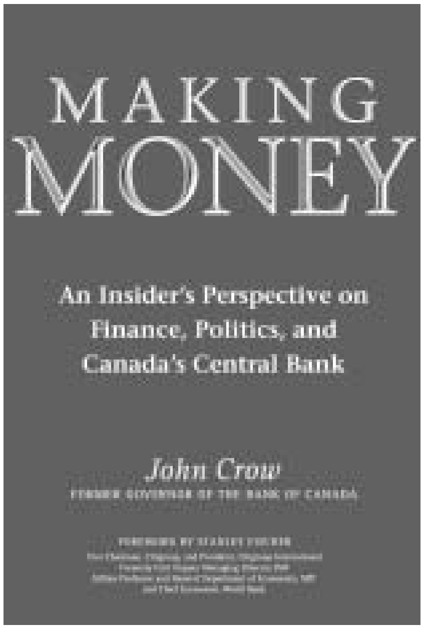
When Crow Ran the Loonie

John Crow, *Making Money: An Insider's Perspective on Finance Politics, and Canada's Central Bank.*
John Wiley & Sons Canada Ltd., 2002.



Review by Patrick Grady

"Since I have become a central banker, I have learned to mumble with great incoherence. If I seem unduly clear to you, you must have misunderstood what I said." Alan Greenspan, Chairman of the US Federal Reserve Board, as quoted in the *Wall Street Journal*.

During his seven-year term as governor of the Bank of Bank of Canada, John Crow always spoke clearly for a central banker, even if his speeches bore the marks of drafting by committee. In *Making Money*, Crow shows that, when freed from the shackles of centralbankese, he can write with a plain style that is a real pleasure to read, provided of course that you are not on the receiving end of his biting wit.

This book provides the most frank inside account of the workings of a central bank since the 1954 publication of Emile Moreau's *Souvenirs d'un Gouverneur de la Banque de France*, which recounts the history of the stabilization of the franc following its World War I inflationary decline. Crow's book is destined for similar status as a cult classic among central bankers, but it also deserves a wider readership among those interested in monetary policy.

Making Money is not a memoir in the traditional mode. In his book talks, Crow is quite contemptuous of what he calls the "Country Living" approach to central banking such as was epitomized in the January 2003 *Report on Business Magazine* profile of current Bank of Canada Governor David Dodge. In contrast, Crow takes pride that his book provides a serious treatment of the Bank of Canada and monetary policy and does not gloss over the hard, controversial technical issues at the heart of monetary policy.

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The main theme of *Making Money* is how the Bank fits in to the monetary policy decision-making framework. Unlike past governors who vanished into closed-lip retirement at the end of their terms, Crow does not hesitate to criticize the Bank of Canada and the government's current approach to monetary policy when they fail to meet his high expectations.

Crow's distaste for colourful personal exposés notwithstanding, a few words on how he came to be governor of the Bank of Canada help to understand the man. Born into a working class family in the Cockney east end of London, he won scholarships first to Parmiter's, a good solid grammar school, and the Balliol College Oxford, Adam Smith's alma mater, where he studied philosophy, politics and economics. Crow's first job was in the Western Hemisphere Department of the International Monetary Fund in Washington, D.C. Working on Latin America, he learned first hand about the links between government profligacy and inflation and the damage that it can wreak on an economy. Transferring to the North American Division and subsequently becoming its chief, he visited Canada regularly as part of the team assessing Canada's economic prospects and policies. Senior staff at the Bank of Canada were so impressed with Crow that in 1972 they offered him a job as deputy chief of the Research Department. Rising quickly through the ranks, he took office on the next-to-top floor of the Bank's art deco temple enshrined between two glass towers on Wellington Street as the Bank of Canada's fifth governor on February 1, 1987.

The monetary policy episode starring in the book is the setting of the inflation targets that were announced by Conservative finance minister Michael Wilson in his February 1991 budget. Inflation targets were an idea first raised in its *1990 Annual Review* by the former Economic Council of Canada, an organization which Crow held in low esteem and for whose demise he shed few tears. While Crow is reticent about telling tales out of school, he stresses "that the initiative for introducing targets came not from the Bank but from the Department of Finance."

In his view, its motivation mainly was to contain the consumer price inflation resulting from the introduction of the GST. A big concern at the time, which he shared, was the call by union leaders for 7-percent wage increases to compensate for the GST even though the direct price impact of the GST was only expected to be 1.5 per cent.

The Bank of Canada under John Crow's tutelage was successful in bringing inflation down to below 2 per cent in 1992 and 1993, perhaps too successful as inflation continued to fall averaging around zero in 1994.

Bringing inflation so quickly and effectively to heel was a thankless job that was not made any easier by the Conservative government's unwillingness to rein in its ballooning deficit, and by the inflationary impact of the GST on wage demands, not to mention the Meech Lake and Charlottetown constitutional debacles, which played havoc with the Canadian dollar. During this very difficult period, John Crow's unpopularity increased with the unemployment rate, particularly among the Liberal Opposition with whom he sparred before Parliamentary committees and in other public fora.

Given John Crow's unpopularity among Liberals, was he ever a serious candidate for reappointment? What would the Liberal government have done if deputy governor Gordon Thiessen had been unwilling to take the job with the new targets? Remember, with a $42 billion dollar deficit and nervous financial markets waiting to dump Canadian bonds and dollars, the new government was a bit over the barrel and needed a governor in whom markets had confidence.

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Crow also worries that the Bank of Canada has lost an important element of its independence now that its objectives are set by the government, leaving it only with a much less important "instrument independence" to set monetary policy to meet inflation targets.

Crow noted that, in an article in early 2001 on the appointment of David Dodge as the new governor, *The Economist* magazine referred to the inflation targets "set by Mr. Dodge's predecessors." In Crow's view, it would have been more accurate to say they were "set by Mr. Martin and his predecessors." Except for being less transparent, the situation in Canada is now like in the United Kingdom where the "Chancellor of the Exchequer hands down the targets."

While Crow recognizes that with the dramatic turnaround from "ballooning deficits to debt reduction" in the mid-1990s there was a "place for a monetary policy that was easy to the point of pushing the currency down," he argues that it is "a bad idea to have a policy promoting currency decline." His record speaks for itself. When he took over as governor in February 1987, the Canadian dollar was worth 74.6 cents US and when he completed his term, it was worth 75.9 cents. Since he left office, the Canadian dollar has fallen to below 66 cents.

The Liberal government comes in for some of Crow's sharpest verbal barbs. He asks if its statement about monetary policy in the Red Book, which counts on economic growth and fiscal responsibility to "make possible a monetary policy that produces lower real interest rates and keeps inflation low, so that we can be competitive with our main trading partners," was "a joke." After tearing its meaning apart word for word, he concludes that he is "probably in danger of having too much fun getting his gums into material that is newspaper thin." He sarcastically contrasts the ambiguity of the monetary policy statement with the clarity of the Red Book's promises to "replace the GST," "renegotiate the FTA," and establish an "independent ethics counselor." No one can say Crow doesn't have an instinct for the jugular.

John Crow left his successors at the Bank of Canada an important asset, a high degree of credibility for its monetary policy. This has allowed Canadian interest rates to decline to US levels or even below and been an important factor behind the good economic performance of the last decade. With consumer price inflation already at 4 percent and still on the rise, *Making Money* provides good advice on how not to blow it.

Patrick Grady was formerly a senior official in the Bank of Canada and the Department of Finance and now is an economist with Global Economics Ltd., an Ottawa-based economic consulting firm (www.global-economics.ca).