

BANK OF CANADA

ANNUAL REPORT TO
MINISTER OF FINANCE
AND
STATEMENT OF ACCOUNTS

FEBRUARY 9TH, 1943

BANK OF CANADA

INCORPORATED UNDER THE BANK OF CANADA ACT, 1934

HEAD OFFICE—OTTAWA

BOARD OF DIRECTORS

G. F. TOWERS
Governor

D. GORDON
Deputy Governor

E. G. BAKER	TORONTO, ONT.
W. D. BLACK <i>Member of the Executive Committee</i>	HAMILTON, ONT.
G. G. COOTE	NANTON, ALTA.
J. L. HOLMAN	SUMMERSIDE, P.E.I.
F. MAGEE	PORT ELGIN, N.B.
W. K. MCKEAN	HALIFAX, N.S.
A. STEWART McNICHOLS	MONTREAL, QUE.
A. C. PICARD	QUEBEC, QUE.
E. J. TARR	WINNIPEG, MAN.
A. C. TAYLOR	VANCOUVER, B.C.
R. A. WRIGHT	DRINKWATER, SASK.

Ex Officio Member of the Board

W. C. CLARK
Deputy Minister of Finance

OTTAWA, ONT.

OFFICERS

G. F. TOWERS
Governor

L. P. SAINT-AMOUR
Assistant Deputy Governor

D. GORDON
Deputy Governor

K. A. HENDERSON
Securities Advisor

SECRETARY'S DEPARTMENT

D. G. MARBLE
Secretary

FOREIGN EXCHANGE DIVISION

S. TURK
Chief

W. A. CAMERON
Deputy Chief

L. P. J. ROY
Deputy Secretary

CURRENCY DIVISION

C. E. CAMPBELL
Chief

J. P. MELVIN
Deputy Chief

RESEARCH DEPARTMENT

D. A. SKELTON
Chief

J. R. BEATTIE
Deputy Chief

CHIEF ACCOUNTANT'S DEPARTMENT

H. R. EXTENCE
Chief Accountant

PUBLIC DEBT DIVISION

M. G. ANDERSON
Chief

F. M. PETERS
Deputy Chief

SECURITIES DEPARTMENT

W. B. WATSON
Chief

W. H. BUDDEN
Deputy Chief

J. W. GRANT
Toronto Representative

C. DE V. WELSFORD
Montreal Representative

AUDIT DEPARTMENT

E. FRICKER
Auditor

AGENCIES

CALGARY, ALTA. J. PARRY AGENT

CHARLOTTETOWN P.E.I. D. A. MACKINNON "

HALIFAX, N.S. P. B. WOOSTER "

MONTREAL, QUE. J. H. C. DESMARAIS "

OTTAWA, ONT. E. METCALFE ACTING AGENT

REGINA, SASK. G. A. IVEY AGENT

SAINT JOHN, N.B. E. H. CAMERON "

TORONTO, ONT. K. FREDERICKSON "

VANCOUVER, B.C. S. A. STADEN "

WINNIPEG, MAN. W. MORTON "

BANK OF CANADA

Ottawa, February 9th, 1943

The Hon. J. L. Ilsley,
Minister of Finance,
Ottawa.

Dear Sir,

In accordance with the provisions of the Bank of Canada Act Amendment Act, I am enclosing herewith in duplicate a statement of the Bank's accounts for the fiscal year 1942, signed by the Governor and the Chief Accountant, and certified by the Auditors in the form prescribed by the by-laws of the Bank.

The major changes which took place in our various asset and liability accounts during the course of the year are indicated in the following table, which shows the effect of these changes on the cash reserves of the chartered banks.

