BANK OF CANADA

ANNUAL REPORT OF THE GOVERNOR TO THE MINISTER OF FINANCE

AND STATEMENT OF ACCOUNTS

FOR THE YEAR 1969

BANK OF CANADA Ottawa 4

February 28th, 1970.

The Hon. E. J. Benson, P. C.,
Minister of Finance,
Ottawa, Ontario.

Dear Sir,

In accordance with the provisions of the Bank of Canada Act I am transmitting herewith my report for the year 1969 and a statement of the Bank's accounts for this period which is signed and certified in the manner prescribed in the by-laws of the Bank.

Yours very truly,

L. Rasminsky

Governor

BANK OF CANADA

Report of the Governor — 1969

Some Highlights of the Year

The past year was one of both strain and progress in the world economy. The major industrial countries virtually all experienced strong inflationary pressures which threatened the continuation of the long period of expansion. There was, however, reason for encouragement in the action taken by the authorities of many countries, including the United States, to change the inflationary environment by checking excessive demand pressures. Another hopeful development was that the international currency system, which had been beset by a number of crises in the past few years, was a good deal more stable at the end of 1969 and a considerable degree of confidence had been restored.

While economic activity in Canada continued to expand for the ninth successive year, the over-all performance of the economy in 1969 cannot be regarded as satisfactory; prices continued to rise at an unacceptable rate, and public policy, including monetary policy, had to be vigorously directed to restraining the inflationary pressures.

After so long a period of expansion and after several years of significant price rise, the expectation of continued price increases had come to be firmly embedded in the thinking of many important elements of the community and the response to the policies of restraint was slow. However, by the latter part of 1969 there were signs of a slowing down in the rate of expansion, though there is not as yet convincing evidence of moderation in the rate of price and cost increase.

The slowing down in the rate of expansion in Canada and the development of a greater degree of slack does not become apparent if one looks merely at the annual changes in output and unemployment. Indeed, the increase in real output in 1969—nearly 5 per cent—was about the same as in 1968. Unemployment in 1969 averaged 4.7 per cent, slightly less than in 1968 and in January 1970 it was 4.5 per cent, seasonally adjusted. But the labour force has grown at an abnormally low rate since the first quarter of 1969; and the higher average level of output in the year as a whole owed a great deal to a continuation into the first quarter of 1969 of a particularly strong period of expansion. For the balance of the year the underlying trend—if one looks through the distorting effects of the important strikes that occurred—was that expansion was proceeding at a distinctly lower rate.

For five years now, the Consumer Price Index has been rising at a rate in excess of 3 per cent a year and for the past two years at rates of 4 per cent to 4½ per cent. The need for stringent monetary policies to help contain and combat this erosion in the purchasing power of money has been widely accepted in Canada, mainly, I believe, because of a growing appreciation, based on concrete experience, of the dangers of inflation. There are, to be sure, some differences of opinion in the approach to economic policy, but it would be a mistake to believe that these differences reflect different basic attitudes towards fundamental aims. In particular, there is not, as is sometimes alleged, one group who care about people and their employment and another group who care only about price stability. This is a false antithesis. Everyone wants to achieve increases in output, employment and standards of living that are as great as can be managed. The differences of opinion reflect, in large measure, differences in time perspective. Some concentrate their attention on the short-run costs of anti-inflationary policies. On the other hand, those who stress as I do the importance of price stability believe that we shall have a better chance of maintaining a high rate of growth of employment in the future if care is taken to preserve the purchasing power of money. More than this, they feel as I do that there is no justification for risking the serious injury to our economy and our society which would occur if measures of restraint were insufficient and inflation were permitted to accelerate.

Some slowing down of the economy was indeed, in the circumstances, a necessary prelude to a reduction of price and cost pressures. The purpose of restraint is not, however, to slow down the economy for its own sake but as a means of slowing down the price and cost increase in order to provide a solid base for sustainable economic expansion. Policy will not achieve its objective if it is abandoned at the first sign of success, namely, as soon as the growth of the economy shows signs of deceleration. This is particularly the case if there are widely held inflationary expectations.

The public authorities must, of course, always be mindful of the danger of pushing restraint beyond the point necessary to do the job of dealing with the inflationary situation. There are lags in the effect of policies of restraint on total spending in the economy and of changes in total spending on costs and prices which must be kept in mind. So far as the central bank is concerned, there is no escape from the difficult judgments which must continuously be made: it must be constantly appraising all the information which is becoming available and must balance the risk of going too far and contributing to an undesirable degree of slack in the economy against the risk of premature or excessive relaxation which would trigger off fresh inflationary expectations and actions.

The results up to the present of the policies followed during the past year make it reasonable to hope that continued efforts to control inflation will begin to yield their fruit and permit us to return to sustained non-inflationary growth. There has been an encouraging change in the economic climate. Meanwhile, a widespread understanding of the problem continues to be necessary, and because of this I comment in some detail in the immediately following pages of my Report on the way in which anti-inflationary policies can be expected to work, on some of the particular problems of conducting such policies in Canada, and on the reasons why, in my opinion, we have no choice but to continue the effort in spite of all the difficulties involved. This is followed by a review of the main developments in monetary policy during the past year; the first part of the Report concludes with some general observations on recent international financial developments.

THE PROBLEM OF INFLATION

Throughout the past year the policy of the Bank has been directed towards achieving and maintaining tight credit conditions in order to help bring inflationary pressures in the economy under control. The thrust of fiscal policy has been in the same direction. For the most part, monetary and fiscal policies operate through market forces. The slowing down of the growth of total spending which these policies produce causes markets for goods and services to soften, and it becomes difficult for businessmen to raise prices. A squeeze on profits develops and businesses eventually have no alternative but to resist cost increases, including increases in wages and salaries which go much beyond the increase in productivity. (The crucial role played by wages and salaries in the price increases of recent years is shown in the table on page 32.)

Policies of financial restraint do not eliminate inflation very rapidly, particularly if price and cost increases have developed a good deal of momentum. Moreover, they are not without real costs in terms of a temporary loss of employment and output. Unless we are prepared to accept widespread direct governmental intervention, there is really no choice but to place major reliance on monetary and fiscal policies if we seriously wish to control inflation and avoid major damage to the economy. Naturally, it would be better if inflation could be dealt with by increasing the supply of goods and services rather than by restricting demand. "Supply" policies designed to increase the efficiency and mobility of our resources (such, for example, as retraining and the development of labour skills) are indeed of fundamental importance to the long-run performance of the economy, and much emphasis has properly been placed on them by governments. But such policies cannot unfortunately be expected to make an important contribution to the present urgent problem of controlling inflation.

There are time lags which delay the impact of policies to restrain spending. I shall refer in the next section to some of the lags involved in the effect of changes in monetary policy on the availability of credit. Even when monetary restraint is fully effective and conditions in financial markets become tight, individuals and businesses do not react immediately by moderating their spending plans; this is particularly so in the case of expenditures on new plant and equipment. The impact of tightening is delayed even more if there are strong expectations of continuing inflation. In this situation individuals may continue to believe that it is in their interest to spend sooner rather than later. If taxes are raised, for example, they may for a time save less. If interest rates go up, borrowers of all types may nevertheless be willing to pay the higher rates in order to forestall anticipated price rises. Even very high rates of interest may not stimulate enough saving and lending because of lack of confidence in the purchasing power of the dollars that will be received in repayment.

As I noted earlier, the growth of total spending in the economy has now slowed down. One reason this has so far had little obvious effect in checking price increases is that our economy, like other modern industrial economies, is not perfectly competitive. After demand slackens prices and costs may continue for awhile to rise, even though this means a reduction in the volume of output.

External price pressures have also tended to delay the price response to the slowing down of demand in Canada. In 1969 consumer prices increased more in the United States than in Canada and our other major trading partners have problems of inflation somewhat similar to ours. However, the United States and other countries are making determined efforts to bring inflation under control and our dependence on foreign trade makes it necessary for us to do at least as well.

Canada has a special problem in dealing with inflation which results from its proximity to the United States. The expectations of Canadians as to their incomes and standard of living tend to be based on the American example—and may surpass it in the case of some government services—even though our productivity is currently at least 20 per cent lower and this fact sets a real limit on our current living standards which no amount of wishful thinking can remove.

We also have difficult problems arising out of the geographic characteristics of the Canadian economy. Our population and natural resources are unevenly distributed over a large area, with great differences in the regional economies and considerable variations in economic conditions. These disparities are a fact of our national life, one which we must constantly work at mitigating. A later section of this Report (pp. 34 to 38) provides a good deal of evidence of our problems of regional disparity. There it is shown, for example, that while average unemployment (not adjusted for seasonal variations) in the fourth quarter of 1969 was 4.3 per cent of the labour force for the country as a whole, it was over 6 per cent in New Brunswick and Quebec and nearly 9 per cent in Newfoundland. At the same time, it was under 3 per cent in Manitoba, Alberta and Ontario. Other regional disparities arise from changes in the world markets for specific products, over which we have little if any influence. The recent serious blows to the Saskatchewan economy from developments in the world wheat and potash markets constitute a case in point.

The federal nature of our country also creates some special problems in dealing with inflation. The primary responsibility for economic stabilization rests with the federal Government, but the impact on the economy of the policies of other levels of government has increased sharply over the last decade. Rapidly growing demands have been placed on the services which are the primary responsibility of provinces and municipalities—education, health care, roads and urban facilities. This situation, coupled with problems of divided jurisdiction in some fields, complicates the problem of achieving a good over-all balance of policy with suitable regional impact. It is an important reason why consultation and co-operation among governments is highly desirable in the development of economic policies.

Recognition of all these Canadian facts of life cannot, however, alter the basic fact that at the present time inflation is the foremost economic problem of the country as a whole and that there is no realistic alternative to bringing it under control. Although I have explained on a number of occasions the reasons why I hold the view that inflation is unacceptable, it may be worth repeating them here in some detail.

