BANK OF CANADA
BANQUE DU CANADA

FOR IMMEDIATE RELEASE
12 December 2011

CONTACT: Jeremy Harrison
613 782-8782

Prolonged Period of Deleveraging Ahead, Says Bank of Canada Governor Mark Carney

Toronto, Ontario–The world's advanced economies are entering a prolonged period of deleveraging after several decades of accumulating debt, Bank of Canada Governor Mark Carney said today. "The direction may be clear, but the magnitude and abruptness of the process are not. It could be long and orderly or it could be sharp and chaotic."

"In general, the more that households and governments drive leverage, the less the productive capacity of the economy expands, and the less sustainable the overall debt burden ultimately is," the Governor told a joint audience of the Empire Club of Canada and Canadian Club of Toronto.

Excessive private debts usually end up in the public sector, he noted. "This means that the public debt of most advanced economies can be expected to rise above the 90 per cent threshold historically associated with slower economic growth," the Governor said.

Excesses of leverage are dangerous, in part because debt is a particularly inflexible form of financing. "Hard experience has made it clear that financial markets are inherently subject to cycles of boom and bust and cannot always be relied upon to get debt levels right. This is part of the rationale for micro- and macroprudential regulation," he said.

It is not just the stock of debt that matters, but who holds it. Heavy reliance on cross-border flows, particularly when they fund consumption, usually proves unsustainable.

To restore necessary competitiveness, debtor countries in Europe will have to adopt fiscal and structural reforms, which are the responsibility of citizens, firms and governments, Governor Carney noted. "Central banks can only bridge real adjustments; they can't make the adjustments themselves."

In Canada, non-financial debt, or debt held outside the financial sector, increased over the past twenty years less than any other G-7 country. Nonetheless, the economy's reliance on "debt-fuelled household expenditures" must be reduced, and Canadian companies must invest in improving their productivity and access fast-growing emerging markets. "This would be good for Canadian companies and good for Canada," he said. "Indeed, it is the only sustainable option available."

"Canada's relative virtue throughout the debt super cycle affords us a privileged position now that the cycle has turned," the Governor said. "Our strong position gives us a window of opportunity to make the adjustments needed to continue to prosper in a deleveraging world. But opportunities are only valuable if seized."

The Bank of Canada is doing its part by fulfilling its mandate to keep inflation low, stable and predictable so that Canadian households and firms can invest and plan for the future with confidence. It is also assisting the federal government in ensuring that Canada's world-leading financial system will be there for Canadians in bad times as well as good and in pushing the G-20 Action Plan because it is in Canada's interests.