what our inflation control framework is all about. That is very important.

In my opinion, it is important to realize that it is difficult for people to understand a policy that is too complex. People may think about inflation one day, but not the next. They may think of it one year, but not the next. Our policy is simple: we are aiming for a low, stable and predictable rate of inflation of 2 per cent annually, year after year. I am talking about the overall consumer price index. It is important to have a simple, clear and effective policy. And, everything points to the fact that our policy has been meeting those objectives for the last 15 years.

Mr. Paul Crête: I have one last question. As part of your mandate, do you believe you have a duty to consider the possibility that Canada may fall prey to something like Dutch disease? You know what Dutch disease is: it's when an industry boosted by the energy sector has negative impacts. In terms of your mandate, do you believe that this will be an important or crucial issue in the coming years in Canada?

Mr. Mark Carney: There are several points to be made here. First of all, the Bank of Canada always has to consider such issues or eventualities. There is one fundamental point in that regard, however, and it is that our economy is highly diversified. You cannot just say that we have an energy sector, a forestry sector and that's all there is. Our economy is highly diversified, and the services industry is very significant. It has had great success in recent years. There are also a lot of jobs in that industry that pay higher than average salaries. So, I see this as one aspect of monetary policy, but at the same time, our economy is highly diversified, and that is an even more important fact.

● (1610)

[*English*]

The Chair: Thank you very much. Now we'll move for seven minutes to Mr. Menzies and Mr. Dykstra.

I believe you're sharing your time, Mr. Menzies. The floor is yours.

Mr. Ted Menzies (Macleod, CPC): Yes, I will.

Thank you, Mr. Chair, and thank you, Mr. Carney, for appearing at our committee.

I'm very encouraged to hear your comment that this committee can indeed play a role, whether it be an advisory role or simply a questioning role. That's good to hear.

First, congratulations on your appointment. We do wish you well in your decision-making in the future in setting monetary policy in Canada, and please convey the thanks of this committee to the gentleman you will be replacing, David Dodge. It's a challenging job, and we thank him for his leadership in that role.

An hon. member: Hear, hear!

Mr. Ted Menzies: We're all very well aware—in fact, this committee has spent quite a bit of time recently talking to different organizations from across the country—of the impact of the Canadian dollar vis-à-vis the U.S. dollar. Many countries are experiencing some turbulence in their monetary markets. We saw the credit crunch in the U.S. due to those subprime mortgages.

I was interested in your view, in your present position—and I respect that you're speaking today as an advisor to the governor—of what the Bank of Canada's role will be in the future, if you can explain it to us, in dealing with this issue. We realize the Montreal proposal is helpful, but where do we go from there? You comment about a wider range of securities in dealing with things like this, so could you share that with us, please?

Mr. Mark Carney: Thank you for the question. I do want to leave this as one of the messages in my remarks, but these issues are very topical and very important, and I think they will extend well into the first year, certainly, and potentially beyond the work program of my tenure at the Bank of Canada. So it's not only a current topical issue; these are deeper issues.

I'll reiterate that there is a very fundamental role for the bank in financial stability. Financial stability and monetary policy are very tightly linked.

The first thing we do is to make sure we provide liquidity. We set an overnight target rate. It was changed yesterday, as you all know, and we want the actual rate in overnight money markets to be the overnight target rate. So we provide—it seems sensible—liquidity into the overnight market occasionally, as required, in order to ensure that on average the overnight rate is the target rate. We have done that recently, and we have done it frequently, I guess, since August. It's common to other central banks around the world during this time of some stress in the money markets.

The issue is, what happens between the overnight rate and the rates about three months out? What you have in Canada is a fairly steep, unusually steep, yield curve going from overnight to three months out, and three-month rates are important rates for financial institutions.

The curves in the U.S., in Europe, and in the U.K. are much steeper than they are in Canada. So if we have an issue, it's a bigger issue elsewhere. And the question is—and this is what I was referring to in terms of instruments—what can the bank do or what should the bank potentially do to ensure that there is necessary liquidity further out so that changes in the overnight rate are transmitted out along the curve?

I will make one side point, if I may—it is simply an observation—which is that the change in the overnight rate yesterday has resulted in a lowering of that curve. So while the curve is still steep, at least it is moving with the overnight rate.

That's some of the aspect of what we're looking at in terms of providing some term liquidity. It is a very topical issue. It's being discussed, and you will see it consistently south of the border and in Europe, where they quite frankly have more flexibility in that overnight to three-month area than we currently do at the bank.