The overriding consideration is of course that failure to control inflation could eventually lead to a serious recession and disruption of the economy. Maladjustments and distortions accumulate during a period of inflation which, if neglected, would ultimately produce a severe adjustment from which all would suffer. If, moreover, it ever became clear that inflation would not be controlled by official policies, or even if there were serious doubts about the will of the authorities on this matter, there would be a great multiplication of efforts to protect against inflation, including demands for larger and more frequent income adjustments. The wage and salary settlements in recent years at levels far in excess of the long-term trend of productivity increase must reflect in large part an attempt to compensate for inflation which has occurred and to protect against further inflation which is anticipated. This process could become cumulative and result in severely restrictive policies being needed just to keep the price rise from accelerating.

A second reason is that we simply cannot ignore the inequities of inflation, its serious impact on the poor, the retired, and other elements in the community who because of their weak bargaining position are unable to keep up in the race with rising prices. Even those who manage to maintain their position fairly well on a current basis suffer greatly when the time comes to retire on fixed pensions. The life expectancy of a man retiring at sixty-five is just long enough for him to see the real value of his pension cut in half by an average price rise of 5 per cent a year.

Third, inflation militates against economic growth. It introduces an additional element of uncertainty about the future which diverts people's energies and skills away from constructive activities towards trying to out-guess the course of the inflation. It rewards economic initiatives on the basis of how well they happen to fit the progress of the inflation rather than on their economic contribution. Such temporary stimulating effects as inflation can have on the level of economic activity depend on it not being expected: if inflation is pushed to the point where it is generally expected and constant efforts are being made to adjust to it, then the stimulating effects are lost.

Fourth, inflation is extremely damaging to capital markets. The less confidence there is in the maintenance of the value of money, the more reluctant investors are to commit their funds for long periods of time. Economic growth cannot fail to be retarded if it becomes extremely difficult to borrow long-term funds for projects that take many years to yield their full return. It is true that some borrowers, notably business corporations, can continue to obtain a portion of the funds they require by giving up equity in some form or other, for example, through convertible debentures. But this is not possible for homeowners or for provincial or municipal governments borrowing to provide social capital, including funds for schools, universities and hospitals.

Finally, inflation can undermine our international competitive position. It is true that other countries are also having a difficult time in controlling inflation, but we should not assume that they will fail to do so. And if we could make some gains in our competitive position by doing somewhat better than others in controlling inflation, the long-term rewards in the form of increased output and employment and an improved trade balance would be tangible and worthwhile.

For all of these reasons, it is really not open to us to abandon the effort to deal with inflation. The special characteristics of the Canadian economy do, however, require that we should constantly be seeking, in ways that include co-operative action between different levels of government, to make the impact of our policies as equitable and selective as we can. They also reinforce the general point I have made on a number of occasions that the over-all policies of fiscal and monetary restraint should, to the maximum extent possible, be supplemented by voluntary restraint in order to shorten the duration of such policies and thus minimize their temporary unwelcome side effects. Everyone would derive benefits from a concerted effort to break into the interrelated cost-price push of recent years. I strongly support the efforts of the Prices and Incomes Commission to achieve this objective.

MONETARY POLICY

Since the autumn of 1968, when it became clear that the anticipated moderation of inflationary pressures was not occurring, monetary policy has again been directed towards restraint. The tightening of credit conditions has involved both higher costs for money and the restriction of credit availability.

The trend of interest rates in Canada in 1969 was greatly influenced by movements of rates abroad, and particularly by the direct and indirect effects of the extraordinary increases which occurred in the Euro-dollar market. The magnitude of these increases is illustrated in the next section of this Report. The Euro-dollar market is a very large international money market, and the very high rates paid in it exerted a powerful pull on funds and put strong upward pressure on short-term interest rates in all countries.

As interest rates rose in the first half of 1969 our Bank Rate was increased three times—from 6½ per cent to 7 per cent at the end of February, to 7½ per cent in June and to 8 per cent in July, where it has since remained. Commercial paper rates reached a peak of about 9½ per cent towards the end of the year; the average yield on long-term Government of Canada bonds reached a level of 8⅜ per cent; the prime conventional residential mortgage rate was about 10½ per cent. There was a moderate decline in security yields early in 1970, reflecting in part a larger downward movement in the United States and some relaxation in the Euro-dollar market.

The general restriction of the availability of credit lagged somewhat behind the increase in its cost, except in the case of new bond issues in Canada. A substantial decline in the amount of new money raised in Canada through the issue of long-term bonds took place in 1968 and there was a further decline in 1969. Part of this decline in domestic bond issues was offset by increased borrowing in foreign markets. In the mortgage market, the flow of funds was relatively well maintained until the second half of 1969. Bank loans continued to rise rapidly through the first part of 1969 but since the beginning of the summer the banks have felt the need to ration loans severely.

The restrictive monetary policy was slow in having a substantial impact on the availability of bank credit because at the beginning of the present period of severe restraint the banks were quite liquid and because under the pressure of the heavy loan demand which developed they turned out to be willing to see their liquidity run down to considerably lower levels than they had in the past. By April 1969 the combination of the restrictive policy of the central bank and the continued rapid expansion of bank loans had reduced the banks' ratio of more liquid assets to total assets below 29 per cent, a new low up to that time. On April 11 the Bank of Canada announced that it was raising the minimum secondary reserve ratio requirement from 7 per cent of deposit liabilities to 8 per cent, an action which had the effect of impounding about $250 million of the banks' liquid assets, thus making them unavailable to finance further loan expansion.

The Bank of Canada has continued to keep the cash and liquid positions of the banks under pressure in order to maintain tightness in the credit system. Between April 1969 and February 1970, the banks' more liquid assets were reduced substantially and the ratio to their total assets has moved down to around 25 per cent.

The effects of monetary policy on the banking system in 1969 show up clearly in the broad aggregates. A definite slowing in the rate of increase in bank loans occurred in May and June, and in the second half of 1969 the annual rate of increase in the aggregate of business and consumer loans was less than 4 per cent. Despite some upward movement in November and December, the total Canadian dollar assets of the banks grew at an annual rate of only 2 per cent in the second half of 1969—5 per cent for the whole of the year. The privately held money supply as broadly defined (i.e. the total amount of currency outside banks and Canadian dollar bank deposits held by the general public) rose by less than 4 per cent in 1969; the increase in money holdings would be somewhat greater if account were taken of the large rise in foreign currency deposits at the chartered banks.

The availability of credit through the banking system in 1969 was affected by the Bank of Canada not only through cash reserve management and the increase in the secondary reserve requirement but also by the Bank's request to the larger chartered banks that they compete less aggressively for large blocks of Canadian dollar short-term deposits. Large investors wishing to stay liquid look for temporary employment for their funds in bank deposits, short-term government securities, commercial and finance company paper and short-term claims on other financial institutions. In many cases the funds are in effect put up for auction, and the competition for them tends to be very intense as the major banks are very reluctant to lose accounts of large, established customers. In our system this has in some circumstances led to an undue escalation of interest rates paid on short-term deposit instruments, which in turn has tended to pull up the whole structure of rates.

In response to requests of the Bank of Canada, the larger banks have limited the rates paid on their short-term Canadian dollar certificates of deposit. Since last July the maximum rate has been 7½ per cent. As a result in part of the restraint exercised by the banks, their deposits in this category have declined considerably. It also seems likely that the rise in the short-term interest rate structure has been in some degree limited. The Bank of Canada is well aware of the problems involved in using moral suasion to influence the rates of interest paid by banks, since this affects the distribution of savings between various financial institutions and various types of instrument. However, the experience of recent years suggests that there are circumstances in which some such action is necessary. I wish to acknowledge that the co-operation of the banks in this matter has been of considerable help in the implementation of monetary policy.

The decline in the short-term certificates of deposit just referrcd to was to some extent offset by a very rapid increase in foreign currency "swapped" deposits* with the chartered banks. The rates of interest available on such deposits were influenced by the upward spiral of short-term rates in the Euro-dollar market. In the middle of July, when the Bank Rate was raised to 8 per cent, the Bank of Canada requested the chartered banks to accept a temporary ceiling on "swapped" deposits. The purpose of this action was to limit the impact on the Canadian market of the extraordinarily high rates prevailing in the Euro-dollar market. In January 1970 the Bank asked a number of other financial institutions not to frustrate the effect of the ceiling on "swapped" deposits by arranging similar transactions in other ways.

The Bank of Canada has requested the co-operation of the chartered banks on a number of other matters. In order to soften the impact of tight credit conditions on less prosperous areas of the country, the Bank of Canada has asked them to have special regard for borrowers in those areas. The Bank has also asked the banks to pay particular attention to loan applications from small businesses throughout the country since, unlike large corporations, they do not normally have alternative sources of credit. The Bank has also expressed the view that the chartered banks should maintain a reasonable continuity of lending on housing mortgages. Finally, in view of the higher bank loan rates now prevailing in the United States, which give United States corporations an incentive to borrow here directly or through Canadian subsidiaries, chartered banks were asked to give priority in the use of their total loan resources to the credit-worthy demands of their Canadian customers.

INTERNATIONAL FINANCIAL DEVELOPMENTS

The past year has witnessed a number of remarkable developments in the international financial system. The one on which I shall comment first is the very sharp increase in interest rates in the Euro-dollar market. Others reflected encouraging progress in dealing with some of the problems that have beset the system in recent years.

Interest rates on term deposits in the Euro-dollar market rose from a level of a little above 7 per cent at the beginning of the year to a peak of over 12 per cent in June, and they averaged well above 10 per cent for the rest of the year. They dropped below 9½ per cent in the early months of 1970.

Although many factors affected the level of Euro-dollar rates in 1969, the principal one was massive borrowing in that market by the foreign branches of

* Funds converted into a foreign currency, usually U.S. dollars, which have been placed on term deposits with a bank and which the bank has undertaken through a forward contract to convert back into Canadian dollars at maturity.