<u>Calendar Year 1942</u>	<u>Changes producing a decrease in chartered banks' cash</u>	<u>Changes producing an increase in chartered banks' cash</u>
	(Millions of Dollars)	
Decrease in Sterling and U.S.A. Dollars	200.4	
Increase in Dominion and Provincial Government Securities		407.9
Decrease in Other Assets	2.2	
Increase in Rest Fund	.9	
Increase in Active Note Circulation	192.9	
Decrease in Dominion Government Deposits		18.0

BANK OF CANADA

<u>Calendar Year 1942</u>	<u>Changes producing a decrease in chartered banks' cash</u>	<u>Changes producing an increase in chartered banks' cash</u>
	(Millions of Dollars)	
Increase in Other Deposits	13.1	
Decrease in All Other Liabilities		16.1
	<u>409.5</u>	<u>442.0</u>
Deduct		<u>409.5</u>
Increase in Chartered Banks' Cash Reserves		<u><u>32.5</u></u>

NOTES IN CIRCULATION

At December 31st last, Bank of Canada note issue was \$693,617,931, an increase of \$197,661,699 from the preceding year. Of the total amount of our notes outstanding, \$121.1 millions were held by the chartered banks and \$572.5 millions in the hands of the general public. The amount of Bank of Canada and chartered bank notes in public hands at the end of each of the last five years has been as follows:

	(Millions of Dollars)				
<u>December 31st</u>	<u>1938</u>	<u>1939</u>	<u>1940</u>	<u>1941</u>	<u>1942</u>
Bank of Canada Notes	118.4	162.2	261.6	379.6	572.5
Chartered Bank Notes	88.3	84.6	79.8	70.6	60.3
TOTAL	<u><u>206.7</u></u>	<u><u>246.8</u></u>	<u><u>341.4</u></u>	<u><u>450.2</u></u>	<u><u>632.8</u></u>

In previous annual reports I have referred to various factors which explain the large and continued increase in publicly-held note circulation. Broadly speaking, this expansion is the result of the growth in employment and incomes which has taken place during the war. Most of this increase has been in the armed services and industry where the proportion of income payments by means of currency is quite high.

RESERVES

In last year's annual report, I referred to the fact that the Foreign Exchange Control Board found it necessary during the latter part of 1941 to sell sterling exchange to the Bank of Canada under a repurchase agreement. This acquisition of sterling by the Bank continued in the first quarter of 1942 and the amount so held reached a total of \$474 millions on March 25th. Following the passing of the War Appropriation (United Kingdom Financing) Act on March 27th, 1942 the Bank's holdings of sterling exchange were repurchased by Foreign Exchange Control Board and sold to the Government. This transaction took place in two main stages. At the end of March, the Government used part of the proceeds of the Second Victory Loan to repurchase sterling and in June the Government sold \$193 millions of short term securities to the Bank of Canada to obtain funds for the same purpose. The total of "Sterling and U.S.A. Dollars" shown on our balance sheet on December 31st last was \$499,192.

INVESTMENTS

Our holdings of Dominion and Provincial Government securities were \$1,016,400,722 on December 31st last, having increased \$407,928,857 during the year. All of this increase was in the category of securities maturing within two years. In January and February of 1942, the Bank sold about \$175 millions of short term Dominion securities to the chartered banks in order to offset an increase in chartered banks' cash reserves which otherwise would have taken place, due to the increase at that time in our sterling exchange holdings to which I have already referred. Early in March, these securities were repurchased from the chartered banks, offsetting the effect on cash reserves of the transfer of Dominion Government balances to the Bank of Canada pending the purchase of sterling by the Government. On June 2nd, the

Bank bought from the Government \$192,831,000 of short term securities the proceeds of which were used by the Government to purchase sterling exchange as I mentioned in the preceding section.

In the latter half of 1942, chartered banks' Canadian deposit liabilities increased because of Government financing requirements to which I shall refer later. During this period we bought a considerable amount of securities on the market in order to maintain the cash reserve position of the banks at the usual ratio to their deposit liabilities.

On the basis of the Wednesday figures published in our weekly statement, our total investments averaged \$165 millions more in 1942 than in 1941.

