Interest rates could raise despite lower U.S. rates



Diane -Maley Your Business homson News Service

Falling interest rates south of the border and signs of economic slowdown have led forecasters to predict with confidence that Canadian rates will fall substantially over the next few months. Many think a decline is long overdue.

Wood Gundy, for example, expects the prime business lending rate to fall from 13.5 per cent to 11.75 per cent by December and 11 per cent by next June. The prime is the bank's benchmark business lending rate.

But conventional wisdom is seldom right. At least one economist thinks the prime could actually rise a full percentage point before long. David Marshall of MMS International bases his belief on the strong demand for credit in Canada. The possibility that he could be right is forcing borrowers and lenders to rethink their strategies.

The case for higher interest rates is supported by a recent Fortune magazine forecast. Fortune's economists say the U.S. Federal Reserve Board will soon begin to

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tighten the money supply again as inflation proves more tenacious than policy makers had thought. A smaller supply of money will raise its price, or interest.

The Federal Reserve is the American counterpart of the Bank of Canada.

PRESSURE IS OFF

If U.S. rates begin to climb again, the pressure will be off John Crow, governor of the Bank of Canada, to lower rates in Canada. Mr. Crow will be able to point to the American experience to defend his high-rate policy.

Rather than raising rates substantially, Mr. Crow is likely to keep them steady to slightly higher. The reason is simply that the Canadian economy cannot withstand much higher borrowing costs.

Overshadowing the interest rate outlook is the mountain of debt that overhangs North American government, business and consumers. In Canada, household debt stands at a record 54 per cent of household income, not a healthy situation.

The question Mr. Crow is pondering in his struggle with inflation is, how much can he squeeze us without tipping the economy into recession?

Another reason Canadian rates could stay high is the vulnerability of the Canadian dollar on foreign exchange markets. True, the dollar is stronger than it has been in nearly a decade. That just akes it all the more vulnerable.

TRADE WORSENS

Undermining the dollar's strength is our worsening trade position. Net exports are shrinking. A shrinking trade surplus adds to the traditional current account deficit, spelling trouble for the dollar.

The current account includes goods and services - such things as dividend and interest payments to foreigners.

Given that most people expect rates to fall, what is likely to happen if they stay relatively high or rise even further?

So far, most of the pressure has been on short-term rates. This is likely to continue. Longer-term rates will seem low by comparison. If rates hold fairly steady, spending will continue to slow.

But if interest rates rise another point or so, we could be in for a much more severe recession than the soft-landing we are now enjoying. It could hit late next year or early in 1991. If it does, interest rates will drop dramatically.

Chambers says "play ball"

More than 2,000 members of 18 Chambers of Commerce from around the Golden Horseshoe will converge on the SkyDome Friday, Sept. 15 for the game between the Toronto Blue Jays and the Cleveland Indians.

"This is a first," said Halton Hills Chamber of Commerce President Dave Page. "Although we have traditionally co-operated with other chambers in the past to develop programs, policies and events which we believed would be beneficial to our Halton Hills business community, this is the first time for a social event such as this."

In addition to the Halton Hills Chamber of Commerce, the following chambers will be sending

representation: Burlington, Brantford, Brampton, Cambridge, Coburg, Belleville, Elmira, Hamilton, Peterborough, Flamborough, Milton, Niagara Falls, Oakville, Oshawa, Welland, Stoney Creek and Whitby.

"Every year many of us are able to get together at the Annual Meetings of the Ontario and Canadian Chambers of Commerce for an exchange of views and ideas," said Dave Page, "and our staff are able to do this same through their own professional management associations, but this is different."

For further information contact Doug Penrice of the Halton Hills Chamber of Commerce at 877-7119.

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