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Recent Economic Developments in Canada,
September-November 1963 18 pages

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Summary

The shock to business confidence associated with the Gordon budget message in June and the U.S. interest-equalization tax proposal in July coincided with a pause in Canadian economic expansion in mid-summer, when industrial activity declined rather sharply and unemployment rose contra-seasonally.1/ Forward momentum was soon regained, however, on the basis of a generally favorable export performance reinforced in September by unexpectedly huge wheat contracts with Soviet-bloc countries. Since then, the Canadian dollar has been strong, notwithstanding a virtual cessation of new flotations of bonds in the U.S., and financial and money markets have, for the most part, demonstrated a remarkable degree of stability.

At this moment, the main areas of concern tend to be political rather than economic. Within Canada, there is a continuing contest for fiscal control, spear-headed by Quebec. A special Dominion-Provincial Conference was convened on November 26 to consider further provincial demands upon the Federal authorities. Internationally, the extended program for encouraging exports of autos and auto parts announced by the Honorable C. M. Drury on October 25 has been adversely received in the United States. Indeed, the Canadian authorities have introduced what is in effect an export subsidy that, while not a technical violation of the GATT, is clearly in violation of the GATT spirit. As a result, Canada seems once again to be attempting to enjoy the best of all possible worlds, as it did when it operated a floating exchange rate in a world of fixed rates and, more recently, when Canadian officials sought exemption

1/ Developments in the Canadian economy earlier in 1963 are reviewed in "Recent Economic Developments in Canada: June-August 1963," September 9, 1963.

from the proposed U.S. interest-equalization tax at the same time that Parliament was considering the implementation of fiscal measures that discriminate against U.S. direct investment in Canadian enterprise.

Domestic activity and employment upward

General measures of economic activity showed continued or renewed vigor following the abrupt set-back registered in July. During that month, the index of industrial production had lost all of the ground gained since February; unemployment continued at the relatively high figure of 6.0 per cent of the labor force (seasonally adjusted); and the monthly value of new automobile sales had declined almost 12 per cent, also on a seasonally adjusted basis.

Even before the generally stimulating effects of the Soviet wheat contract could make themselves felt, forward momentum had been regained. The unemployment rate declined to 5.6 per cent in August (see Table 1) and fell further to 5.3 per cent in September, the lowest level attained in the course of the economic upswing that began in early 1961. The October rate was unchanged from September. Total retail sales, which had also receded somewhat in July, advanced to successive record levels in August and September. Production of steel ingots in July-September registered its second successive quarterly record. The seasonally adjusted index of industrial production (1949=100) advanced by 1.4 per cent in September to a new high of 197.9. Manufacturing was up 1.1 per cent, mining 2.7 per cent, and electric power and gas utilities 1.9 per cent. Within manufacturing non-durables were unchanged but durables rose almost 2.5 per cent.

Data for domestic activity beyond September are more fragmentary. Production of steel ingot, however, has shown a vigorous expansion above year-ago levels throughout October and November while department store sales are also up, though less markedly. Housing starts in urban centers through October registered a cumulative

Table 1. Canad Selected Indicators of Domest Economic Activity
August-November 1963 (with compari ns)