PROFIT AND LOSS

The net profit from our operations in 1942, after providing for contingencies and reserves, was \$9,097,478.25. Payment of a dividend of \$225,000 on capital stock held by the Minister of Finance left \$8,872,478.25 as compared with \$5,588,385.80 in 1941. The increase was mainly attributable to the higher average level of our security holdings to which I have already referred.

Section 31 (b) of the Bank of Canada Act provides that one-tenth of the surplus available from operations of the Bank shall be allocated to the Rest Fund and the residue paid to the Receiver General and placed to the credit of the Consolidated Revenue Fund. In accordance with these provisions \$887,247.82 of the profits available for distribution was added to our Rest Fund and the remaining \$7,985,230.43 was paid to the Government.

PREMISES

In my report last year I referred to the fact that we had found it necessary to undertake the construction of a fire-proof building to house the War Savings Section, which is

responsible for the issuance and redemption of War Savings Certificates. The move of our staff to these new premises in King Edward Avenue, Ottawa, took place last October. I feel that the architects and contractors ought to be congratulated on having produced, at reasonable cost, a building of simple and pleasing design which is well suited to our purposes.

STAFF

Excluding personnel who are on leave of absence while serving with the Armed Forces, the staff of the Bank numbered 1180 as at December 31, 1942, an increase on the year of 81. On January 1, 1942, 115 of the temporary staff on loan to the War Savings Committee were absorbed by the National War Finance Committee. This decrease was more than offset by the net addition of 170 to the staff of the War Savings Section, and of 26 in all other departments and Agencies of the Bank. Almost all of the new employees are young women, and it will be of interest to note that the male staff is now reduced to 13.8 per cent of the total.

The additions to the public debt arising out of the sales of new Victory Bonds and War Savings Certificates, the increase in notes in circulation and special activities arising out of the war have added very greatly to the work of the Bank. It is due to the devotion of senior officers in training new employees as well as looking after their own increased duties, and the excellent response from the young women who have been placed in positions of some responsibility, that we have been able to carry on successfully. I wish to record my sincere appreciation of the able and unselfish co-operation of all members of the staff.

BANK RATE

Bank Rate has remained unchanged throughout the year at $2\frac{1}{2}$ per cent. Some credit facilities were required by

banks subsequent to the issuance of the Second and Third Victory Loans, but the total amounts involved were relatively small.

SECURITY MARKETS

The year was marked by two large public security offerings. The Second Victory Loan issued in February and March received total cash subscriptions of \$843 millions and was participated in by 1,681,267 subscribers. The Third Victory Loan issued in October and November brought cash subscriptions totalling \$992 millions and a total of 2,041,610 subscribers. These figures show the broad measure of support which these loans have obtained from the public; since the Government's borrowing requirements have increased, an even greater degree of public participation will be needed in 1943.

Our estimate of net new bond issues during 1942 is shown in the appended table. The Dominion Government's net new borrowing from the Canadian public as a result of increased war expenditures again reached a new high. On the whole, provincial and municipal governments and corporations continued to effect a net reduction in their bonded debt.

Although the Canadian bond market continued to absorb a large amount of new money during the year, high-grade bond prices remained firm and even rose fractionally in some cases. In the United States and United Kingdom, long-term government securities also remained relatively unchanged over the year.

CREDIT EXPANSION

During 1942, Canadian deposit liabilities of the chartered banks increased \$499 millions; in addition total active note circulation rose \$183 millions. The total expansion in bank deposits and notes, therefore, was \$682 millions during the year.

In view of the pressure on our human and material resources brought about by war requirements, it has not been necessary or desirable for some time to provide a further stimulus to the economy through monetary expansion. But the Government's war expenditures have mounted more rapidly than receipts from greatly increased taxation and purchases of securities by the public, making it necessary to borrow the remaining requirements from the banking system. That monetary expansion during the past year has been associated with Government fiscal needs is shown by the fact that the increase in banking security portfolios has been greater than the rise in the volume of money.

