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Remarks by Mr. J.E. Coyne,
Governor of the Bank of Canada,
at the Annual Meeting of The
Dominion Mortgage and Investment
Association, held at Montreal,
May 5, 1955.

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It is a great pleasure to have been given the opportunity today to meet with your members, representatives of the investment side of the life insurance companies, trust companies and loan companies of Canada.

As a central banker, I am more directly concerned with the securities of the national government than the other forms of investment in which you are interested. But central banks and investment institutions have a wider field of common interest. The objectives of monetary policy relate to the effective functioning of the economy as a whole. To carry out these objectives, it is necessary to study and keep in touch with the general level of activity in the economy, its structure and development, and particularly with aspects of economic growth and change. These same factors provide the environment in which your investment decisions have to be made. And besides such common interests, we have a reciprocal interest, for the activities of the central bank in the monetary sphere will directly or indirectly have a bearing on your investment activities, and these in turn will have an influence upon monetary policy, both in conception and in detailed operation.

The title originally given to my remarks this evening -- "Investment in 1975" -- may have been somewhat misleading. If it suggested that I know what your investment problems will be in 1975, it promised more than I can deliver. My subject could be better described as a review of some possible features of economic growth in Canada, with a speculative eye turned on potential growth over the next twenty years.

The Minister of Finance in his budget speech announced that the Government is going to appoint a Royal Commission to study the problems of the future economic development of Canada. The Commission will no doubt cover a very broad field, and look far into the future. I have no wish to trespass on their territory, and will do little more than touch on a few broad aspects in the course of this after-dinner speech. I come armed with more questions than answers, and am confident only of one thing, that the future, even the relatively near future of 1975, will turn out to be in many ways quite different from what we expect. Life would be very dull if it were otherwise.

In the field of economics and finance, we can see tremendous changes if we look back over past decades, and all the indications are that this will continue for many years to come. In building a picture of the growth of the Canadian economy, the first factor to consider is the size of the population. The population of the world is said to have doubled between the birth of Christ and the year 1750 A.D. It took only 140 years to double again, and only 70 years to double the next time, if we may project present trends to 1960. The population of Canada is rising at a faster rate than that. Even with an annual rate of increase somewhat lower than that of the last 10 years, it is not difficult to foresee a rise of 50% over the next 20 years. The increase will apparently be concentrated very largely in urban areas, if the proportion of the population living on farms continues the decline that has been apparent here for several decades, and even longer in the United States. Changes in the age distribution of the population and, within each age group, of the proportion entering the labour force will apparently balance off, so that the total Canadian labour force may also be projected as about 50% greater in 1975 than in 1955.

The second major factor in economic growth is the average productivity of the economy per man employed. Over the past quarter century in Canada this seems to have risen at about 2% per annum on the average, although individual years have shown marked departures from this, and the rate of increase of productivity has varied widely from one industry or occupation to another. From 1947 to 1953 the average rate of increase was 2.7% per man per year. The recent rapid progress in mechanization in agriculture, and the increase in overall productivity resulting from the shift in the proportions of the labour force engaged in agriculture compared with occupations with a higher product value per unit of labour input, have perhaps made recent figures of increases in productivity greater than can be expected in future. But advances in technology will continue, and in Canada we should also realize each year more of the economies of mass production for a growing domestic market. A straight projection of future increases in productivity per man employed at the rate of 2% per annum would produce a gross national product by 1975, at 1955 prices, of $55 billion, or more than double the amount indicated for 1955.

Such a projection contains an implicit assumption that hours of work will continue to decline at no more than the rate evident in recent years, about ½% per year. Clearly, there might be a major change in thinking on this subject. Already one hears talk of the possibility of a 30-hour week; perhaps a more attractive target would be a 1500-hour year, or something intermediate between that and the present 2000-hour year in many industries, with leisure time taken more in the way of longer vacations than shorter hours of work during the work-week. In any case, the benefits of increased productivity could, if desired, be taken partly in the form of more leisure rather than more annual pay. Gross national product in material terms would to that extent fall short of the potential indicated.