United States banks on behalf of their head offices. This borrowing was induced by a tightening of monetary conditions in the United States, and the nature of United States banking arrangements was such that the borrowing continued even after Euro-dollar rates rose far above United States rates, thus producing an escalated upward movement in Euro-dollar rates. In the countries most exposed to the influence of Euro-dollar rates a rising trend in interest rates was in general appropriate to their domestic economic situations, but the rapidity and extent of the Euro-dollar increases was so great that many countries took special measures aimed at limiting the pull of the Euro-dollar market and moderating the impact on their rates of the high Euro-dollar rates. As already indicated, the Bank of Canada in July 1969 obtained the co-operation of the chartered banks in limiting outflows through "swapped" deposits.

Turning to the international exchange rate situation, one outstanding problem that was resolved was that of the foreign exchange value of the German mark. On September 29, 1969 the German authorities announced that they would no longer maintain the declared par value of the mark and, after allowing its exchange value to float for four weeks, they declared a new par value at a level approximately 9 per cent higher than the old parity.

A widespread opinion that the German mark would sooner or later be appreciated had been evident for at least a year before it happened. Among the factors which contributed to this view were the persistent strength in the current account of the German balance of international payments and indications that Germany would experience growing inflationary pressures if it did not revalue. Expectations regarding revaluation erupted in massive purchases of marks in November 1968 and in May and September 1969; and on each occasion great strains were placed on the payments positions of a number of other countries. It is estimated that the cumulative net inflow into Germany in anticipation of revaluation had reached the extraordinary level of some U.S. $5 billion at the end of September 1969. It now seems that the greater part of this vast inflow had been reversed by the end of the year. The return flow strengthened the foreign exchange positions of many countries, particularly the United States.

One benefit to the world of the period of substantial German payment surpluses was the emergence in Germany of a large international market for long-term capital. Since the revaluation the availability of new long-term German capital to foreign borrowers has been sharply reduced. In the longer run it will be helpful to other countries if Germany achieves a payments equilibrium which is consistent with being a substantial exporter of capital.

The foreign exchange value of the French franc gave rise to considerable uneasiness after the events of May and June 1968 had weakened the international payments position of France. There were widespread expectations that a depreciation of the French franc would accompany an eventual appreciation of the German mark, and in these circumstances each surge of buying of marks gave rise to some selling of francs. The French authorities announced a reduction in the par value of the franc by approximately 11 per cent effective August 10, and followed this with a programme of fiscal and monetary measures designed to restore both internal and external equilibrium. Thereafter, and particularly since the revaluation of the German mark, France experienced a substantial return flow of funds and the franc has strengthened in foreign exchange markets.

The payments position of Britain continued to be a source of concern in the first part of 1969, as it had been for a number of years, and each outbreak of speculation on the German mark and the French franc put pressure on sterling. By late summer, however, it became evident that a significant improvement in Britain's payments position was under way, and subsequent developments have confirmed that trend. In the second half of 1969 Britain had a substantial overall surplus in its balance of payments, sterling strengthened on the exchanges, and the British authorities were able to make substantial repayments of the large short-term debt that they had incurred in recent years.

The long international discussions of plans to protect the world against a future shortage of international liquidity were brought to a successful conclusion in 1969. Members of the International Monetary Fund agreed to empower the Fund to create Special Drawing Rights, and approved the recommendation of the Fund's Managing Director to create and distribute 3.5 billion SDRs (having a value of U.S. $3.5 billion) on January 1, 1970 and a further 3 billion in 1971 and in 1972. In the perspective of history, I have little doubt that the decision to create SDRs will be regarded as the outstanding event of 1969 in the monetary field. In previous Reports I have expressed my strong support for the SDR plan, and I regard the first creation of SDRs as a great forward step in the evolution of the international monetary system.

The regular quinquennial review of the size of member countries' quotas provided for in the Articles of Agreement of the International Monetary Fund was successfully concluded late in 1969. It recommended an average increase in quotas of about one-third, and this recommendation has been approved. There is considerable variation around the average to take account of the different rates of growth of member countries since the last revision. The increases will become effective late in 1970 for Fund members who agree to them. The increase approved for Canada is from U.S. $740 million to U.S. $1,100 million, an increase somewhat greater than the average. The increase in quotas will enable the Fund to meet the growing needs of an expanding world economy for conditional credit. The increase in the Canadian quota will allow us to provide more balance of payments assistance to other countries through the Fund when our payments position is strong, and to receive more assistance from others should we have need of it.

One indication that confidence in the structure of foreign exchange rates had been restored by the end of 1969 was the decline in the price of gold in the private market. For most of the time from the establishment of the two-tier market for gold in March 1968 until late in 1969 the price of gold in the private market was above U.S. $40 per ounce. After rising to a peak of close to $44 in March 1969, it fell rapidly from $40 late in October 1969 to touch $35 early in December and has since fluctuated in a narrow range around $35. At the end of December the International Monetary Fund announced that agreement had been reached providing for the purchase under certain conditions of newly-mined gold from South Africa at $35 per ounce. This terminated a long period of uncertainty, and the Fund has since bought South African gold. The current tendency of the world's stocks of monetary gold to rise is in sharp contrast to the heavy outflows from those stocks in the period preceding the introduction of the two-tier gold market.

The experience of recent years has given rise to frequent suggestions that the world economy could be strengthened by altering the Fund's arrangements for determining countries' exchange rates in a way that would encourage more flexibility in rates, and a number of means of doing this have been proposed. The Fund is now engaged in a thorough study of these proposals and a report on its conclusions is expected this year. I have noted with interest an increasing awareness that a good deal of the rigidity in exchange rates that has attracted critical comment is not due to the nature of the Fund system or to Fund policy, but to the reluctance of governments to change their parities. One consequence of the recognition of this fact is an increasing tendency to focus on the question of national policies, a tendency which I welcome for I believe that it is primarily to better national policies rather than to changes in the exchange rate system that we must look to achieve and maintain a satisfactory operation of the international financial system.

I record with pleasure that on January 2, 1970, the Bank of Canada became a member of the Bank for International Settlements by subscribing to shares of BIS capital stock. Meetings of the BIS bring together regularly senior officers of most of the world's larger central banks, and have made the BIS an important centre for international monetary collaboration. The Bank of Canada has frequently taken advantage in recent years of a standing invitation from the BIS that we be represented at its meetings, and we have found both these contacts and our operating relationships with the BIS to be very helpful. Bank of Canada membership in the BIS will thus confirm and continue a valuable external association.

The International Environment

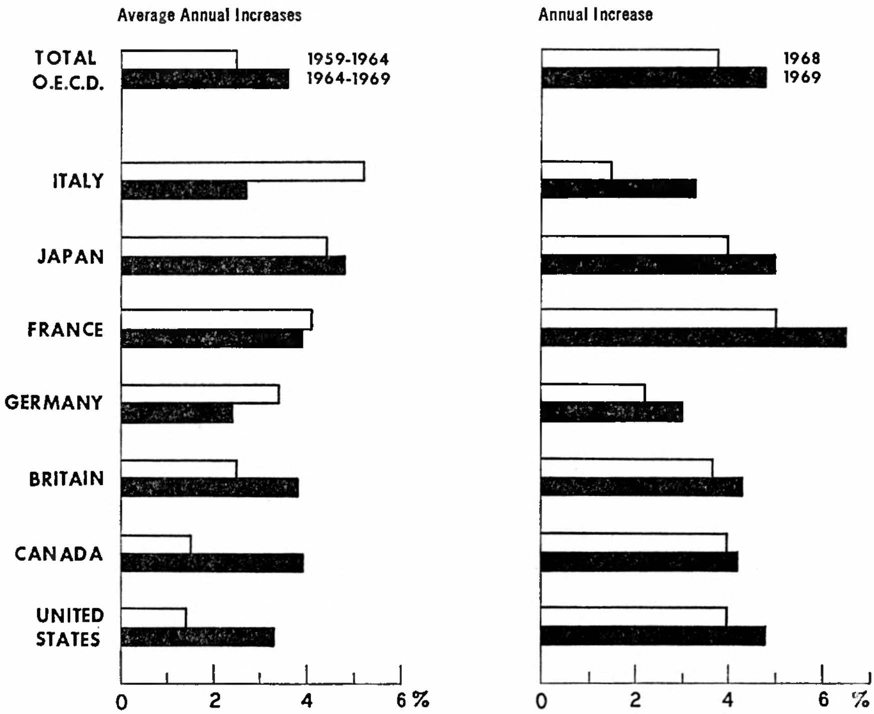
ECONOMIC AND FINANCIAL DEVELOPMENTS

Despite the slowing of economic expansion in the United States, the rate of growth in world output was well maintained in 1969; production in the industrial countries rose by approximately 5 per cent, slightly less than in 1968 but about in line with the average for the past ten years. Measures to restrain demand resulted in a very moderate rate of expansion in Britain and in a progressive slowing of the growth of the United States economy. In the latter country the increase in real output, which had been as much as 6½ per cent annually during the first half of 1968, dropped to only 2¼ per cent annually in the first half of 1969 and came to a halt in the final quarter. Nevertheless, the labour market in the United States remained tight. For the year as a whole the unemployment rate averaged 3½ per cent, as low as in 1968 and lower than at any other time since the Korean War. Late in the year, however, it was tending to move up and was at a seasonally adjusted rate of 3.9 per cent in January 1970. There were substantial increases in output in Japan, Germany and most continental European countries and the pace of activity brought increasing pressure on plant capacity and labour markets. Expenditures on plant and equipment continued to rise strongly in practically all industrial countries, reflecting both the very high levels of demand and the incentive to offset rising labour costs by more capital-intensive methods of production.

Wage rates rose sharply in most countries. In North America continued large increases in wages and salaries together with slower growth in output resulted in an acceleration in the rise in unit labour costs and a squeeze on profits. In continental Europe, wage settlements have been larger than in North America; particularly dramatic increases occurred in France in 1968, in Germany during 1969 and in Italy in recent months. Even though the growth in productivity has continued, unit labour costs have risen appreciably in most European countries. Recently there also has been some tendency for unit labour costs to rise in Japan. Widespread increases in industrial material prices in 1969 added to the rise in costs.