Chartered bank holdings of Dominion and Provincial Government securities rose \$485 millions during 1942. The major part of this increase was accounted for by the Government selling Deposit Certificates to the banks, starting in the last week of July and continuing on a weekly basis in varying amounts until the proceeds of the Third Victory Loan began to come in during October. At that time \$645 millions of Deposit Certificates were outstanding but the Government subsequently by arrangement took up \$205 millions from the banks in November, leaving the amount presently outstanding at \$440 millions. Deposit Certificates were issued for a term of six months at a rate of three-quarters of one per cent per annum.

GENERAL

Over the past four years, total government expenditure (including provincial and municipal) has increased from about \$1 billion a year to about \$5 billions a year. At the same time, unemployment has virtually disappeared and the gross value of Canada's output of goods and services has increased from about \$5 billions a year to more than \$9 billions. Even after allowing for an over-all price increase of, say, 20 per cent., the figures indicate that the volume of output has shown a tremendous expansion, which has not yet ceased.

At the beginning of this period, much surplus capacity was available and rising war expenditures did not at first entail any net decrease in the volume of things which civilians could buy. Indeed, the production (and consumption) of these things expanded somewhat in response to the increased demand of those whose incomes were rising because of the war expenditures. In terms of employment and, to a smaller degree, standards of living, the contrast with the depressed years before the war was striking. In the later stages, of course, war expenditure has increased more rapidly than national production and average living standards are therefore declining. But the experience of the last four years has shown that Government war expenditure on a sufficient scale can produce full employment.

These developments undoubtedly have made a deep impression upon the public mind. There may be a tendency to conclude that Government expenditure for other purposes, at a high enough level, is all that is required to prevent depression in peace time. Such a conclusion does not give sufficient weight to the other important conditions which have existed during the war period.

The need for war goods and services has by common consent been given preference over every other interest. The public has been willing to do whatever is necessary to obtain the maximum output for military purposes. Individuals have worked, have shouldered tax burdens, and have put up with limitations upon their freedom as producers and consumers to a degree that would have been regarded as unthinkable before the war. The Government's willingness to spend the large amounts of money involved in the war programme has been a necessary and important feature but even more important has been the unity of national purpose which has produced such remarkable economic results over the past four years.

After the war is over, the present driving stimulus to maximum employment and production will be removed. If we are to maintain full employment in peace time, we must substitute other objectives for the current will to win the war. Broadly speaking, our goals should be to provide a rising standard of living and to contribute to the establishment of a world economy which will remove the threat of war. However, concrete and detailed consideration and approval of the specific measures which must be taken to implement a general programme are necessary before broad policies can be effectively translated into action. Proper financial and economic policies can play an important part in the attainment of such peace time objectives. But if we are to achieve success, I feel that we must have the same broad measure of public support behind those objectives that is now back of our efforts to win the war.

I am,

Dear Sir,

Yours faithfully,

G. F. TOWERS,

Governor.

ESTIMATED
NET NEW BOND ISSUES OR RETIREMENTS

(Par Values in Millions of Canadian Dollars)

Calendar Years	Dominion and C.N.R. (1)	Provinces	Private Corporations	Total (2)
PAYABLE IN CANADA ONLY				
1936	125	66	183	374
1937	25	82	75	182
1938	91	60	31	182
1939	74	52	96	222
1940	434	74	21	487
1941	731	3	30	698
1942	1,830	3	5	1,822
PAYABLE ABROAD, ONLY OR OPTIONALLY				
1936	39	27	139	205
1937	14	24	87	125
1938	21	11	45	77
1939	96	29	127	194
1940	156	15	34	205
1941	183	18	26	227
1942	290	42	48	380

(1) Includes War Savings Certificates, but takes no account of Treasury Bills, Deposit Certificates or Dominion of Canada short-term issues sold to the banks, of which the amount outstanding increased (in millions of dollars) 57, nil, 5, 200, 325*, 290 and 633** respectively in the calendar years 1936 to 1942.