Month or Week	RETAIL SALES (sea. adj.) Total	M.V.	Dept. Stores	DEPT. STORE SALES: chgs. from prev. yr. %	INDUSTRIAL PRODUCTION (sea. adj.) Total	Mining	Manuf.	Electric Power and Gas Utils.	STEEL INGOT PRODUCTION Total '000 t	Chg. from prev. yr. '000 t	UNEMPLOYMENT (sea.adj.) % lab. force	HOUSING STARTS in urban centers (seas. adj. ann. rate) Month thousand	Year to Date
	million dollars												
1962 Aug.	1445	211	131		188.7	299.9	165.8	350.4			5.9	101.4	
Sept.	1466	213	135		188.8	290.6	167.6	339.4			5.7	104.1	75.7
Oct.	1474	232	129		189.1	296.2	167.3	340.7			5.8	107.0	86.6
Nov.	1496	242	133		189.6	291.9	168.3	341.9			5.9		
1963 July	1508	230	138		192.8	286.0	170.8	373.9			6.0		
week 1													
week 2													
week 3													
week 4													
week 5													
Aug.	1530	226	143		195.1	293.8	173.1	366.2			5.6	113.4	
week 1													
week 2													
week 3													
week 4													
week 5				+13.6					156.4				
Sept.	1556	249	140		197.9	301.8	175.0	373.1			5.3	116.0	81.7
week 1				+ 8.1					138.7	+ 6.9			
week 2				+ 1.3					164.1	+21.0			
week 3				+ 6.0					159.8	+19.7			
week 4				+ 0.8					153.5	+15.6			
week 5													
Oct.											5.3	111.7	92.8
week 1				+13.4					153.4	+31.3			
week 2				+19.8					154.8	+26.5			
week 3				-12.9					156.7	+18.5			
week 4				+ 3.6					157.2	+19.0			
week 5													
Nov.													
week 1				+ 6.8					163.1	+30.8			
week 2				+ 7.8					161.7	+19.4			
week 3				+ 4.4					160.2	+21.7			
week 4				+ 7.4					168.6	+53.1			

gain of almost 9.5 per cent, although the year-over-year gains have declined somewhat in recent months.

Prices and wages rising slowly; profits, more rapidly

Despite buoyant demand, domestic price movements were of modest proportions. The consumer price index rose marginally in September and October but remained below its August peak. The general index of wholesale prices, which climbed 0.5 per cent in October 1963 after a lesser rise in September, also held below its previous peak but, reflecting in part the impact of devaluation, it stood 6.1 per cent above its year-ago level. Similarly, the industrial composite figure on average weekly wages and salaries declined somewhat in July but rose 1 per cent in September after holding steady in August, to a level 3 per cent above its year-ago rate.

Business profits have been tending to rise. Of 21 major industrial companies that had reported earnings for the first three quarters by early November, 15 had shown increases and only 6 decreases as compared with the same period in 1962. With new orders and unfilled orders both running considerably higher than in 1962, a number of companies expect earnings to reach record levels for this calendar year. Dividend payments by Canadian companies were up 10 per cent in the first nine months, to a record $703 million, mainly because of increases by a half-dozen large companies including International Petroleum Company Ltd., and International Nickel Company of Canada Ltd.

Foreign trade position strongly improved

The most spectacular element in Canada's current economic performance is the foreign-trade sector. Sparked by increased export volume at substantially unchanged prices, Canadian exports in July-September exceeded the quarterly figure of $1.7 billion for the first time on record. They established their second consecutive quarterly record, and were 10 per cent higher than in the corresponding period of

1962. The month of September was particularly strong, registering a year-over-year advance of 22 per cent. With exports through September in excess of $5 billion, up 8 per cent, and imports only 1.5 per cent higher than in 1962, the cumulative trade deficit of $75 million registered a year ago had been converted into a trade surplus of $233 million.

Cumulative exports to the U.S. thus far this year have risen only modestly, but shipments to most other destinations were sharply higher. Among individual commodities, gains of 8 per cent or more were recorded for lumber, wheat, iron ore, aluminum, newsprint, and woodpulp. Shipments of iron and steel products reached a cumulative total of $71.8 million, up 23 per cent over 1962.