In virtually all of the industrial countries year-to-year price increases were larger in 1969 than in 1968. In the United States the GNP price deflator rose by 4¾ per cent in 1969, compared with 4 per cent in 1968, and at year-end the

GROSS NATIONAL PRODUCT PRICE DEFLATOR



Consumer Price Indcx was 6 per cent higher than a year earlier as against a rise of 4¾ per cent during 1968. For all the industrial countries combined, the OECD estimates that the increase in the GNP price deflator was 4¾ per cent compared with less than 4 per cent in 1968. This was a continuation of the deterioration in price performance of this group of countries from an average increase of 2½ per cent per year over the first half of the 1960's to an average increase of 3½ per cent per year over the past five years. The acceleration between these two periods has been most noticeable in Canada and the United States, the countries which enjoyed the best price performance in the first half of the decade.

Inflation has thus become more generalized and serious than at any time since the early 1950's, and in most of the industrial countries high priority is now being given to anti-inflationary policies. In the United States, fiscal and monetary policy has been used vigorously to restrain demand. As a result of the tax increase in mid-1968 and a limitation on both military and civil expenditures the federal budget swung from a deficit of $25 billion in the fiscal year ending mid-1968 to a surplus of $3 billion in fiscal 1969. A smaller surplus is officially projected in the current fiscal year.* Monetary policy applied increasing constraint on the reserve position of the commercial banks during the first half of 1969 and this pressure was maintained throughout the second half; the growth in loans and investments of commercial banks was held to 2½ per cent during 1969, compared with 11 per cent during the previous year. Credit conditions tightened generally in the course of the year and interest rates rose. The yield on three-month Treasury bills exceeded 8 per cent at year-end, almost two full percentage points above a year earlier, while the yield on new issues of long-term high-grade corporate bonds exceeded 8½ per cent compared with 7 per cent at the beginning of the year. Interest rates moved down in the first months of 1970.

In Britain restrictive policies have been followed for several years to contain inflationary demands and to strengthen the balance of payments position. The deterioration in the French balance of payments and the severe inflationary pressure which followed the events of May and June 1968 led the authorities to take a number of measures, including the devaluation of the franc in August 1969, to restore both internal and external equilibrium. In Germany strong inflationary pressures emerged earlier in the year, and the authorities now look to the revaluation of the mark and measures of domestic financial restraint to restore internal balance in the economy. Concern about signs of an over-heating of the Japanese economy was expressed by the authorities last September when the Bank Rate was increased.

BALANCE OF PAYMENTS DEVELOPMENTS**

The widespread strength of demand was reflected in a growth in the volume of world trade close to the record 12 per cent increase achieved in 1968. In value terms the increase was higher in 1969 as export prices rose between 2 per cent and 3 per cent on average compared with a 1 per cent decline in the previous year. World prices of basic commodities in particular rose sharply. The increase was most pronounced in metals but prices of a wide range of industrial materials and many foodstuffs were higher, though wheat was a notable exception.

While current account imbalances remained large some progress towards achieving more viable positions was discernible by year-end. In the United States, the current account including unilateral transfers was in deficit during the first half of the year, but a recovery in the merchandise trade surplus during the second half of the year brought the current account back to about a balanced position. This improvement still leaves the United States balance well short of the current account surplus of over $3½ billion achieved, on average, in the

* The surtax on corporate and personal tax liabilities which was scheduled to expire at the end of 1969 was extended to the end of June 1970 at half the original 10 per cent rate.

** All values in this section are expressed in U.S. dollars.

years 1964-67. Britain has been in a position to take advantage of buoyant world demand and its current account surplus in the second half of 1969 appears to have been running at a rate consistent with the longer-term objective of $1.2 billion per year. Although the French deficit on current account in 1969, at more than $1 billion, was considerably larger than in 1968 there were signs at year-end that the trade deficit was contracting. In the second half of 1969 the German current account surplus ran at an annual rate of almost $2½ billion, nearly as large as in 1968, though it is expected to decline as the impact of revaluation is felt. The Italian surplus for the whole of 1969 does not appear to have fallen much from the level of more than $2½ billion in 1968, but the trend at year-end was obscured by widespread work stoppages. The Japanese surplus more than doubled to over $2 billion in 1969 as the exceptionally rapid growth in that country's exports continued.

During the course of 1969 there were extraordinarily large flows of short-term capital which at times placed severe pressure on the international payments system. The Euro-dollar market was the principal channel for these flows, and heavy demands for funds caused rates to rise dramatically in the first half of the year and to remain very high throughout the rest of the year. During the first half of the year, United States banks drew more than $6 billion from the Euro-dollar market through their foreign branches in order to offset the loss of term deposits associated with the Regulation Q ceiling on domestic deposit rates.* At the end of June the United States monetary authorities proposed that reserve requirements should be imposed on increases in United States banks' liabilities to foreign branches** and only limited net use was made of this market during the rest of the year. During the latter months of the year there was some recourse by United States banks to direct borrowing from official holders abroad rather than through the Euro-dollar market.

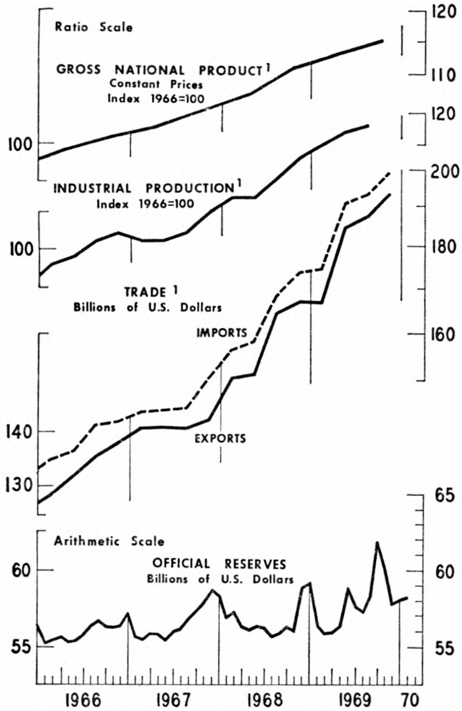
Sporadic demands for short-term funds were associated with speculation that Germany would revalue the mark. Expectations of an imminent change in the exchange rate of the mark led to a surge of about $4 billion into Germany in late April and early May, drawing funds from many countries including France, where there was speculation that the French franc would be devalued. The authorities succeeded in dispelling expectations of an immediate change in exchange rates and some reversal of the flow to Germany took place in late May and June. In the uneasy calm that prevailed during the summer months the French franc was devalued by 11.1 per cent in mid-August. The approach of the German election in late September brought on a renewed wave of speculation that the mark would be revalued causing a further flow of some $2 billion into

* Early in 1970 there was an upward adjustment of maximum interest rates under Regulation Q on time and savings deposits. The top rate for single maturity time deposits of $100,000 or more was raised to 7½ per cent for maturities of one year or more, from the previous maximum of 6¼ per cent.

** Under a regulation announced in August a 10 per cent reserve requirement was imposed, beginning October 16, on borrowings by member banks from their foreign branches in excess of the average amount outstanding during the four-week period ending May 28, 1969.

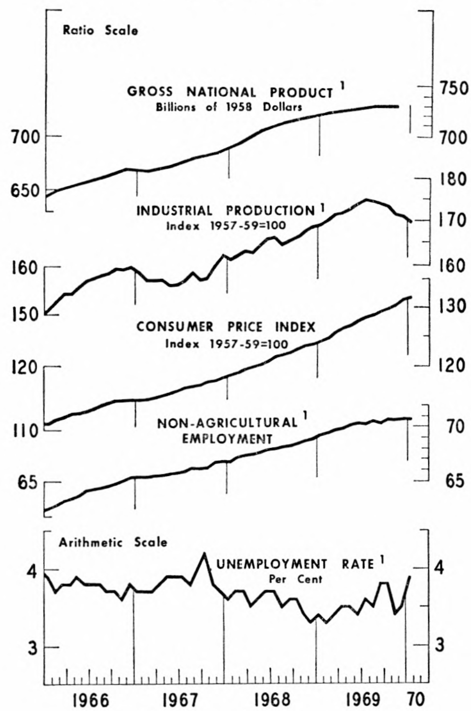
ECONOMIC INDICATORS

ALL O.E.C.D. COUNTRIES



1. Seasonally adjusted: Trade at annual rates.

UNITED STATES



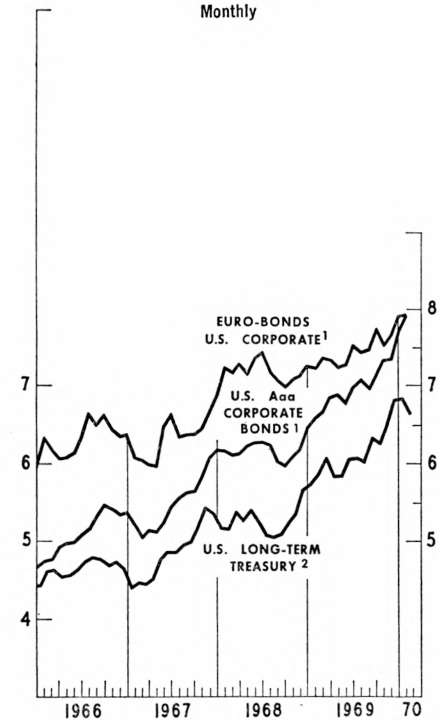
1. Seasonally adjusted: GNP at annual rates.