Another assumption for maximum economic progress is that a high level of employment will prevail more or less continuously over the period. You may consider this a tall order. Personally, I am confident that the great depression of the thirties will never be repeated. Under-employment of productive facilities on such a scale is inconceivable now that society has come to understand and is determined to use the instruments of fiscal and monetary policy to promote economic stability and expansion. That milestone along the road of social evolution has been passed.

The question remains whether fiscal and monetary policy will be used effectively not only to prevent a major depression, but to prevent unemployment rising beyond a moderate level if and when temporary recessions in activity occur. There seems to be little division of opinion in Canada over the principle involved. Naturally, there will always be differences of opinion over the timing of particular measures, and the magnitude of what should be done. But it is recognized that both monetary policy and fiscal policy should be responsive to changes in general economic conditions, and adapt themselves to serve a broad economic purpose, rather than narrow technical purposes.

The same can be said of most other western countries. In the United States we have seen over the past several years wide variations in monetary policy, to restrain a boom and limit the spread of a recession.

In considering our own position in Canada we must recognize the possibility, indeed the probability, that from time to time recessions will develop in large industrial countries and communicate their effects to Canada, particularly as affecting our export industries, and industries competing with imports in the domestic market, and also industries which as a result of foreign ownership or close contacts with their opposite numbers outside our borders, are subject to the same psychological influences as are associated with the recession abroad. The relative impact on Canada may be greater than in the country of origin of the recession. At such a time it is possible that, in the interests of domestic stability, fiscal and monetary policy here might have to go a bit farther than the action being taken in, say, the United States. Such international differences in anti-recession policy might have the result of accelerating structural changes in the Canadian economy. The maintenance of a relatively higher rate of overall activity in Canada than in the outside world in such circumstances would mean that industries producing for domestic consumption would operate at a higher level than those producing for export.

In any case, it is reasonable to expect that exports, though continuing to be a major influence in our economy, will decline in importance relative to the whole. For example, if present trends continue, agricultural production will continue to rise in absolute terms, but not as fast as gross national product, and not as fast as the rise in the consumption of agricultural products in Canada. The exportable surplus may therefore be expected to decline, and before many years have passed we may have ceased to export any foodstuffs except wheat.

The value of all exports of goods and services in recent years has been equivalent to about 24% of gross national product, as compared with 30% in the late 'twenties, and a projection of the trend suggests a ratio of about 20% by 1975. This would be consistent with a rise in exports of goods by as much as 65% (against a rise of 100% or more in gross national product), so that I am not suggesting that exports and export industries will cease to be important, or that we will lose interest in efforts to keep open and if possible widen the channels of international trade.

We must recognize, however, that there are limits to our natural resources, and to the growth in production of raw and semi-finished materials which are the chief items in our export trade, and so to the amounts available for export after greatly increased domestic requirements have been met. On the other side of the trade picture, with increasing economic maturity we will be able to produce efficiently more of the finished goods hitherto imported, so that imports, rising by perhaps 50%, will nevertheless grow less rapidly than total consumption of such goods.

The overall effect of such developments should be that the Canadian economy would be more stable, because more dependent on production for domestic use and less exposed to the leverage effect on a small country's trade and unemployment of even moderate fluctuations in other much larger economic units.

This picture would be somewhat changed, at least in degree, if strong foreign demand for raw materials, and rising prices, coincided with large new mineral discoveries in Canada. Over the next 20 years, while the population of Canada rises by 7 or 8 million, the population of the United States is expected to increase by 50 million or more, and while our gross national production, and so consumption, may increase by $30 billion worth of goods and services per annum, the United States economy will be capable of chewing up an extra $300 billion worth, or more, in 1975 as compared with 1955. A very large increase may also take place in the rest of the world. At present it looks as though the United States will become increasingly dependent on foreign sources of raw materials. Perhaps the necessary supplies will be developed at moderate cost from the virtually untouched resources of Africa, Asia and South America. If not, the rate of development and exhaustion of Canadian resources, particularly of minerals, will be greatly accelerated. Agricultural settlement, at least of a familiar kind, has not much farther to go, and our forest resources are also within sight of maximum annual cropping. Minerals once taken are not replaced. One can see the possibility of major questions of conservation policy and of the best utilization of natural resources arising for consideration in the years ahead.