Large wheat contracts (see Table 2), especially with the Sino-Soviet bloc, will provide an underlying source of further strength for some months to come. From Canada's point of view, with a record wheat crop and carry-over in prospect, the U.S.S.R. contract represented an outstanding achievement. The quantity involved was equivalent to two-thirds of Canadian wheat and flour shipments to all destinations during the preceding crop year. With these sales, prospective exports in 1963-64 were raised to 550 million bushels as compared to the previous high of 408 million recorded as long ago as 1928-29. Because the contract was closed on a bilateral basis and at the relatively low prevailing price, however, Canada is open to criticism on three major grounds: (a) full commercial advantage was not taken of its bargaining position; (b) the late President Kennedy was pushed into the awkward position of officially concurring in a U.S. export contract with the U.S.S.R. which has yet to be consummated; and (c) the West did not utilize this opportunity for wringing significant political concessions from the Soviet bloc. The Western nations have of course gained in financial terms from the heavy gold sales made since early September by the U.S.S.R., which appears not to have been availing itself of its assured credit facilities.

Table 2. Canada: Major Sales Contracts for Wheat, August-November 1963

Approx. date of contract		Country	Quantity	Period of Shipment	Down Payment	Loan Terms	Price per bushels	Approx. Value (Mill.Cdn.$)
August	1	China (Mainland)	112-186.7 mill. bus.	3-years	25%	6,12, & 18 months		200-350
September	10	U.S.S.R.	11.2 mill. bus.					22
	16	U.S.S.R. 1/	198 mill. bus. wheat 29.5 mill. bus. flour	by 7-31-64	25%	6,12, & 18 months	$1.96-5/8	500
	--		18.7 mill. bus. wheat	3-years				
October	8	Bulgaria	min. 300,000 metric ton	3-years	33%			33
			+150,000 metric ton	by 7-31-64				
	8	Japan	800,000 tons	100,000/mo. Jan.-Aug. '64			$1.96-5/8	52
	29	Czechoslovakia	44.4 mill. bus.	5-years	10%	24,30, & 36 months	$2.00-3/4 first 120,000 t.	89
November	5	Poland	44 mill. bus.	3-years; min. 7.4 m. by 7-31-64	10%	24,30, & 36 months		80-90

1/ U.S.S.R. also contracted to purchase 58.5 million bushels from Australia on September 19, for cash at time of shipment; and, on September 26, 250,000 tons of flour from West German millers, part of it processed from imported U.S. wheat. (1 bushel of wheat = 60 lbs.; 1 short ton = c. 33.3 bushels.)

Financial and money markets stabilize after August

The period of sharp run-up in yields on Government securities that commenced around mid-June had largely run its course by late August. (See Table 3.) After registering a modest further rise in early September, bond yields eased generally, except for the Government of Canada issue due in September 1965, which abruptly fell 43 points over a two-week interval. Throughout October and November, this market was characterized by an exceptionally high degree of stability at both the long and the short ends of the yield curve. The yield on Treasury bills, however, dipped slightly in mid-October, while that on the longest-term issue was temporarily rising. The September 1965 issue continued to perform in a somewhat volatile fashion, but at end-November was at almost the same level as in October. By comparison with security yields in late April, yields in late November were lower for Treasury bills and short-term bonds; but yields on the medium-term issue due in 1975-78 had risen 17 percentage points and those on long-term offerings were fractionally higher.

The peaks in corporate and local-government yields were also reached in late August. Between end-May and end-August, the 40 bond index had climbed 34 percentage points. The rise was particularly large in municipals and only modest in industrials. During September, the index fell back somewhat, with municipals again registering the major swing, but it changed little in the course of the succeeding two months; with increases in the yields on municipal bonds largely offset by a decline in those of public utilities. The 15 point increase in the index from April to November was due mostly to higher yields on provincial and municipal securities.