INTEREST RATES

Per Cent

LONG-TERM

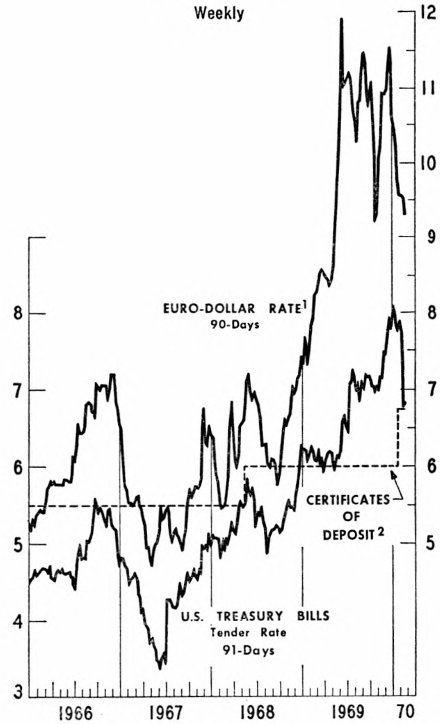
Monthly



1. Month-end.
2. Average of daily figures.

SHORT-TERM

Weekly



1. Average of daily figures.
2. Ceiling rate on 90-179 days deposits under Regulation Q.

Germany. The German authorities closed the exchange market, allowed the mark to float upwards for four weeks, and at the end of October established a new official parity 9.3 per cent higher than the previous one. This was followed by a very large reflux of funds from Germany, much of it apparently going to the United States.

The strains on the payments positions of individual countries caused by the speculative flows of funds were eased to some extent by the use of both new and existing credit facilities between official institutions. Among the facilities already in position were four central bank networks in which Canada is a participant, namely, one in favour of the Bank of England set up at the time of the devaluation of sterling in November 1967, a second in favour of the Bank of England set up in September 1968 in connection with an arrangement to discourage the conversion into other currencies of sterling held by countries of the sterling area, one in favour of the Bank of France set up in November 1968, and the very large structure of reciprocal facilities between the Federal Reserve System and a number of other central banks. The network in favour of the Bank of France, in which Canada's share was $100 million, was terminated in the course of 1969. Canada's share in the other facilities remained unchanged during the year at $100 million in each of the networks in favour of the Bank of England and $1,000 million in the reciprocal network of the Federal Reserve System.

In 1969, as in 1968, there was again a substantial volume of foreign long-term borrowing in the main European markets, particularly in Germany. The total of new Euro-bond issues was above the $3 billion level or only a little below the 1968 total, despite a decline in issues by United States companies from $2 billion to $1 billion. There was also a large volume of foreign issues denominated in German marks placed directly in the German market, including new issues by Canadian borrowers equivalent to more than $400 million. In total, thc German capital market provided about $5 billion of long-term capital to foreigners in 1969, about twice as much as in 1968.

There were major changes from 1968 to 1969 in the capital account of the United States balance of payments. The large inflow of funds associated with substantial non-resident purchases of American equities and other non-government securities fell off sharply after the first quarter of 1969, and the net inflow from foreign official purchases of special United States Treasury certificates, which had been large in 1968, did not continue in 1969. At the same time there appears to have been an increase in the outflow of private long-term capital, presumably reflecting in part the liberalization of balance of payments guidelines in 1969. There was also a large outflow under the "errors and omissions" item in the first three quarters, most of which probably reflected a flow of United States funds to the Euro-dollar market. These developments contributed to the swing in the liquidity balance from a position of approximate balance in 1968 to a substantial deficit in 1969. The large inflow of funds through banking channels, noted earlier, did not reduce the liquidity deficit because the resulting indebtedness is recorded as a liquid liability to non-residents. On an official settlements basis, which indicates more accurately the position of the U.S. dollar in exchange markets, there was a surplus of about \$2¾ billion, composed of a decline in liabilities to foreign official institutions of about \$1.5 billion and an increase in official reserve assets of \$1.3 billion.

The strengthening of Britain's current account position in 1969 and an inflow of capital has permitted that country to commence repayment of drawings on international credit facilities and to add to its reserves. During the past year Japan has been shifting the financing of its trade from foreign to domestic sources and the resulting net outflow of capital has helped to offset a part of its large current account surplus, but there was also an increase of more than \$0.7 billion in its reserves. Italy's large current account surplus was exceeded by even larger net capital exports and its reserves show a decline of \$0.4 billion. In the first nine months of 1969 Germany's net export of long-term capital substantially exceeded its current account surplus but speculative inflows were sufficient to increase German official reserves by more than \$2 billion. In the last three months of the year the return flow of speculative funds contributed to a decline in German reserves of about \$5 billion.

Economic Developments in Canada

GENERAL REVIEW

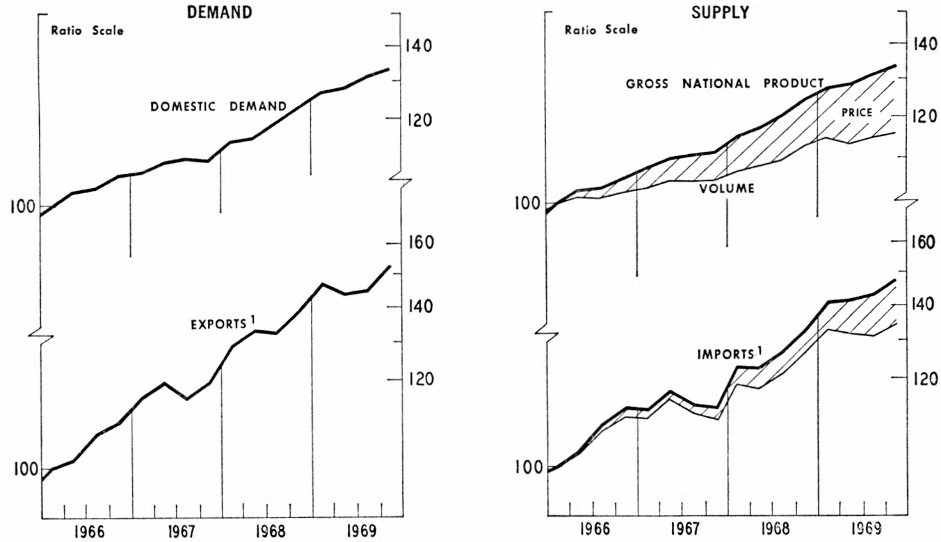
The course of economic activity in Canada in 1969 was badly distorted by strikes. However, it appears that following a vigorous expansion from late 1967 through the first quarter of 1969, the underlying trend of demand grew at an appreciably slower pace. Exports, which had been one of the most dynamic elements of total demand in the period of rapid growth, provided considerably less stimulus after the first quarter. This reflected some major strikes which disrupted trade from the second quarter until late in the year, the slowing of the expansion of the United States economy during 1969 and the weakness of the world wheat market.

The less rapid rise in exports was accompanied by a moderation in the growth of domestic demand in response to tightening fiscal and monetary restraints. Consumer spending on durable goods rose more slowly as the market for new cars weakened, initially in the spring but more markedly towards year-end. Outlays on residential construction, which had been rising very rapidly, levelled off about mid-year. Business investment in inventories was at a much lower rate after the first quarter. On the other hand, business investment in plant and equipment continued to rise moderately and a much larger increase would have occurred had it not been for major strikes in the construction industry. There was also an appreciable rise in government expenditure on goods and services in 1969 in response to rising costs, notably a substantial increase in the wage and salary bill of the public sector.

In the aggregate, and after allowance for strike distortions, the growth of demand in money terms since the first quarter of 1969 seems to have been at an annual rate of about 7½ per cent, compared with more than 10 per cent during the preceding six quarters. Since the prices of goods and services rose more rapidly in the recent period, the deceleration in terms of volume was even more pronounced. Imports also grew more slowly after the first quarter of 1969; indeed, over the balance of the year there was scarcely any increase in volume.

MAJOR ECONOMIC AGGREGATES

Quarterly — Index 1Q 1966=100



Seasonally adjusted.
1. Goods and services.

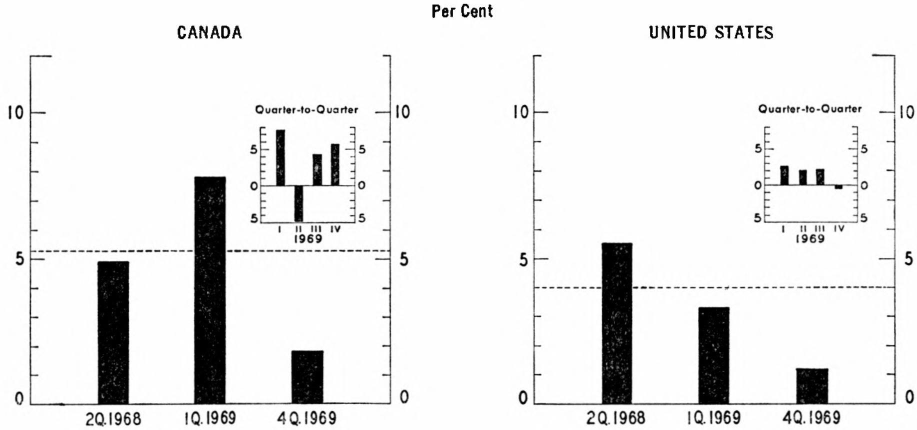
OUTPUT. The expansion in the volume of output decelerated somewhat later in Canada than in the United States and, while the slowing here was more abrupt, the economy was still registering more growth at year-end. Canadian output was severely affected by a series of major labour disputes beginning in the second quarter and continuing with varying impact until late in the year. These occurred first in the construction and iron ore industries, then in steel and nickel. For 1969 as a whole, 7¾ million man-days were lost as a result of strikes, 50 per cent more than in either 1968 or 1966, both of which were also affected by strikes to an exceptional degree. Though the level of activity was still influenced to some extent by strikes well into the fourth quarter, their impact had been considerably reduced, contributing to a strong rebound in output at year-end. In the United States, on the other hand, a major strike in the electrical industry had a weakening effect on total output in the fourth quarter.

Perhaps the most meaningful way of assessing recent trends is to compare the growth between the first and fourth quarters of 1969 with the two earlier three-quarter periods. In Canada, real output grew during the recent period at an annual rate of less than 2 per cent compared with an average annual rate of 6½ per cent during the preceding year and a half. The comparable annual rates of growth in the United States were 1¼ per cent and 4½ per cent.

VOLUME OF OUTPUT[1]

Average Annual Rates of Growth in Constant Dollar G.N.P.

3 Quarters Ending



Seasonally adjusted.

