# Pierre Duguay: The Bank of Canada's perspective on the penny

Remarks by Mr Pierre Duguay, Deputy Governor of the Bank of Canada, to the Senate Committee on National Finance, Ottawa, Ontario, 26 May 2010.

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Good evening Mr. Chairman, honourable Senators.

I'm pleased to have the opportunity to appear before you tonight to provide the Bank of Canada's perspective on the penny. First, let me take a moment to explain the Bank's role regarding Canada's currency. We are responsible for supplying Canadians with bank notes that they can use with confidence. At year-end 2009, there were 1.8 billion bank notes in circulation, with a total value of $55.5 billion – approximately $1,630 per Canadian. The Bank of Canada is not responsible for coins. Decisions on coinage rest with the federal government, in particular, the Department of Finance, and with the Royal Canadian Mint. However, coins are an essential adjunct of bank notes to complete cash transactions. So, the Bank does have an interest in coins, and we welcome your review of the case for keeping or eliminating the penny.

I would like to remind you that cash remains very important to Canadians, despite the popularity of alternative payment options. Surveys by the Bank of Canada have found that almost three-quarters of Canadians pay with cash at least once a week, compared with 64 per cent for debit cards and 36 per cent for credit cards.[1] These surveys show that cash is the preferred method of payment for purchases under $25. (Debit cards are preferred for purchases in the $25 to $100 range, and credit cards are preferred for purchases greater than $100.)

The Bank's interest in coins can also be viewed in the context of our responsibility for monetary policy, which is anchored in our commitment to achieve our 2 per cent target for inflation. Experience has shown that the best way for monetary policy to contribute to economic performance is by keeping inflation low, stable, and predictable. Therefore, the Bank views the possible elimination of the penny in terms of the potential impact on inflation, and has conducted some preliminary research on this issue. The findings, which have been made available to other researchers, show that any impact on inflation would be insignificant and more likely non-existent.

A common concern is that retailers, who often post prices ending in 9 cents, may round prices up to an even number, absent the penny, and that this would be inflationary. This concern is unwarranted for a number of reasons. First, even if the elimination of the penny did result in a rounding up of prices to the nearest multiple of 5 cents, which is unlikely, that would be a one-time price increase and not a change in trend inflation.

Second, this one-time price increase of one or two cents would be so small, relative to the prices of the items that make up the basket of goods and services priced by the total consumer price index (CPI) that it would not register on that index since the CPI is rounded to the nearest 0.1 per cent.

Third, it is very unlikely that prices would be rounded up, since such rounding would not carry through to the cash register after sales taxes are applied, and retailers would lose the perceived marketing benefit of posting a price that ends in 9 cents. In the absence of a penny, rounding would only need come into play in cash transactions and would apply to the total bill after tax, and not to each individual item purchased. If applied symmetrically,

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[1] Varya Taylor. "Trends in Retail Payments and Insights from Public Survey Results." *Bank of Canada Review*. (Spring 2006): 25-36.

rounding down of cash purchases ending in 1,2, 6, and 7 cents would offset the rounding up of those ending in 3,4 8, and 9 cents.

In New Zealand, for example, the choice of rounding up or down on cash transactions was left to retailers after the country eliminated its one- and two-cent coins in 1989. Many larger retailers opted to round down; a few small retailers opted to round up. Ultimately, there was no noticeable effect on inflation in New Zealand.

Indeed, that has been the international experience that we have seen. In both Australia and New Zealand, the elimination of small coins (one-cent and two-cent coins) has had no noticeable effect on inflation.

Inflation, however, does have an influence on the value of the penny. Since the coin was first produced by the Royal Canadian Mint in 1908, the penny has lost 95 per cent of its purchasing power. In other words, the penny then had the same purchasing power as 20 cents would today. Indeed, in 1908, you could buy your daily newspaper for two cents, and a loaf of bread cost five cents.

On that, I thank you for your invitation to appear here tonight, and welcome the opportunity to answer your questions related to the future of the penny.