Canadian stock prices, which had advanced to an all-time high in early May, fell sharply backward as the aftermath, first, of the Gordon Budget Message in June, and then of measures introduced (or proposed) by the U.S. in July to strengthen its own balance-of-payments position. (See Table 3.) The stock market remained in the doldrums throughout the month of August, but strengthened somewhat following the announcement of the Canadian-USSR wheat contract. Even at its recent peak, however, the DBS index of industrial-stock prices remained 1.5 per cent below its all-time high,

Table 3. Canada: Security Yields and Stock Prices, Selected Dates, April-November 1963
(per cent per annum)

Week of 1/		Treasury Bills 2/ 3mos.	Treasury Bills 2/ 6 mos.	Govt. of Canada Bonds Sept. 1965	Govt. of Canada Bonds Jan. 1975-78	Govt. of Canada Bonds Sept. 1996-Mar.'98	Other Canadian Bonds 3/ Prov'l	Other Canadian Bonds 3/ Municp.	Other Canadian Bonds 3/ Pub. Utils.	Other Canadian Bonds 3/ Indust.	Other Canadian Bonds 3/ 40-Bond Avg.	Stock Market Canada DBS Indust's	Stock Market U.S. S & P Indust's
April	24	3.66	3.80	4.51	5.00	4.97						137.1	73.09
	30						5.32	5.47	5.39	5.33	5.38		
May	8	3.33	3.40	4.26	4.92	4.94						140.6	73.49
	31						5.29	5.39	5.34	5.26	5.32		
June	12	3.19	3.30	4.07	4.88	4.90						140.1	73.71
	26	3.22	3.32	4.09	4.89	4.90						133.8	73.04
	30						5.29	5.41	5.42	5.26	5.34		
July	3	3.26	3.36	4.08	4.91	4.88						135.3	73.04
	31						5.44	5.59	5.50	5.43	5.49		
Aug.	28	3.71	3.95	4.64	5.26	5.06						131.8	75.56
	31						5.67	5.88	5.61	5.49	5.66		
Sept.	4	3.75	3.98	4.56	5.26	5.06						133.0	76.43
	11	3.78	3.98	4.60	5.27	5.14						135.9	76.77
	18	3.68	3.87	4.51	5.24	5.11						137.3	76.93
	25	3.56	3.71	4.17	5.08	5.08						137.7	76.57
	30						5.50	5.67	5.56	5.44	5.54		
Oct.	2	3.61	3.76	4.09	5.02	5.02						137.4	76.25
	9	3.56	3.69	3.97	5.03	5.04						137.3	76.31
	16	3.54	3.69	4.00	5.03	5.04						138.5	76.88
	23	3.56	3.73	4.13	5.07	5.05						137.7	77.46
	30	3.59	3.77	4.11	5.08	5.01						136.9	78.45
	31						5.51	5.66	5.48	5.40	5.51		
Nov.	6	3.63	3.79	4.08	5.08	5.01						137.3	77.35
	13	3.66	3.81	4.35	5.17	5.04						137.3	77.17
	20	3.63	3.78	4.20	5.14	5.04						135.7	75.37
	27	3.63	3.76	4.10	5.17	5.02						135.7	76.73
	29						5.53	5.72	5.48	5.41	5.53		
Net change: April-November		-.03	-.04	-.41	+.17	+.05	+.21	+.25	+.09	+.08	+.15	- 1.4	+3.64

1/ Or month ending.
2/ Average tender, Thursday dates.
3/ Source: McLeod, Young, Weir & Company.

Table 1. Government of Canada Security Holdings, August-November 1963
(million of dollars, par value)

	August 31	September 30	October 30	November 27	Change: August-November
Bank of Canada:					
Treasury Bills	388	341	381	353	- 35
Other	2655	2655	2702	2683	+ 28
Total	(3044)	(2997)	(3083)	(3036)	(- 8)
Chartered Banks					
Treasury Bills	1193	1242	1301	1302	+109
Other	2527	2517	2559	2615	+ 88
Total	(3720)	(3759)	(3860)	(3917)	(+187)
Government Accounts					
Treasury Bills	111	34	30	63	- 48
Other	416	433	448	461	+ 45
Total	(527)	(467)	(478)	(524)	(- 3)
eral Public					
Treasury Bills	548	628	553	537	- 11
Canada Savings Bonds	4410	4385	4380	5167	+757
Other	7140	7150	7181	7139	- 1
Total	(12098)	(12163)	(12114)	(12843)	(+745)
Treasury Bills: Total	2240	2245	2265	2255	+ 15
Canada Savings Bonds: Total	4410	4385	4380	5167	+757
All other Direct & Guaranteed: Total	12738	12755	12890	12898	+160
Total Outstanding	19,388	19,385	19,535	20,320	+932

rce: Bank of Canada, Statistical Summary and Weekly Financial Statistics.