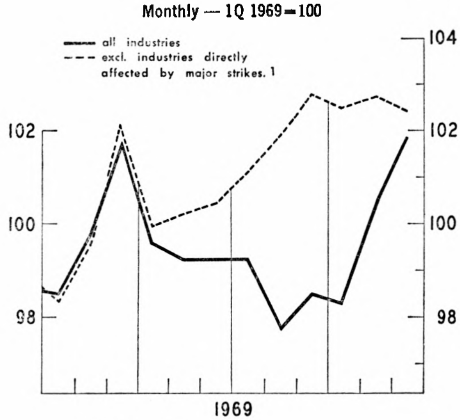
1. Broken horizontal lines represent potential rates of real growth : these are estimated for Canada by the Economic Council of Canada and for the United States by the Council of Economic Advisers.

Excluding industries affected by strikes, the rate of real growth in Canada in the last three quarters of 1969 seems to have been about 3 per cent per annum.

The impact of strikes in the industrial sector is illustrated in the accompanying chart. This suggests that the index of industrial production (which covers about one third of total output in the economy) would have followed a very different pattern if several industries had not been affected by prolonged work stoppages. Excluding strike-affected industries, industrial output rose moderately until the end of the third quarter, then levelled out. There was some decline in production of primary textiles and around the end of the year a marked reduction in automobile assemblies, reflecting weakening demand in North America. There was also a drop in lumber production from its high level in the early part of 1969, as house-building activity slowed in Canada and the United States.

INDEX OF INDUSTRIAL PRODUCTION

Monthly — 1Q 1969=100



Seasonally adjusted.

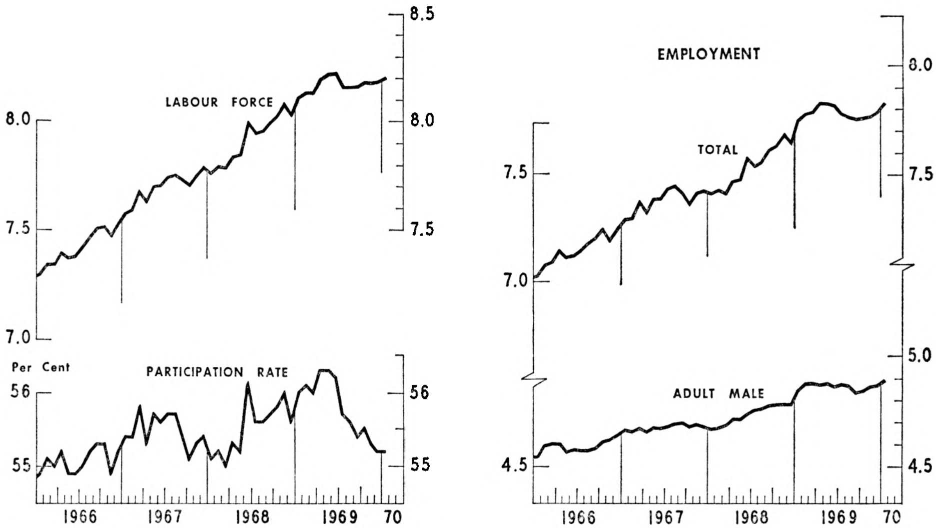
1. Industries excluded : iron mines, miscellaneous metal mines, iron and steel mills, and smelting and refining. These industries together account for about one-eighth of the total index.

Farm output appears to have increased at about the same rate as in the previous year. Although the adverse wheat marketing situation induced Prairie grain growers to cut back acreage sharply, unusually favourable growing conditions resulted in near-record yields and a large high-quality crop. This high production in the face of a major decline in exports of wheat and flour in 1969 led to the accumulation of very large stocks of grain both in commercial positions and on Prairie farms. Late in the year, the signing of new contracts with the Soviet Union and China helped to ease the marketing situation somewhat. The general weakness in the world wheat market was reflected in a sharp drop in prices in 1969, but in recent months they appear to have stabilized at a relatively low level.

EMPLOYMENT AND PRODUCTIVITY. According to labour force statistics, employment reacted very promptly to the trend of output. Indeed, total employment (seasonally adjusted) declined for several months after mid-year, though some pick up occurred again at year-end. There appears to have been an unusually large increase in students employed in the late spring followed by a reduction as the summer progressed. Another factor which probably influenced the trend of employment was the indirect effect of labour disputes even though striking workers themselves are counted as employed. Adult male employment

LABOUR FORCE AND EMPLOYMENT

Monthly — Millions



Seasonally adjusted: Adult male employment adjusted by Bank of Canada.

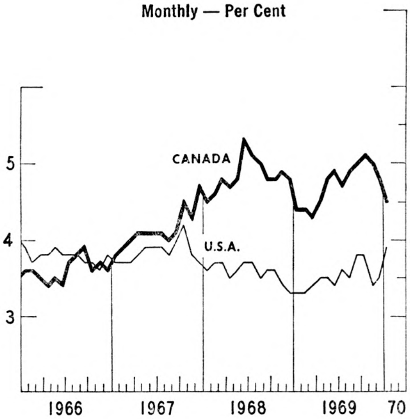
did not weaken as much as total employment last summer; indeed, it was virtually level after a sharp increase at the beginning of the year.

Labour force growth appears to have been responsive to changing employment opportunities to a remarkable degree during 1968 and 1969. The proportion of the population of working age participating in the labour force rose strongly through 1968 and early 1969 and declined sharply thereafter. As a result, the labour force increased by about 4¼ per cent between the first quarter of 1968 and the first quarter of 1969, but only at an annual rate of about one per cent between the first and fourth quarters of 1969. These rates compare with an underlying growth trend in the labour force of about 3 per cent per annum. While the main explanation for these variations over the past two years can be found in the labour force participation rates of married women, students and older workers, there was an unusual drop in 1969 in the participation rates of adult male workers, which can be explained only in part by increased enrolment in retraining programmes.

Owing to the sensitivity of labour force participation to changes in labour demand, the number of unemployed has fluctuated within a fairly narrow range during the past two years. On a seasonally adjusted basis, the unemployment rate exceeded 5 per cent of the labour force in the summer of 1968, fell below 4½ per cent in the first quarter of 1969, rose to about 5 per cent in the autumn, then declined again to 4½ per cent in January. Throughout this period, unemployment remained above the low point reached in 1966 when the average for the whole year was about 3½ per cent. This was in marked contrast to the situation in the United States where the unemployment rate over the past two years has generally remained exceptionally low.

UNEMPLOYMENT RATES

Monthly — Per Cent



Seasonally adjusted.

NON-FARM EMPLOYMENT

Paid Workers

Monthly — Millions

Seasonally adjusted : All Establishments Survey adjusted by Bank of Canada.

The above analysis of labour market developments has focussed exclusively on data provided by the labour force survey. It should be noted that alternative official measures of employment convey a somewhat different impression. Direct estimates, based on payroll information rather than the household sample survey, suggest that the growth of employment was better sustained throughout 1969. For this reason, and because of the disruptions caused by labour disputes, it is difficult to draw precise conclusions about the short-term trend of productivity. However, it does seem clear that, following exceptionally large productivity gains during the period of rapid growth, there has more recently been a marked deterioration in performance such as usually occurs when the pace of expansion slows down.

PRICES AND INCOMES. The gradual accumulation of some slack in the economy has so far led to few definite signs of easing in prices and money incomes though some lag was, of course, to be expected. While some tentative signs of moderation did appear during the summer, price increases were slightly larger over 1969 as a whole than during the previous year. This marked the fourth consecutive year of clearly excessive rates of price increase. As noted in the preceding part of this Report, there were greater inflationary pressures in the United States and other industrial countries in 1969 than there had been for many years. These external developments not only had important effects through such direct channels as export and import prices but also tended to reinforce and prolong inflationary expectations and behaviour in Canada.

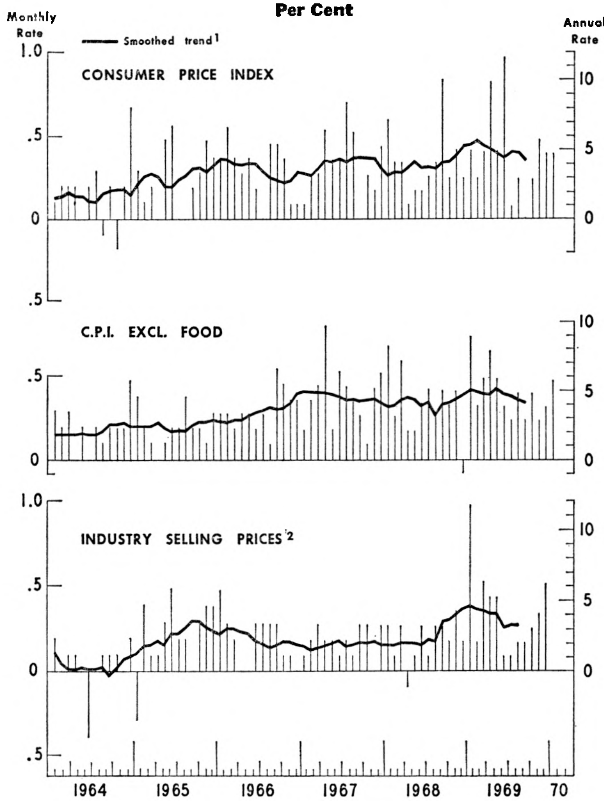
The Consumer Price Index in January 1970 was 4.6 per cent higher than a year earlier, compared with a 3.8 per cent increase during the preceding twelve-month period. Food prices rose by 4 per cent following an increase of 3 per cent the previous year. Excluding food, the index rose by 4.7 per cent, as against an increase of 4 per cent during the previous year. Prices of goods other than food increased at about the same rate in both years but shelter and service prices accelerated. Prices of durable goods increased somewhat faster than they did during 1968 but there was a slight moderation in the rise in prices of non-durable goods. Shelter costs advanced by about 7 per cent, somewhat more than in 1968: costs of home-ownership, including such items as mortgage interest rates, property taxes and insurance, again rose substantially, though there was a slightly smaller increase in rents. Prices of other consumer services also rose more than 7 per cent, representing a major acceleration from the previous year. Unusually large increases occurred in charges for local transportation and prepaid medical care. Given their labour-intensive character and the small scope for productivity improvement, the prices of services tend inevitably to reflect more directly than those of goods the continued rapid rise in wages and salaries. In addition, prices of many services are subject to regulation and are often adjusted to past cost increases only after appreciable time lags.