The other things we need to do, very quickly.... I think we need to consistently monitor the situation, both from a macroeconomic perspective and to bring it on down to individual institutions, and that's where we work with OSFI, the Department of Finance, and CDIC to make sure everybody has a best sense of the situation. I should reiterate for the committee that the bank is the lender of last resort, if necessary, to federally regulated institutions, solvent but illiquid federally regulated institutions, and we are actively working internationally through the Financial Stability Forum to provide our input to broader reforms.

A last point, though, and I don't want to leave any doubt, is that there is a fundamental principle here that what we're trying to do is make sure that current issues in the financial system do not propagate into the broader economy and impact the broader economy. But there is a principle that market participants should bear the consequences of their actions, so we need to strike the right balance between those two very important principles.

● (1615)

Mr. Ted Menzies: Are we just about out of time?

The Chair: You have time for one more quick question, if you'd like.

Mr. Ted Menzies: I know Minister Flaherty just recently was in a meeting with the IMF. Can you describe for this committee the connection between the bank and the IMF?

Mr. Mark Carney: Yes, very briefly, what we have tried to do, what Governor Dodge has tried to do, and what the Government of Canada has tried to do is to help revitalize the IMF. There are two ways to do that. I reference surveillance. I won't bore you with the details of surveillance, but the core aspect is that the IMF, in surveying economies, should be much more frank and direct in terms of their assessment of those economies, the policies the countries are following and the impact of those policies on other economies. You can think of Asian economies who may be targeting their exchange rate, running an export-oriented economic policy that has impacts in terms of the distribution of changes in exchange rate and interest rates around the world. They should be more frank and direct, and the IMF itself should serve as a forum where you get policy-makers around the table to talk more frankly to each other about what needs to be done to come to a coordinated solution.

The Chair: Thank you very much.

Now we'll go to Mr. Mulcair. You have seven minutes.

[*Translation*]

Mr. Thomas Mulcair (Outremont, NDP): Thank you, Mr. Chairman.

I want to begin by welcoming Mr. Carney and thanking him for accepting our invitation, although we would have liked to have been sufficiently interesting to attract him when he was in London. But we are happy to see him today.

I also want to say that one of the first articles written about him that I read said he was taking French courses.

So, you've done that. Good for you! The answers you gave my colleagues from the Bloc Québécois reflect your academic background: you learn very quickly and your answers were excellent.

This has nothing to do with you, but I find it regrettable that, in the history of Canada, there has never been a Francophone Governor of the Bank of Canada. However, you do speak French which, by definition, makes you a Francophone. I want to extend my sincere congratulations to you on the quality of your French, as seen in the way you expressed yourself today in front of the Committee.

I am a little like my friends in the Bloc Québécois. I am somewhat concerned about the destabilization of our economy right now, with the overheating that is occurring in the oil patch. I am going to get started because I have a feeling, based on the way the meeting has been going, that we will have two rounds.

[*English*]

The Chair: I can't guarantee you'll be back on, but I know we will have four rounds in total.

[*Translation*]

Mr. Thomas Mulcair: I want to begin by asking you a question about income trusts.

In your previous position, as an expert, you played an active role in the economy, and that had a significant influence. As you know, our political party was not favourably disposed towards income trusts. However, we never lied to people the way the government did.

This is what I would like to know. In your view, in light of what has occurred with income trusts, have the basic premises that were behind your recommendation proven to be accurate? I am going to cite the specific example of Abu Dhabi National Energy Company, which has purchased certain income trusts, including PrimeWest Energy Trust.

In your opinion, are these new companies, which are now managed offshore, contributing to the Canadian economy in terms of tax revenues? That was one of the basic premises underlying the decision you presided over.

● (1620)

Mr. Mark Carney: First of all, I want to thank you for congratulating me on my French. It's probably too soon, and I apologize for that. I am going to continue to work hard.

But let me get back to your question. When the income trust decision was made by the government, as you know, I was a senior official with the Department of Finance. The role of a senior official is to provide advice and implement decisions. So, I provided advice, obviously, and the government made a decision. Parliament then approved the decision made by the government. As I see it, it's quite simple. That is the role of a senior official.

And I would like it to remain that way, because I will be the next Governor of the Bank of Canada, and the role of a Governor of the Bank of Canada is not to comment on every initiative that is approved.

Mr. Thomas Mulcair: I want to reassure Mr. Carney. I am not asking him to comment on the merits or appropriateness of a decision. He is here to speak to us as someone with a certain vision based on his training and experience, and we want to entrust to him one of the most important tools we have in our economy for the next seven years.