whereas the Standard and Poor's index for corresponding U.S. securities pushed ahead to its record high in late October. Both indexes declined abruptly immediately following the news of President Kennedy's assassination, but both had staged recoveries by the end of November.

Between the end of August and late November, the total volume of Treasury Bills outstanding increased $15 million. (See Table 4.) A supplementary factor contributing towards some upward pressure on short-term rates was a decline of $83 million in the total held by the Bank of Canada and Government Accounts. At the same time, these two official holders were purchasing a combined total of $73 million in longer-term Government securities. Over the period, a major shift occurred in the volume of

Table 5. Canada: Currency and Chartered Bank Deposits
(millions of dollars)

	August 31	September 30	October 30	November 20	Change: August-November
Currency Outside Banks:					
Coin	186	189	190	190	+ 4
Notes	1804	1802	1812	1795	- 9
Total	(1990)	(1991)	(2002)	(1985)	(- 5)
Chartered Bank Deposits:					
Personal Savings	8437	8495	8634	8358	- 79
Other Public	5224	5337	5407	5438	+214
Total held by Public	(13661)	(13832)	(14041)	(13796)	(+135)
Total Currency and Deposits held by Public	15650	15824	16043	15782	+132
Government of Canada Deposits	415	260	379	948	+533
Total Currency and Chartered Bank Deposits	16065	16084	16422	16730	+665
Total Government of Canada Deposits 1/	508	307	407	1002	+494

1/ Canadian dollar balances at Bank of Canada and Chartered Banks.

Source: Bank of Canada Statistical Summary and Weekly Financial Statistics.

Canadian Savings Bonds held by the general public. By November 15, total sales of new C.S.B.'s had passed the $800 million mark and buyers numbered 1.12 million, more th[an] half of them undertaking to make their purchases through the Payroll Savings Plan.

There was a consequent increase in Canadian dollar deposits held with the chartered banks by the Government of Canada. (See Table 5.) Indeed the rise in these balances since the end of September amounted to $688 million, or slightly larger than the over-all increase in total currency in circulation and chartered bank deposits (which has been the subject of recent comment in the daily press). In this manner, the injection of liquidity resulting in considerable degree from the trade surplus has been neutralized, temporarily at least.

Canadian dollar strengthens; modest arbitrage flows

The Canadian dollar, which had declined abruptly after mid-July and had remained below par throughout the month of August, rose above $92.50 (U.S.) on September 11. Shortly thereafter, and reflecting the closer alignment of Canadian-U.S. short-term money rates, the discount on three-months forwards, which had reached a high of .7 per cent in mid-August, was completely eliminated. During October and November, the Canadian dollar held strong, fluctuating within the extremely narrow range of $92.70 and $92.86. For most of the month of October, a small premium prevailed on the three-months forwards, while the forward quotation was practically flat throughout November. (See Table 6).

With the rate on the U.S. 3-month Treasury bill rising rather steadily from early July through mid-November, and the Canadian bill rate declining somewhat from its peak levels of mid-September, the uncovered differential in favor of Canada fell from a high of .33 percentage points as of September 12 to trivial (and temporarily) negative figures in mid-October and again in early November. On a covered basis, the incentive in favor of Canada ranged narrowly between ± 10 percentage points after mid-October.