Financial growth will accompany physical growth of the economy, though the annual increase in the rate of investment in capital assets may not be as great as the rate of increase in total output. There are some signs that the proportion of gross national product devoted to annual capital formation may decline from recent levels, which have been unusually high. One would certainly expect that the net inflow of capital from abroad evident in the last three or four years would disappear with growing maturity, and with it the corresponding deficit in the current account of the balance of payments, or excess of imports of goods and services over exports. Perhaps the rate of capital formation will decline by more than the change in our international balance, the difference being matched by a decline in the percentage of income saved in Canada from the very high levels of recent years. This might take the form of an increase in personal consumption expenditures as a percentage of personal incomes, or an increase in the percentage of corporate profits distributed to shareholders, or both.

These are questions of degree. There seems little doubt that both saving and investment will continue to grow on a sufficient scale to provide financial institutions as a group with the pleasant prospect of continuous and substantial increases in their total assets.

A marked feature of the present century is the development of financial institutions to handle and invest sums saved out of income by a very large number of individuals. Accumulation of bank deposits and accumulation of savings in the form of insurance reserves of life insurance companies have been the two chief channels of these funds. Pension funds seem likely to develop into a third major channel in the years ahead.

An expansion of bank deposits is sometimes regarded as a symptom of inflation; indeed, some people would define inflation as simply meaning an increase in the money supply as represented by bank deposits. This seems to me to rob the word of any real meaning. Inflation in any significant sense means a rise in the general price level and while this can, it is true, be brought about by an excessive increase in the money supply, it is clear that a growing economy requires more money for the transaction of business and that an increase in the active money supply which is reasonable in relation to such requirements need not have any inflationary effect on prices. Similarly, it is to be expected that savings deposits as well as current account balances with our banks will continue to increase over the next twenty years and that monetary policy must be such as to facilitate such an expansion.

One can see the possibility of changes in the outlets for investment funds. It seems likely that residential mortgage financing, at least of new residences, will decline in relative importance. For several years recently the net increase in the supply of housing -- new houses built, plus additions by conversion of existing premises, less the number of housing units demolished -- has exceeded the rate of net family formation. This catching-up process will come to a natural end. The population statistics I have been using indicate a rate of net family formation by 1975 of about 120,000, compared with about 90,000 in recent years.

So far in our history, the estimated rate of scrappage of houses has not exceeded 10,000 per annum. Admittedly that figure should grow, but unless and until it does, the required volume of housing starts per annum will not increase over the actual rate of last year by more than a moderate percentage. It is possible, of course, that the cost of building houses will rise in relation to the general price level, and also that part of the higher standard of living will take the form of a higher standard of housing, both of which developments would add to the amount of funds required for investment in that field.

The capital requirements of governments and public enterprises may increase relative to total investment. Very large sums will be required for investment in social capital, by way of highways, schools, universities, hospitals and various urban facilities, together with great expansion in transportation and public utility enterprises under public ownership. Under conditions of growth it would be unrealistic to expect governments to pay for capital expenditures out of ordinary current revenue. One might expect therefore a substantial rise in borrowings by or guaranteed by various levels of government to finance the creation of capital assets, and so long as growth continues the amount of new borrowing will exceed the amount of annual repayments of government direct or guaranteed debt. This outlet for investment funds will therefore continue to bulk large in the total.

No doubt there will be a continuation of a substantial volume of investment in resource development, although perhaps not increasing as rapidly as total investment. The remaining categories of new investment, such as heavy industry, secondary industry and services, may well increase relatively to the total.

Canadians have not been very enthusiastic investors in the equity or common stock of productive enterprise in Canada. Preference for debt instruments rather than equities seems to have been very strong both amongst individuals and amongst institutional investors, as a glance at the portfolio distribution of your members will emphasize.