I am using a concrete case: income trusts. He made the case that income trusts lead to tax leakage and that there was a need to stop the leak.

Based on the experience since then, did that theory turn out to be accurate or has there been a realization that with foreign companies talking control of these income trusts, the tax landscape hasn't improved? This is an objective question that I'm putting to him, and not a subjective question aimed at soliciting a personal opinion.

Mr. Mark Carney: There are several reasons why the government made that decision, including tax leakages, questions related to productivity, and the principle of a neutral system of taxation in terms of its impact on different industry sectors, companies and regions. That is a general question which I can comment on as the next Governor.

In our opinion, because of international competition and the value of our currency, it is very important for our economy to be able to adjust. Thus it is useful for labour markets to be flexible, for there to be free trade between the provinces, and for our tax system to be as neutral as possible.

Mr. Thomas Mulcair: Is my time up?

[*English*]

The Chair: Thank you very much.

We'll now move on to Mr. McKay. You have five minutes in this round.

Hon. John McKay (Scarborough—Guildwood, Lib.): Thank you, Chair.

Thank you, Mr. Carney, for coming, and I want to add my personal congratulations to your anticipated appointment.

Mr. Menzies has partly anticipated some of my questions with respect to asset-backed commercial paper, and I know you've been involved in all of those discussions in Montreal. You alluded, on page 5 of your reference, to your colleague, Pierre Duguay, talking about that the facility that would provide liquidity at terms longer than overnight, and you did in part respond to Mr. Menzies on that point. If in fact that is a change, is that a policy change, a regulatory change, or a legislative change? That's question number one.

The second question is this. If in fact it is implemented, is this simply in effect the Bank of Canada bailing out an institution that made poor financial decisions because you're changing monetary policy in order to respond to the turmoil in the market?

As my third question, is that turmoil in the market in part what precipitated the interest rate cut, and would you agree with Doug Pottier's statement from Nesbitt Burns? He said, “I think it was the ongoing turmoil in financial markets and the very real risk it's morphing into a macroeconomic event.” Would you agree with that statement?

And the fourth question is—

● (1625)

Mr. Mark Carney: That was the fourth question.

Hon. John McKay: Well, when you have five minutes, you've got to pack it in here.

The fourth question has to do with other regulatory institutions involved in these kinds of decisions. Do you think our regulatory system is up to the challenge of things such as asset-backed commercial paper risk?

Mr. Mark Carney: Thank you for those questions.

This issue—the new facility, policy, or regulatory change—is something we are studying. In the context of looking at it, we will have to form a judgment about whether legislative change is required in order to enact it.

Just for education—some of you may know this—the Bank of Canada has very broad powers under paragraph 18(g) of the Bank of Canada Act, but they're powers in the case of a serious financial disruption, and that has to be declared. It can be declared *ex post*, but it has to be formally declared and gazetted by the governor.

It has some broad powers there, and what we're looking at is not something that would fall under this, but would be...not quotidian but a more regularly used vehicle. You can think about it as potentially akin to the Federal Reserve's discount window, which has been recently used.

Then the judgment needs to be made: is there a need for legislative change? If there's a need for legislative change—obviously, we'll take a conservative view on that—we would have to come back to explain it to this committee and to the House.

I have four more questions—

Hon. John McKay: Just before you leave that point—I'm not likely going to get them anyway—there is the issue of what a serious financial crisis is, and I've forgotten the exact phrasing. Is that the same phrasing or declaration that is needed to precipitate the guarantees that go with the asset-backed paper? There's a cascading set of guarantees on those.

Mr. Mark Carney: No. You're referring to a very technical point, general market disruption, which is a term of art of lawyers in liquidity agreements for these asset-backed CPs, and there's a very wide range of it. This has nothing to do with that.

On your question about bailing out, I want to repeat what I said earlier. It is extremely important that financial market participants bear the consequences of their decisions, and this is one aspect that has to be balanced. What we have to make sure is that the consequences of the difficulty in financial markets don't fall on the shoulders of all Canadians when trying to teach a really harsh lesson to those participants.

Is the regulatory system up to it? It's a very important point. I said in my remarks, and I believe it's fundamental, that one of the advantages of the Canadian system is the degree of cooperation among the principals: OSFI, the Bank of Canada, the Department of Finance, CDIC, and, importantly, the provincial securities commissions.