The covered differential on 3-month prime finance company paper, which is more relevant to the actual movement of short-term funds then is the prevailing differential on Treasury bills, remained sufficiently high throughout the period to promote modest flows of funds into Canada. In early September, the differential amounted to 1/2 per cent, and at no time did it fall below 1/8 per cent, despite the upward tendency in the rate on U.S. paper after early August. (See Table 6). An increase in the U.S. rate of 1/8 per cent in early October was followed, after a month's time lag, by a corresponding rise in the domestic Canadian rate, increasing the covered spread to 1/4 per cent per annum. Perhaps reflecting year-end pressures, rates on all maturities of Canadian finance and commercial paper were raised by 1/4 per cent on December 9.

Table 6. Canadian-U.S. Arbitrage Computations, July-November 1963
(per cent per annum)

Week of	3-Month Treasury Bills 1/: Cdn. Bills, N. Y.	U.S. Bills, N. Y.	Spread in favor Canada (uncov.)	Prem. (+) Disc. (-) on 3-mos. fwd. Cdn. dollar	Net Covered Diff'l in favor Canada	3-Mos. Prime Finance Co. Paper 2/: Canadian Paper In Cdn. dollars	Canadian Paper Fully Hedged	U.S. Paper	Net Covered Diff'l in favor Canada
July									
3	3.17	3.01	+0.16	+0.10	+.26	3.625	3.625	3.375	+0.250
11	3.28	3.21	.07	.20	+.27	3.625	3.625	3.375	+ .250
18	3.32	3.20	.12	.07	+.19	3.875	3.625	3.375	+ .250
25	3.37	3.19	.18	-.34	-.16	3.875	3.54	3.375	+ .165
Aug.									
1	3.28	3.25	.03	-.07	-.04	4.00	3.88	3.375	+ .505
8	3.35	3.26	.09	-.41	-.32	4.125	3.62	3.50	+ .120
15	3.52	3.29	.23	-.27	-.04	4.25	3.80	3.50	+ .300
22	3.52	3.35	.17	-.27	-.10	4.25	3.85	3.50	+ .135
29	3.58	3.38	.20	-.34	-.14	4.25	3.80	3.50	+ .300
Sept.									
5	3.62	3.34	.28	-.41	-.13	4.25	3.80	3.50	+ .300
12	3.67	3.34	.33	-.14	+.19	4.25	3.90	3.625	+ .275
19	3.66	3.39	.27	+.07	+.34	4.00	4.00	3.625	+ .375
26	3.52	3.34	.18	-.18	--	3.875	3.80	3.625	+ .175
Oct.									
3	3.48	3.41	.07	-.07	--	4.00	3.85	3.625	+ .225
10	3.50	3.42	.08	+.07	+.15	4.00	3.96	3.75	+ .210
17	3.44	3.47	-.03	+.07	+.04	4.00	3.94	3.75	+ .190
24	3.42	3.42	--	+.07	+.07	4.00	3.94	3.75	+ .190
31	3.47	3.45	+.02	--	+.02	4.00	3.875	3.75	+ .125
Nov.									
7	3.50	3.51	-.01	--	-.01	4.00	3.90	3.75	+ .150
14	3.58	3.52	+.06	--	+.06	4.13	4.00	3.75	+ .250
21	3.57	3.48	+.09	--	+.09	4.13	4.00	3.75	+ .250
28	3.54	3.49	+.05	+.04	+.09	4.13	4.00	3.75	+ .250

1/ 360-day year, discount basis. Source: Federal Reserve Bank of New York.
2/ Source: Morgan Guaranty Trust Company of New York.

New issues of Canadian bonds payable in U.S. currency contributed practically nothing to the Canadian foreign exchange position during the three months under review. Presumably on the basis of new issues actually placed prior to the announcement of the proposed interest-equalization tax, some $32 million of corporate bonds were reported by Ames & Co. between late July and early August, and a further $10 million (about half of these in the provincially-guaranteed category) by mid-September. Since then, no new issues have come to the attention of Ames & Co. to date. According to the daily press, the first sizeable sale of new Canadian bonds to a U.S. purchaser since mid-July occurred around the middle of November when Mutual Life Insurance Company of New York took up $6.5 (Cdn.) of a $15 million issue of Home Oil Company Limited 6-1/4 per cent collateral trust bonds due April 1, 1965.