* \$250 millions of 1% 1-year notes and \$75 millions of Treasury Bills issued to the Bank of Canada in connection with the Foreign Exchange Acquisition Order of April 30th, 1940.

** Including \$193 millions sold to Bank of Canada, proceeds of which were used by the Foreign Exchange Control Board to re-purchase sterling exchange sold to the Bank in 1941.

(2) Available information concerning issues and retirements by municipalities and religious institutions was not sufficiently comprehensive to justify including such classifications of bonds in the table. However, the net reduction in total municipal bonded debt less sinking funds has been (in millions of dollars) approximately 25, 30, 39, 30, 47 and 45 respectively, in the years 1937 to 1942.

BANK OF CANADA
STATEMENT OF ASSETS AND LIABILITIES
as at 31 December, 1942

LIABILITIES

CAPITAL :

Authorized, 100,000 shares par value \$50.00 each \$ 5,000,000.00
Issued and Paid Up \$ 5,000,000.00

REST FUND 6,472,952.97

NOTES IN CIRCULATION 693,617,931.36

DEPOSITS:

Dominion Government . . . \$ 59,617,502.50
Chartered Banks 259,939,055.97
Other 19,070,677.48 338,627,235.95

DIVIDEND DECLARED :

Payable 2nd January, 1943 112,500.00

ALL OTHER LIABILITIES 4,380,593.82

AUDITORS' REPORT

We have examined the above statement of assets and liabilities of the Bank of Canada as at 31st December 1942 and have received all the information and explanations we have required. We report that, in our opinion, it is properly drawn up so as to exhibit a true and correct view of the state of the Bank's affairs as at that date, according to the best of our information, the explanations given to us and as shown by the books of the Bank.

G. T. CLARKSON, F.C.A.,
of the firm of Clarkson, Gordon,
Dilworth & Nash,

MAURICE CHARTRÉ, C.A.,
of the firm of Chartré, Samson & Co.

Ottawa, Canada, 26th January, 1943.

\$1,048,211,214.10

ASSETS

RESERVE :

Sterling and U.S.A. dollars, at market value \$ 499,191.73

SUBSIDIARY COIN 55,547.24

ADVANCES TO CHARTERED AND SAVINGS BANKS 1,250,000.00

INVESTMENTS—at values not exceeding market :

Dominion, Dominion guaranteed and Provincial Government short term securities . \$807,227,340.51

Other Dominion, Dominion guaranteed and Provincial Government securities . . 209,173,381.67 1,016,400,722.18

BANK PREMISES :

Land, Buildings and Equipment —at cost less amounts written off 2,108,475.99

ALL OTHER ASSETS 27,897,276.96

\$1,048,211,214.10

G. F. TOWERS,
Governor.

H. R. EXTENCE,
Chief Accountant.

BANK OF CANADA

PROFIT AND LOSS ACCOUNT

For the Year Ended 31st December 1942

PROFIT FOR THE YEAR ENDED 31ST DECEMBER, 1942, after making provision for Contingencies and Reserves	\$9,097,478.25
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APPROPRIATED AS FOLLOWS:

Dividends for the year ended 31st December 1942 at the rate of 4½% per annum:-		
No. 16 paid 2nd July 1942	\$ 112,500.00	
No. 17 payable 2nd January 1943	112,500.00	225,000.00

BALANCE	\$8,872,478.25
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TRANSFERRED TO REST FUND	\$ 887,247.82
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TRANSFERRED TO THE RECEIVER GENERAL OF CANADA FOR CREDIT TO THE CONSOLIDATED REVENUE FUND	7,985,230.43 <u>\$8,872,478.25</u>
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REST FUND

BALANCE AS AT 31ST DECEMBER 1941	\$5,585,705.15
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AMOUNT TRANSFERRED FROM PROFIT AND LOSS ACCOUNT AT 31ST DECEMBER 1942	887,247.82
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BALANCE AS AT 31ST DECEMBER 1942	\$6,472,952.97
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