Some of this is legislated, but it is a question in practice where people get together, talk about issues, meet regularly, and work in a cooperative fashion. We need that, or we may need it, in the coming months.

● (1630)

The Chair: Thank you very much.

Monsieur St-Cyr, you have five minutes.

[*Translation*]

Mr. Thierry St-Cyr (Jeanne-Le Ber, BQ): Thank you, Mr. Chairman and Mr. Carney.

I want to pursue the line of questioning with respect to the volatility of the exchange rate and the high Canadian dollar overall, because this has important repercussions—everyone agrees on that—for the manufacturing industry, but also the farming industry and a number of other sectors. It also has significant consequences for the tourist industry.

If I understood you correctly, you believe the Bank of Canada's fundamental role is to continue to pursue inflation control. I take from that that the problem should resolve itself. However, other banks across the world are succeeding fairly well. They influence exchange rates by using interest rates and their monetary reserves to purchase or sell currencies. I'm wondering whether the Bank could at least consider that type of intervention.

It seems to me that we should be seriously considering the possibility of a monetary union, as suggested by some, albeit outside considerations that are often more emotional than they are rational. We saw this with Mr. McCallum's comments earlier, when he made the connection between this issue and sovereigntists, when in fact Mr. Jarislowsky—who is not known as a hard-core sovereignist, was the one who came before us to talk about monetary union. There is a monetary union in Europe.

Mr. Jarislowsky also talked about another solution, which would be to establish a target range, a little like what is done for inflation control. We say it should be 2 per cent, or midway between 1 and 3 per cent. Could the Bank consider the option of having a target range, saying that it would like to see the dollar at 80¢, plus or minus 10¢, and intervene on that basis? Is this something that you could look at and that we could debate outside of what are often more sentimental or emotional, as opposed to rational, considerations?

Mr. Mark Carney: Thank you for those questions.

First of all, the Bank of Canada's intervention policy continues to be an option in Canada. Although rarely used—I believe that is correct—it is nevertheless an option. We can intervene in cases of market failures or when the value of our currency could have a serious impact on our mid-term economic prospects.

Second, history has shown us that if an intervention is not accompanied by other measures, it just doesn't work. If it only has an effect for a day or a week, it will be a failure. All that does is put money in the pockets of speculators, in my opinion.

Another very important question has to do with monetary union, which involves a lot of disadvantages. It has the advantage of reducing transaction costs, but the disadvantage is that it leads to a loss of monetary sovereignty. Monetary sovereignty is important for economies which are very different, such as those of Canada and the U.S. There is a greater difference between Canada and the United States than there is with France or Germany, for example. Another disadvantage of monetary union is that the Bank would lose its accountability. Financial stability raises certain issues, particularly the matter of who will act as the lender of last resort.

I was living in Europe at the time the euro was adopted and I know a number of executives who were involved in that process. The pooling of sovereignty was a major political issue. It was a way of achieving political union among the countries. The choice of the euro is more of a political choice than it is an economic choice.

● (1635)

Mr. Thierry St-Cyr: It's sovereignty-association.

[*English*]

The Chair: I'm sorry, but your time has gone. We'll move to Mr. Dykstra.

Mr. Dykstra, you have five minutes.

Mr. Rick Dykstra: Through you, Chair, to Mr. Carney, I'm sorry to take some of the time, as that sounded like a good conversation.

I have a couple of questions. We certainly recognize that the Bank of Canada has responsibility for monetary policy and that there are certain tools the bank has to affect the value of the dollar. Obviously, it will be up to you, when you do become the governor of the bank, to choose to exercise them or not. We also recognize—although some folks on the other side of the table may not agree—quite frankly, that monetary policy is complex and that it's certainly best left in the hands of the governor.

A couple of issues we have tried to benchmark as a government are transparency and accountability and trying to ensure a new culture of openness with respect to government. I wonder if you could comment or commit to this committee that those approaches are ones you'll also endeavour to continue at the bank.

Mr. Mark Carney: Thank you very much for the question.

This point about transparency and openness and open communication is extremely important. Part of what I mentioned in my remarks was the importance of expectations in driving monetary policy.

We had an earlier conversation about expectations grouping around 2%. I think experience has shown that it doesn't just matter that inflation is 2%. The conduct of monetary policy doesn't just matter; it's how you get there and how well people understand how you get there. And the way you encourage that is through dialogue such as this and other outreach efforts. So transparency is a huge element of that. It's been a hallmark of the Bank of Canada.