Capital flows, therefore, were less important than favorable exports as the source of strength for the dollar in the period under review. Total Canadian reserves of gold and foreign exchange, which had declined from a high of $2,713 million at the end of May 1963 to $2,470.5 million by the end of August, rose by modest amounts in each of the following three months. By the end of November they had reached $2,631 million.

New Federal budget approved but major fiscal problems continue

Figures on Federal Budgetary revenues and expenditures, now available through October, show a cumulative deficit in the 1963-64 fiscal year (beginning April) of $128.6 million, as expenditures have been rising somewhat more rapidly than receipts. At a comparable date in the previous fiscal year, the deficit had reached a cumulative figure of only $87 million, although that fiscal year ended with a total deficit of $692 million.

Finance Minister Walter Gordon's revised Budget, as re-submitted on July 8, was finally given its third reading in the House of Commons on November 13. Its main tax provisions are as follows:

(a) the 11 per cent tax on machinery, equipment and building materials will be cut back to 4 per cent for the current fiscal year ending March 31, 1964; the tax on these goods will be increased to 8 per cent on April 1, 1964, and then to the full 11 per cent by December 31, 1964. Equipment and building materials purchased by schools and universities will continue to be exempt from the tax. The net effect of the changes is to reduce revenues in the 1963-64 fiscal year by about $115 million;

(b) the 15 per cent withholding tax levied on dividends paid to foreigners is reduced to 10 per cent in a comporation with 25 per cent or more Canadian ownership but increased to 20 per cent by January 1, 1965, where this condition is not met. 1/

In mid-October, the Senate gave final reading to the Government's bill to increase old-age pensions by $10 per month to $75, estimated to cost the Treasury $116 million per year.

1/ The status of the corporation will be determined by the ownership of its shares two months before the beginning of the tax year. Corporations with widely spread ownership, which would have great difficulty in determining the beneficial ownership of share holdings, will be able to qualify if their shares are listed on a Canadian stock exchange and not more than 75 per cent of the voting stock is owned by a non-resident shareholder and others associated with him. The requirement that 25 per cent of the directors be Canadian if the corporation is to qualify for the lower withholding tax will not apply until 1965.

Responding to criticism of the low level of Canada's foreign aid contribution, External Affairs Minister Paul Martin unveiled an expanded program in the Commons on November 14. The announced policy contains two significant new features: (1) A low-interest fund, to be initiated next year with a first commitment of $50 million, and (2) the promise of aid from this fund to Latin America. In effect, the plan also restores the 1962 austerity cut made in Colombo Plan aid, which was reduced from $50 millinn to $41.5 million. The program, designed to go into effect in the 1964-65 financial year, was estimated by Mr. Martin to raise Canada's foreign aid expenditures from the present figure of $120 million to $180-190 million. Both sets of figures include the Export Credit Financing Program, administered by the Department of Trade and Commerce for the purpose of assisting Canadian exporters.

Two other developments are of far greater long-run significance than these recent budgetary measures. First, the Minister of Industry on October 25 announced a three-year program, to take effect on November 1, 1963, to promote increased domestic production and export of motor vehicles and parts. Expanding on a program initiated by the Diefenbaker government a year earlier, the duty applicable to one dollar of dutiable imports is to be remitted for each dollar of exported Canadian content of vehicles or parts in excess of exports made during the 12 months ending October 31, 1962. Credits for remission of duties may be earned by vehicle manufacturers directly or through exports by parts makers.