A further illustration may be seen in the fact that every year for the past thirty years, the value of dividends paid by Canadian corporations to non-residents, plus the profits of Canadian branches of parent companies abroad, has been greater than the total amount paid by Canadian corporations to Canadian residents, excluding dividends paid by one Canadian corporation to another.

One must expect that as time goes by greater interest will be shown by Canadian individuals and institutions in acquiring a share in the ownership of businesses operating in Canada. In the past, a large part has necessarily been played in our development by large foreign corporations able to provide both capital and know-how and to develop businesses in Canada as off-shoots of much larger operations in the United States and other foreign countries. It is logical to expect that over a period many of these branch plants and subsidiaries will develop into independent enterprises conducting their operations in Canada in much the same manner as our domestic Canadian businesses.

I mentioned earlier the possibility that the need for capital funds might decline somewhat relative to total product and to savings, at least to the extent that we would cease to be a net importer of capital. We might become a net exporter of capital, and find this might become another major outlet for the investment of domestic savings.

It is a normal evolution, exemplified in the history of the United States, among others, for a country which was dependent on foreign capital for its early development, to reach a stage where it begins to pay off foreign debt and repatriate foreign-held investments, not by compulsion but by the voluntary decisions of persons free to buy and sell securities as they chose. Canada has, in fact, largely paid off or bought back foreign holdings of Canadian government securities. The next stage will be the repatriation of corporate securities, foreign holdings of which are mainly in equities.

This requires, of course, not only a desire on the part of Canadians to buy, but a willingness on the part of foreign investors to sell. So far as securities have been publicly distributed, they are free to move across the frontier in either direction, according to the views taken by Canadian and foreign investors as to relative values. But this is not the typical case. There are still many cases where it is next to impossible for a Canadian to buy stock in a Canadian industry, because all or nearly all of the various companies in that industry are wholly owned by foreign corporations. With growing maturity, part or all of the stock ownership of such Canadian subsidiaries may be made available to the public in Canada either by way of a direct public distribution, or by the indirect process by which stock in the Canadian company is in the first place distributed among the shareholders of the foreign parent company instead of being held by the parent company itself. Once so distributed the stock is available for repatriation to Canada. Several important instances of this sort have occurred and it seems reasonable to expect many more in the future.

I believe that Canadian financial institutions will have increasing opportunities over the next twenty years to assist in the financing of Canadian enterprises, and to make substantial profits in so doing for the benefit of the millions of individuals who entrust their savings to such institutions. I should not be at all surprised therefore to see life insurance companies, for example, increase the proportion of common stocks in their portfolios to the extent authorized by their statutes. Only in this way can they and their beneficiaries participate in the real growth of the Canadian economy. Certainly there should be opportunities in the years ahead for all investment institutions to assist in the repatriation to Canada of some of the Canadian enterprises now in foreign ownership, as well as to participate in the future development of Canadian industry by providing a reasonable supply of equity funds as well as funds for fixed interest obligations.

Another field in which further growth within Canada can be expected is that of technological research. There are still broad industrial fields in which the Canadian firms do no research but pay a service charge for the results of research conducted by American parent plants. This may appear economical on a short run view of dollar costs but it has a stultifying effect on national development in such fields and makes it necessary for Canadian scientists and technical workers to leave their homes and go to the United States not in order to obtain the higher salaries there available but simply to find an outlet for their talents and an opportunity for constructive work in the field in which they are interested.

If I may summarize what I regard as a probable major trend in our future economic development, I would say that what might be called a tendency towards Canadianization of our economy, as opposed to Continentalization, will manifest itself in a number of ways as our economy grows more mature and greater pools of savings surplus to immediate requirements accumulate in the hands of the Canadian people.

The decrease in percentage of gross national product represented by exports and imports, the growing consumption within Canada of our agricultural and other natural products, the greater development of secondary industry and the more balanced national development resulting therefrom, the repatriation of at least some share in foreign-owned Canadian enterprises, a greater measure of autonomy and independence on the part of Canadian management, the continued development of communications in Canada, the knitting together of our widely separated centres of population by trade as well as by railroads, highways and national radio and television networks and other cultural movements are all features of this development, and of growing national strength.