We need to continue to look at ways to further enhance that and to further improve our communication. We need to further improve—and we do look at—our regular publications, including our *Monetary Policy Report* perhaps. I will give you some examples of things that one could look at, including looking back at previous decisions and what the expectations were and, more explicitly, saying what the bank's expectations were, and how things turned out and why things were different. There's an accountability element there.

The other element some banks have looked at—and it's more difficult to do this in a consensus-driven organization, but still possible—is the publication of minutes following decisions. So with a lag, the publication of minutes gives a better sense of the range of possible outcomes and the range of considerations that were given to a decision. The Reserve Bank of Australia, for example, last week just announced they will do that as well.

An extreme version of this is the publication of an interest rate forecast. I don't think that fully makes sense, but it's something that one looks at in a fuller review of the inflation-targeting framework.

A last point, if I may, would be to put in a little plug for a website, www.inflationtargeting.ca. I know you all have it in your bookmarks. That is the website of our research program that I alluded to at the start. We want to use that as a forum for open discussion or wiki-type discussions and serious research, but also practical discussion of the next framework we would be discussing for four years' time.

Thank you.

Mr. Rick Dykstra: Well, I think it's interesting to see the obvious coming of age of the Bank of Canada if its next governor gives a plug for its website, in terms of what you're looking at.

Some hon. members: Oh, oh!

Mr. Rick Dykstra: That's great.

One of the things you noted in your opening remarks—and I know you didn't have a whole lot of time to do this—was the whole aspect of deterring counterfeiting through bank-note-related education, communication, and compliance. It's obviously an issue both within the country and in our external relations with other countries to try to make sure that counterfeiting is deterred, and the aspects of it that have weighed heavily upon countries over the last number of years.

I wonder if you could just comment a little further on your commitment to that and on working with the RCMP.

● (1640)

Mr. Mark Carney: Thank you very much.

This is very important. This goes right to the heart of confidence in money as a store of value and a unit of account. I'm sure most are aware that we underinvested in banknotes in the previous decade, and, partly as a consequence of that, counterfeiting spiked up in Canada to unacceptably high levels.

It's a bit like inflation. Once you let this get away from itself, you have to work really, really hard to get it down. What the current governor and the bank put in place a few years ago was a three-pronged strategy, part of which is education, part of which is working with crown prosecutors to make sure it's prosecuted, and part of which is working with law enforcement. I said a three-pronged strategy, but I meant four-pronged, because the other prong is higher-quality banknotes, which the bank has introduced, as you've no doubt seen.

There has been a very sharp fall in counterfeiting. It's still too high, though. It's headed in the right direction, and we're going to drive it all the way down, and then we're going to keep doing that.

The RCMP has been extremely effective in this. I will tell you that the current governor and I met with the commissioner and the deputy commissioners of the RCMP just last week to talk about the next steps in this process.

This is important, but the message I'd like to leave with you is that we're making real progress on this. As a last point on accountability, we have these figures on our website to show where progress is being made.

The Chair: Thank you very much.

We'll now move to Mr. Turner for five minutes.

Hon. Garth Turner: Mr. Carney, you've been called the architect of the Conservative government's income trust strategy, and I'm wondering if that's a fair characterization.

Mr. Mark Carney: I was a senior public servant, as you know, in the Department of Finance. Quite frankly, I was a senior public servant under the previous Liberal government and under the current Conservative government. I ran the last five budgets and all tax decisions that were put forth by both governments. I think it's safe to say I was involved, yes.

Hon. Garth Turner: In terms of income trusts, you basically gave the same advice to Finance Minister Goodale as you gave to Finance Minister Flaherty.

Mr. Mark Carney: I gave the best advice I could to both finance ministers.

Hon. Garth Turner: Was it similar?

Mr. Mark Carney: The advice of public servants to their ministers is covered by cabinet confidence. That's the way the system works, and I gave the best advice I could to those ministers.

Hon. Garth Turner: All right. A year after the decision, more than $40 billion in Canadian trusts have been sold, and it would appear the better part of a billion dollars' worth of tax revenue is not flowing into the government treasury as it was before.

Given that, I have two questions. One, did you anticipate the consequences of the advice you gave the minister? Secondly, how can you consider it to be anything other than a failure?

Mr. Mark Carney: I'll refer to my previous answer, which is that I'm not going to go into the details of advice given to any minister of finance or any minister of the crown that I gave as a public servant.