This measure reflects the opinion of the Canadian government that the Canadian automobile industry, because it is dominated by subsidiaries of U.S. companies, has not been sufficiently aggressive in developing Canadian production that would otherwise be economically feasible and would extend the Canadian economic base in the field of secondary manufacturing. The adverse Canadian trade balance in autos and auto parts, mainly of U.S. origin, amounted to some $500 million in 1962, (a considerable portion of the overall trade deficit of $550 million with the U.S. and in sharp contrast to the small export surplus Canada enjoyed in transactions with all its trading partners).

An export target of $150-200 million is mentioned for the auto-export program, and there is already some discussion of extending similar arrangements to other commodities (such as consumer durables and business machines) in which Canadian production also is dominated by American subsidiaries heavily dependent upon import of component parts.

The heads of the leading Canadian automobile companies have announced that they will cooperate in the development of an independent auto-parts industry. The incidental displacement of American production is of considerable concern to U.S. officials. State Department legal authorities do not regard the plan as a breach of Canada's obligations under the G.A.T.T. The U.S. Treasury, however, must independently rule on the question of whether or not an export subsidy is involved. An adverse ruling would make the imposition of a countervailing duty mandatory.

Fiscal relationships are complicated at this time not only externally, as between Canada and the U.S., but also internally, as between the Federal Government and the various Provincial jurisdictions. By virtue both of economic size and cultural differences, special importance attaches to the problem of working out workable compromises with the Province of Quebec. In late September, Quebec Natural Resources Minister Rene Levesque announced that the Provincial Cabinet had agreed on five major goals to be given top priority during the next five years: (1) establishment of a basic steel industry; (2) civil service reform; (3) reorganization and improvement of the educational system; (b) professional training of competent technicians; and (5) the "rational channelling of capital" through creation of a universal pension fund that would help finance the provinces' economic strength and terminate what is considered at present an anomalous situation, viz., French-Canadian owership of a mere 10 per cent of the Province's economic wealth.

Reflecting the Province's strong identification with the issue of local autonomy, Quebec's brief to the Dominion-Provincial Conference that convened in Ottawa on November 26 argued strongly for a reapportionment of fiscal powers along the following lines: (a) the provinces should exercise minimum taxation authority to the extent of 25 per cent of personal income taxes, 25 per cent of corporate income taxes, and 100 per cent of inheritance duties; (b) inheritance duties should figure in the calculation of equalization payments from the Federal Treasury to bring the per-capita receipts from personal and corporate taxes up to the yield of the wealthiest province; (c) the entire administration of old-age pensions should be turned over to the provinces, together with the means for their financing; and (d) a permanent secretariat should be established to maintain continuing liaison between the two levels of government, together with a permanent council of the provinces. Other recent speeches by Quebec Cabinet Ministers have stressed the abolition of federal-provincial projects except on a strictly optional ("contracting in") basis, the return to the provinces of complete jurisdiction over municipalities, and the provinces' constitutional priority in social-security matters.

In some of these demands, Quebec can count on the support of certain of the other provinces. Alberta is sympathetic to the Quebec position on social welfare programs; Saskatchewan and British Columbia to the need for an increase in the provinces' share of direct taxation; and Manitoba, to the desirability of reassessing cost-sharing programs. Ontario, while urging a greater provincial sharing in direct taxation, argues against making any basic change in the structure of existing fiscal arrangements (which run to the end of 1966), against hampering the growth of wealthier provinces by excessive amounts of federal aid to the poorer provinces, and against any wholesale abandonment of shared-cost programs.

In the course of the conference, Prime Minister Lester Pearson indicated that the Federal Government was prepared to have the provinces take over exclusive responsibility for old-age assistance as well as for pensions to the blind and the disabled. On November 27, he announced the decision to provide the provinces with increased revenues by adjusting the formula for equalization payments, though without any changes in the Dominion-Provincial tax-sharing agreements. The net effect of this revision would be to increase the revenue available to the provinces by an estimated $200 million in the next fiscal year, of which $72 million would go to Quebec and $60 million to Ontario.