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Addressing Financial Market Turbulence

TORONTO, ONTARIO – More than seven months after financial market turbulence began, policy-makers and market participants are entering a new phase, where shortcomings in the current system are better understood and improvements are beginning to be made, Bank of Canada Governor Mark Carney said today in a speech to the Toronto Board of Trade.

In his remarks, Governor Carney discussed three of the most significant factors behind the market turbulence: liquidity; a lack of transparency and inadequate disclosure; and a series of misaligned incentives that encouraged excessive risk taking. Recent events have revealed serious and widespread shortcomings that need to be addressed promptly, completely and credibly, the Governor said.

Governor Carney outlined some of the responses to these factors. First, officials in many countries have been working to strengthen and modernize their liquidity arrangements where necessary. As announced earlier this week, the Bank of Canada engaged in the coordinated provision of liquidity with other major central banks. As well, the Bank plans to expand the list of collateral that it will accept in open market buyback operations, and it welcomes the Federal government's proposals to amend the Bank of Canada Act to modernize the Bank's authorities to support the stability of the financial system.

The Governor noted that authorities around the world are encouraging financial institutions to promptly and fully disclose valuations of structured products. In this regard, he highlighted some issues pertaining to interpretations of fair value accounting. There are indications that market participants are learning the appropriate lessons, realigning incentives, and changing their behaviour, the Governor said.

The turbulence has highlighted the importance of sound monetary policy, Governor Carney concluded. "At a time of great uncertainty, it is more important than ever that monetary policy act as a stabilizing force," said the Governor.

"This underscores the importance of keeping inflation low, stable, and predictable. This means that the Bank will continue to watch developments in the <u>real</u> economy for their impact on inflation."