I will point out, though, as a macro fact, that over the course of the last year and a half, as I'm sure you're aware, the TSX, the largest market, is up substantially. We have a $1.6 trillion market cap on the TSX. It's important to keep context—

Hon. Garth Turner: I know that, and I'm not interested in the TSX—

The Chair: I'm sorry, Mr. Turner, allow Mr. Carney to finish answering the question.

Hon. Garth Turner: No, I'm not, because that's not what I asked him. He can answer a question I didn't ask him if he wants—

The Chair: Do you have another question, Mr. Turner?

● (1645)

Hon. Garth Turner: Yes, I do actually.

The Chair: Then ask it quickly.

Hon. Garth Turner: Stop interrupting me and I will.

It's estimated, Mr. Carney, that—

The Chair: Mr. Turner, a little respect for the chair or you'll have no more time left.

Hon. Garth Turner: Is this coming off my time?

The Chair: Right now it is, yes.

Hon. Garth Turner: Well then shut up, please, if you don't mind.

I would ask, Mr. Carney—

Mr. Rick Dykstra: A point of order—

Hon. Garth Turner: I get my time or I don't.

Mr. Rick Dykstra: I'd ask Mr. Turner to respectfully withdraw the comments he just made. They are completely unparliamentary.

Hon. Garth Turner: I withdraw them.

The Chair: Mr. Turner.

Hon. Garth Turner: I just said I withdraw them.

The Chair: All right. Now ask the question or it will be the last you speak in this committee.

Hon. Garth Turner: Don't threaten me, Chairman.

The Chair: I just stated a fact, sir. Now carry on or you're done.

Hon. Garth Turner: Mr. Carney, I have a question for you. Do you believe that income trusts have a place in the capital markets?

Mr. Mark Carney: I believe capital market participants will make appropriate decisions, in terms of the structure, with which to organize businesses and which securities to buy or sell. That is a decision for capital market participants. A framework exists with tax neutrality between various corporate structures, and market participants make the decision about which structure and which entity to purchase.

Hon. Garth Turner: Did you anticipate the drop in market capitalization of income trusts following the decision on October 31? Was the extent of that anticipated?

Mr. Mark Carney: I'll refer to my earlier answer on advice to ministers.

The Chair: Thank you very much. You're done.

Mr. Del Mastro, you have five minutes.

Mr. Dean Del Mastro (Peterborough, CPC): Thank you, Mr. Chair.

I will pick up on that briefly.

Mr. Carney, on an aggregate scale, does it make any sense to look at markets in isolation and not take a look at the broader TSX, see the growth in the TSX, and see that investment that has gone from one area has likely gone to another?

Mr. Mark Carney: From the conduct of monetary policy, and looking through to the growth and output, the impact on employment, and ultimately, for us, the impact on inflation, it makes sense to look at wealth in aggregate. The big bits of wealth are equity market capitalization in aggregate, the performance of fixed income security, and, very importantly, housing wealth.

Mr. Dean Del Mastro: Thank you. I appreciate that.

I understand. Mr. Turner had an agenda. He actually supported the government decision on income trusts last year and he's just got a very short memory.

Mr. Carney, a lot of actors—

Hon. Garth Turner: A point of order, Mr. Chair.

The Chair: I don't think there's a point of order here.

Hon. Garth Turner: Yes, there is a point of order because Mr. Del Mastro—

The Chair: That's not a point of order; that's debate.

Carry on.

Mr. Dean Del Mastro: Thank you, Mr. Chair. I think the record will show I'm factual, in any event.

Mr. Carney, a lot of actors in the economy out there, especially manufacturers struggling to remain competitive, feel that the value of the dollar is too high and that the Bank of Canada, instead of just focusing on inflation, should adopt a monetary policy that would lower the value of the dollar.

Could you explain to the committee why it is important to our country for the bank's monetary policy to aim at maintaining a low and stable inflation rate?

Mr. Mark Carney: Thank you for that.

One of the problems with success is that you forget why you put in place the framework to begin with.

As I said in my remarks, we've had 15 years of low, stable, and predictable inflation. We owe it to my predecessors and the excellent and dedicated staff at the bank for achieving that success, but we have had 15 years, and people do forget about the costs of inflation. The cost of inflation, I want to emphasize, is what we risk putting in peril if we take our eye off the ball, and I want to assure you I will not take my eye off the ball.

Inflation erodes the value of money. I will put an aphorism in, a Yogi Berra: a nickel ain't worth a dime any more. That is the reality. We see the debate about what to do with a penny; ultimately, that's the consequence of years of inflation compounded.