Many major components of the CPI moved up very sharply in the spring of 1969 when a rise in food prices, especially for beef, coincided with large increases in some service prices and higher sales or excise taxes on a number of other items in the index. After mid-year, food prices eased for several months and prices of other items appeared to be rising more moderately, but towards year-end the pace quickened again, notably in food and new car prices.

Because of so many irregularities, including the infrequency with which certain major service items are priced, it is difficult to identify changes in the underlying trend of prices. The accompanying chart attempts to do this by smoothing out the monthly changes in the CPI and in an aggregate index of industry selling prices, after adjusting for seasonal variation. All three measures show that price increases over the second half of 1969 were less than over the first half, though in the last two or three months there have been perceptibly

MONTHLY PRICE CHANGES

Per Cent



Seasonally adjusted by Bank of Canada.

1. 9-month centred moving average of month-to-month changes.
2. Unofficial gross-weighted aggregation of published selling price indexes for 99 manufacturing industries.

larger increases again, particularly at the earlier stages of the production process, as may be seen in the index of industry selling prices. Much of the easing in this measure during the summer was attributable to lumber prices, which fell back sharply from their exceptionally high level early in 1969. On the other hand, since the autumn there have been increases in prices of several important basic commodities, such as steel, nickel and newsprint, which are still working their way through to final product prices.

The most comprehensive measure of prices of domestically produced goods and services, the GNP deflator, showed a pronounced deceleration in the latter part of the year from its very high rate of increase in the second quarter. However, this measure is also extremely difficult to interpret on a short-run basis because of irregular influences and changes in weighting as expenditure patterns vary from quarter to quarter. From the fourth quarter of 1968 to the fourth quarter of 1969 the increase in the GNP index was 4½ per cent compared with a rise of less than 4 per cent the year before. The deflator for final domestic demand, which includes the cost of imported goods and excludes exports and inventories, increased slightly faster, by 4¾ per cent compared with about 4½ per cent during 1968. In addition to consumer purchases, such measures reflect prices of goods and services purchased by other sectors of the economy, some of which are very directly affected by wage costs and prices of imported goods. During 1969 there was a noticeable acceleration in the price components of business capital investment and government spending. The price of machinery and equipment, about half of which is imported, rose appreciably faster than in 1968. The more rapid increase in construction wages in 1969 contributed to an acceleration in the cost of both residential and non-residential construction, especially the latter. The cost of public works was similarly affected, but the major element in the 8½ per cent rise in the price of goods and services purchased by governments during 1969 was the large increase in rates of pay of employees in the public sector, which included at the federal level substantial retroactive salary payments.

In addition to being the broadest indicator of price movements in the economy, the GNP price index is equally a measure of the extent to which the increase in the total of money incomes and other costs accruing to factors of production exceeds the increase in total real output. The following table shows that, compared with the earlier period of relative price stability, the past several years have been marked by more rapid growth in labour costs per unit of output, accompanied by efforts on the part of business to restore profit margins when market conditions permitted, as in 1968.

The net contribution of the miscellaneous ("all other") income and cost components to the total price change has been relatively small except in 1966 when farm income increased quite sharply, primarily as a result of the record

AMOUNT CONTRIBUTED* TO PERCENTAGE INCREASE IN GNP PRICE INDEX BY DIFFERENT TYPES OF INCOME

Type of Income	Annual average		Second half to second half			
	1961-65	1965-69	1965-66	1966-67	1967-68	1968-69
Corporate business(1)	0.6	–	−0.8	–	1.0	−0.6
Uninc. business (non-farm)	–	–	−0.2	0.4	–	−0.2
Total business	0.6	–	−1.0	0.4	1.0	−0.8
Wages and salaries(2)	0.9	3.1	3.8	2.9	1.6	4.0
Indirect taxes(3)	0.6	0.6	0.3	0.7	0.7	0.8
All other GNP components	0.1	0.3	1.9	−0.7	0.3	0.5
GNP price index(4)	2.2	4.0	5.0	3.3	3.6	4.5

* The contributions are calculated by weighting changes in each category of income per unit of total output by its share of GNP in 1961. The weights used are: total business 21.1; wages and salaries 52.2; indirect taxes 12.5; and all other GNP components 14.2.

(1) Corporation profits before taxes and corporation capital cost allowances.

(2) Includes supplementary benefits and military pay.

(3) Less subsidies.

(4) The GNP "deflator" which measures prices of all goods and services produced.

wheat crop that year. The increases in indirect taxation which have accompanied the growth in the relative size of the government sector have made a significant contribution to the rise in prices, but this has been no greater in recent years than in the early 1960's. Business income per unit of output, particularly in the corporate sector, has been more volatile, and from time to time has contributed significantly to the over-all rise in income per unit of output, most recently in the period of economic expansion during 1968 and early 1969. In the course of 1969, however, a renewed squeeze on profit margins developed, as is also shown in the chart on page 34.

As business income accounts for only a fifth of GNP and as some of its components are relatively stable, the changes in the contributions of this factor in the foregoing table are mainly the result of quite large swings in corporate profits. Corporation profits before taxes (though after depreciation) rose by 21 per cent between the second halves of 1967 and 1968; they remained at a high level until the second half of 1969 when they fell sharply, in part as a result of the major strikes mentioned previously. In this period, profits averaged about 3 per cent lower than in the second half of 1968.

While there was some deceleration in the rise in total wages and salaries in the course of 1969 as employment grew more slowly, labour income in the second half of the year was still 12 per cent higher than in the corresponding period of 1968. Between the second halves of 1967 and 1968 when there was an unusually strong gain in productivity, labour income per unit of output had risen by 3 per cent, compared with an average annual increase of under 2 per cent in the 1961-65 period of relative price stability. Over the most recent year, with average pay increases remaining at least as large and with productivity deteriorating as the economic expansion slowed, there was a sharp acceleration in unit labour costs; they were 7½ per cent higher in the second half of 1969 than in the same period of 1968. Given the important share of GNP represented by wages and salaries—more than half—this sharp rise in unit labour costs meant that they accounted for more than four fifths of the increase in the total of all incomes per unit of output between the second half of 1968 and the second half of 1969, as may be seen in the table on page 32.

In the economy as a whole there appears to have been a slightly larger increase in average income per employee in 1969 than in 1968. Explicit information about average wages and salaries is only available for larger establishments. This covers some 50 per cent of the work force but excludes all public employees. For this important group, average pay increases during 1969 were no larger than in the two preceding years, but they remained very much greater than average increases during the early 1960's. The table below also shows that in contrast to this over-all pattern, there was a substantially larger increase in the average pay of construction employees last year.

AVERAGE WEEKLY WAGES AND SALARIES(1)

(percentage increases)

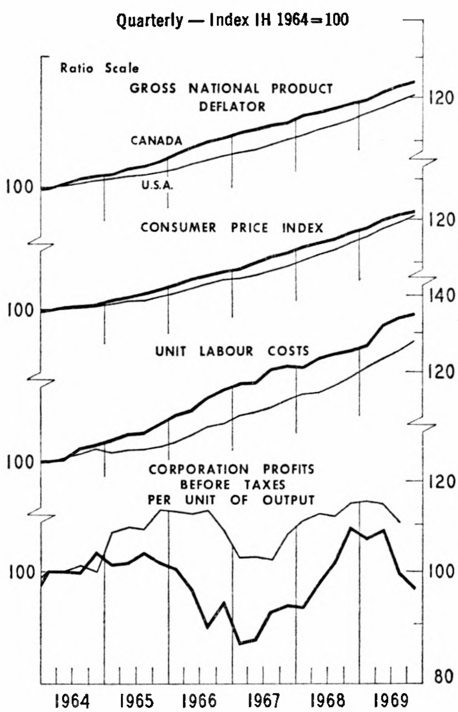
	Annual average		Second half to second half			
	1961-65	1965-69	1965-66	1966-67	1967-68	1968-69
Manufacturing	3.8	6.7	5.9	6.8	7.5	7.2
Mining	3.9	7.5	7.3	8.1	7.8	6.8
Forestry	5.2	8.4	9.0	8.3	7.3	9.6•
Construction	4.7	8.9	11.6	6.4	5.6	10.4
Transportation and utilities	4.4	7.6	3.6	10.9	8.5	8.9•
Trade	3.3	6.3	4.7	5.8	7.8	7.6
Finance insurance and real estate	4.9	6.5	4.8	6.4	8.5	5.7
Other commercial services	3.2	6.4	6.5	7.5	5.0	6.3
Total of above	3.8	6.7	5.7	7.0	7.2	7.1

•: Estimate.
(1) Based on payrolls of firms having 20 or more employees.

A more forward-looking, though less comprehensive, measure of the trend of wages and salaries is provided by the average increase in base rates under new collective bargaining agreements. While the weighted average of these annual increases (excluding construction) was 7.9 per cent in 1969, or about the same as in 1968, there was an accelerating trend after the first quarter. In the fourth quarter such settlements provided for increases averaging almost 9 per cent and included some major industrial settlements providing for average base-rate increases over the life of the agreements of 10 per cent to 11 per cent per year. There were also very large settlements involving construction workers in most sections of the country last year. As usual, many contracts signed in 1969 called for immediate increases which were somewhat greater than the average over the life of the contract.

PRICES AND COSTS

CANADA - U.S.A.



Seasonally adjusted : C.P.I. adjusted by Bank of Canada.