Second, inflation creates uncertainty. It creates uncertainty and has a marked impact on investment and consumption, but investment ultimately, and output and jobs.

Third—and I mentioned this in my remarks, but it really does bear repeating—inflation affects the most vulnerable. It's the poorest people in society who are least well positioned to hedge against inflation and least well positioned to use sophisticated financial products or contracts to protect themselves.

The fifth and most important point when we think about inflation—I shouldn't say the most important point, but the fifth point—and one that really does bear emphasizing, is that inflationary booms always end badly, and you often get a boom when you start to have a run-up on inflation. They always end badly, and Herculean effort is required to put us back onto the path we were already on.

Right now we have low, stable, predictable inflation. We have expectations well anchored. It's incredibly valuable. To those who think about changing the target or adding additional targets when we only have one instrument, I would point out the risks they run in terms of impacting all these costs.

● (1650)

Mr. Dean Del Mastro: In short, maintaining low inflation is a measure to avoid recession.

Mr. Mark Carney: You cannot guarantee it, but it is consistent with it.

As I said in my remarks, the experience of inflation targeting has coincided with the second-longest expansion in our history and low volatility around output and interest rates.

Mr. Dean Del Mastro: Just for the benefit of Canadians, can you explain the difference between core inflation and what factors are taken out when you measure core inflation?

Mr. Mark Carney: Thank you for that.

As you know—and it bears repeating—the bank targets total inflation. That's the objective, because that's the basket Canadians recognize in terms of consumption. There is volatility around eight items in particular in that total basket of 31, particularly related to food and energy, so we take those out in terms of our day-to-day targeting. We are mindful of them, and we look at core inflation, which is very highly correlated.

When we do that—and this is important, and I talked about those four big trends—we have to be mindful of whether you can get upward drift in those items, and we have seen a strong upward drift in energy. We are starting to see globally a strong upward drift in agriculture. Even within core, because of China in particular being integrated, there is a strong downward drift in manufactured goods, so we have to be mindful.

It works, but it's not the sole method.

The Chair: Thank you very much.

Mr. Pacetti, you have five minutes.

Mr. Massimo Pacetti (Saint-Léonard—Saint-Michel, Lib.): Thank you, Mr. Chairman.

Congratulations again, Mark.

I suppose this is part of an interview process, so I am going to get rid of the thorny questions first. This was the favourite Conservative question when we had nominations from apparent Liberals coming before committees.

Have you been a member of a federal political party, Mark, in the last five years? That's just to make it easy on you.

Mr. Mark Carney: We'll go farther back. I've never been a member of any political party, no.

Mr. Massimo Pacetti: Okay, great.

Now take me through the process. What happened? Did you apply for this position? Did somebody approach you? How did that come about?

Mr. Mark Carney: I applied for this position. There was a public announcement that you would have seen in major Canadian papers and internationally, and I applied for it. It was just like for any other job.

Mr. Massimo Pacetti: Subsequently there was an interview process. How did that...?

Mr. Mark Carney: There was an interview process. There is a board of governors of the bank—not the board that makes the policy decisions but a board of governors of the bank that represents various provinces in the country. There's an executive committee of the board. That executive committee—

Mr. Massimo Pacetti: Was the finance minister involved in that at all?

Mr. Mark Carney: The finance minister is not on the board.

Mr. Massimo Pacetti: He is not on the board.

Just take me through—some of the members have spoken about it—your involvement in the income trust decision. How about the Montreal accord? How much involvement did you have in the Montreal accord, and what were your responsibilities there?

Mr. Mark Carney: In my position at the Department of Finance I had overall senior oversight responsibility for international operations in the financial sector, as well as budgetary responsibilities, and I was the alternate member of FSC, which is the financial stability committee, if you will. So it was in that context that I was involved, and continued to be involved, in the development of the Montreal accord, up until my getting this position.

My role and the government's role was I think to play a coordinating role, when events were moving extremely fast, and to ensure that all parties were aware of the potential consequences of their decisions and the potential value of sitting down and negotiating, taking a period of time and seeing whether there was a better solution than just running against the wall. But it was up to the parties to make that decision.

● (1655)

Mr. Massimo Pacetti: I don't mean to interrupt you. It's just that our time is limited and I'm trying to get to a point here.

Was there anybody from the Bank of Canada present at that meeting?

Mr. Mark Carney: These were individual conversations. We did not convene a meeting of all participants. That was done by the participants. They took the decision to do that.

Subsequent to the accord, there was a meeting of the Governor of the Bank of Canada, me, other representatives of the Bank of Canada, and some of the principal investors.

Mr. Massimo Pacetti: Right, but you were there at the time representing the Department of Finance.

Mr. Mark Carney: Yes.

Mr. Massimo Pacetti: Okay.

Now what happens if in the future, because we don't know where this asset-backed commercial paper is going to go...? We don't know. We're still not sure how much is really bad out there, and we don't know what the crisis is going to be in terms of the banks actually claiming the right amount of writedowns in the numbers we're seeing.

What's going to happen if we have a Northern Rock type of example? Would you be responsible for that? Are they going to say to you that you gave them advice, you helped them out on the deal making, and now that you're the Governor of the Bank of Canada you're responsible for bailing them out? Do you have any responsibility for that?

Mr. Mark Carney: The short answer is that I see no connection. But the basic point, which bears repeating, is that in that type of situation, which is extremely unlikely, so we're talking purely hypothetically, the Bank of Canada plays a role as lender of last resort upon the advice of OSFI that the institution is solvent but illiquid.

The Chair: Thank you very much.

Now we're going to go to Mr. Wallace, and we'll give you the remainder of time.

Mr. Mike Wallace (Burlington, CPC): Thank you. I actually don't have a lot of questions, but I have one in particular that I don't think has been touched on today.

First of all, congratulations on your appointment, and I look forward to working with you in the future.

If I'm reading it right, you had a fair amount of work overseas in terms of some experiences around the world with financial markets and finances. I don't know if you're in a position to tell us, but I wouldn't mind your opinion if you can give it to us. We have a fragmented financial market system here in this country. Would you say that you heard anything about that in your work overseas? Did it cause any difficulties or anything that you could share with us? That would be my first part of the question.

Second, do you see anything that could enhance our competitiveness as a financial market compared to what you've seen around the world?

Mr. Mark Carney: In terms of the first part of the question, when I was overseas with an investment banking firm, my work was principally with sovereign governments, particularly emerging markets as they really emerged. For example, there was South Africa, when the ANC came to power and they were doing their first financings, Korea, and other nations like that. I didn't really touch on Canada until I came back to Canada. So the short answer is no, I did not hear about that issue.

The broader issue, though—which is an important one and one close to the heart of the Bank of Canada—is how we enhance the competitiveness and efficiency of our capital markets.

There are things we can definitely do, and I'll start with what the bank can do. It starts with making sure we have an efficient fixed-income market, starting in money markets.

We talked a bit about the potential facility and what that role would be, but we must make sure we conduct our core oversight responsibilities for the payment system. That's important for the money market. We act as agent for the government in federal government debt. The consolidation of government debt, of some of the crowns into government debt, has been a success. We need to get the right level of liquidity there.

I think we need—and this is beyond our responsibility because the market has to do this—securitization to continue in this market. Securitization is under real pressure, and rightly so, because some products have become too complex, but it should shrink down to a core of more standardized products, which can really enhance the efficiency of markets.

We have to strengthen market integrity. Governance is an aspect, but better enforcement is absolutely crucial. I'd recommend the report of Nick Le Pan on IMETs and the role of the RCMP. But an important aspect here is that this is a shared responsibility. So it's not just the RCMP; it's provincial, it's crown prosecutors, it's provincial securities commissions. We'll do what we can to help.

I'd like to make my last three points.

One is about value, openness, and competition. The foreign property rule was removed in 2005. That opened up a lot of exciting markets for our investors abroad. That's important for our retirements. But it also created markets, such as the Maple bond market in Canada. This idea of having the Toronto Stock Exchange push free trade and securities is again the type of thing that can improve competition in Canada. We'll get better results if we have more competition. That's the basic point.

On regulation, my personal view is that I see a value to proportionate regulation, respecting different sizes of companies, different requirements for different sizes of companies, principle-based regulation. And I'll say one lesson to take from what happened in the summer is that people will come up with fancy new financial products. They will be very complex. The next turmoil—to use the official term for what happened—won't look like the last one. There will be different products. If you have principles, you can guide the conduct of those products, but if you have rules, people will get around them. And that's the experience of the market.

Last is investor education, but it's five o'clock and I won't be able to get into that.

● (1700)

The Chair: I want to say, on behalf of the committee, thank you very much for coming and informing us and, by extension, informing Canadians. We wish you very much wisdom as you take on your job as governor, and congratulations on your win. Thank you for being here, and thank you to the committee.

The meeting is adjourned.

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