Canada's price performance over the past year has compared more favourably with the United States than in other recent years. The 4½ per cent increase in the GNP deflator in Canada over the year ending in the fourth quarter of 1969 compared with a rise of about 5 per cent in the comparable United States measure. Consumer prices also rose appreciably less during the year than they did in the United States. This resulted in part from a more rapid increase of food prices in the United States last year. Indeed, somewhat weaker prices in the farm sector in Canada are one of the more significant differences which emerge in a comparison of the prices and cost situation in the two countries. On the other hand, unit labour costs in both countries climbed faster during 1969 with the increase in Canada being at least as sharp as in the United States. The squeeze on profit margins in Canada appears to have been somewhat more severe, though again strike effects complicate the comparison.

REGIONAL DEVELOPMENTS

The easing of activity in the economy as a whole is reflected to some degree in all regions, though here too there are difficulties in allowing for the impact of strikes. Labour income increased at a somewhat slower pace during the latter part of the year everywhere except in British Columbia. Retail sales also rose at an above-average rate in British Columbia but their growth slowed from the high rate of 1968 in the Atlantic Provinces and Ontario, particularly in the former where a sharp decline occurred in the second quarter. In Quebec, retail trade continued to rise at much the same moderate pace as was experienced through most of 1968 following the immediate post-Expo set-back. It also continued to rise moderately in the Prairie Provinces despite a decline in Saskatchewan. The latter province felt the brunt of the continuing weakness in world wheat markets and the resulting sharp drop in farm income had a particularly depressing effect on sales of farm machinery. In addition, Saskatchewan has experienced difficulty in marketing its increased production of potash, even at much reduced prices. Manufacturers' shipments were off markedly in Ontario and British Columbia in the latter part of the year. Strikes were an important factor in Ontario but towards year-end, as output was recovering in the strike-affected industries, manufacturers' shipments were affected by production cut-backs in the automobile industry. In British Columbia, manufacturing was affected by declining lumber sales.

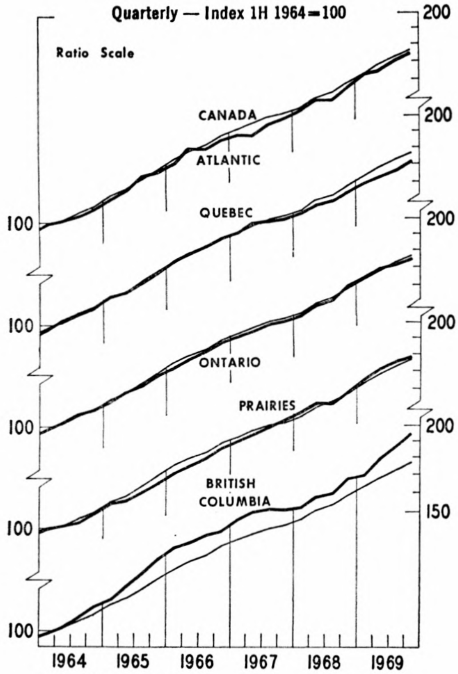
On a regional basis business investment apparently increased most in Ontario, the Atlantic region and British Columbia; in the Prairie region as a whole it remained at a high level, largely reflecting a strong gain in Alberta. In Ontario, business investment intentions for 1969 were up more than 20 per cent from actual 1968 outlays, but these plans were not fully realized. The main reason for the shortfall was a series of work stoppages in the construction industry during the summer; consequently it is likely that there has been an unexpectedly large carry over of uncompleted projects into the current year. Although investment intentions were up slightly in Quebec in 1969 it is not certain that the increase was achieved and investment per employee in that province remained relatively depressed. The achievement of a record level of housing starts nationally in 1969 was reflected in a high level of activity in all regions, though in Quebec and Ontario total starts per capita were lower than in 1968. The decline in starts which occurred in the latter part of the year was evident across the country.

The only region to experience a strong growth in employment in 1969 was British Columbia. In the Atlantic Provinces and Quebec the moderate growth in employment in 1969 represented a second year of relatively weak labour demand. In Ontario, and even more in the Prairie Provinces, the flat or downward trend of employment in 1969 was in sharp contrast to its rapid increase during 1968. The sensitivity of the growth of the labour force to the relative strength of labour demands was a feature common to all regions.

While the annual average rate of unemployment nationally was little changed between 1968 and 1969, there were significant differences in the pattern among the individual provinces. As may be seen in the table on page 38, unemployment in the Atlantic Provinces was generally higher in 1969, except in Nova Scotia, while it was lower in Ontario and all Western Provinces except

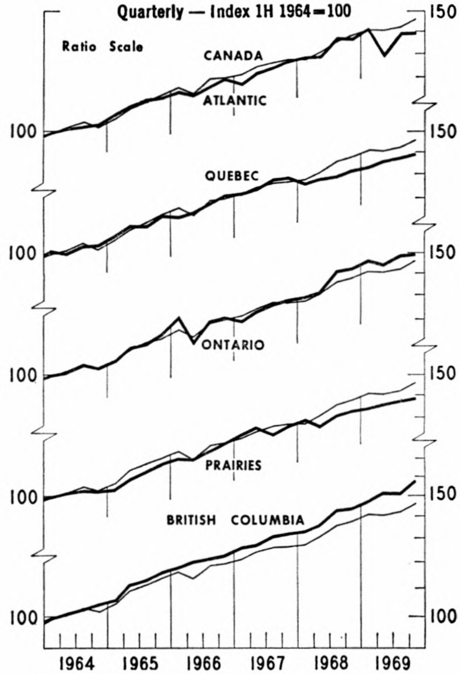
REGIONAL ECONOMIC INDICATORS

TOTAL WAGES AND SALARIES



Seasonally adjusted.

RETAIL SALES

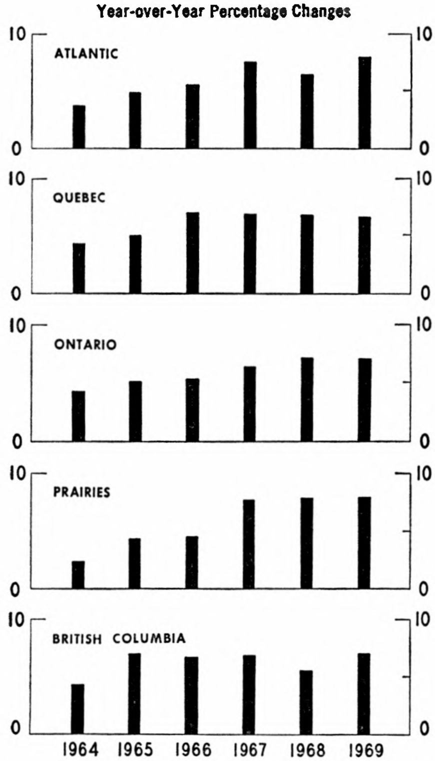


Seasonally adjusted.

AVERAGE WEEKLY WAGES AND SALARIES

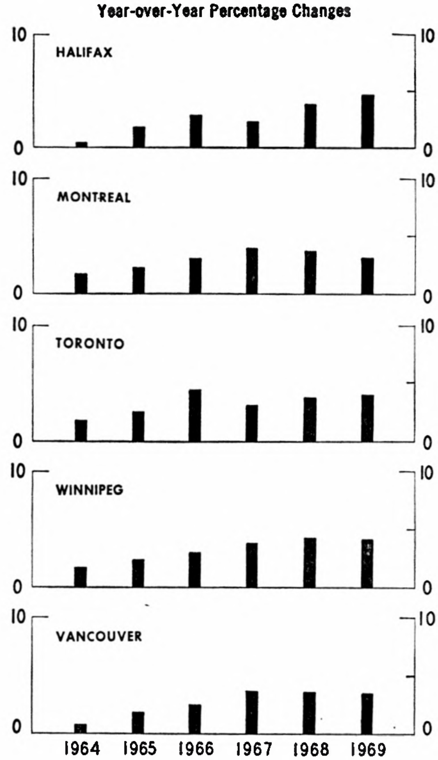
Industrial Composite

Year-over-Year Percentage Changes



CONSUMER PRICES

Year-over-Year Percentage Changes

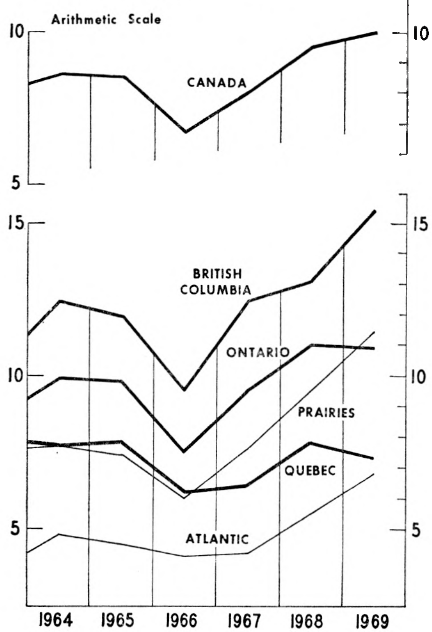


REGIONAL ECONOMIC INDICATORS

HOUSING STARTS

Per Thousand Persons

Annual — Units

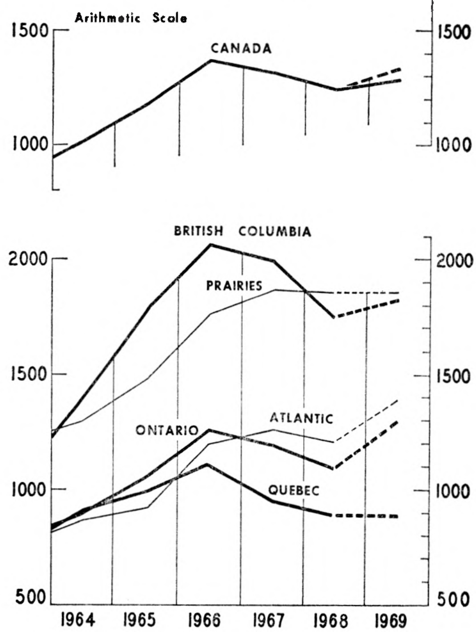


BUSINESS FIXED INVESTMENT[1]

EXCL. HOUSING

Per Employee

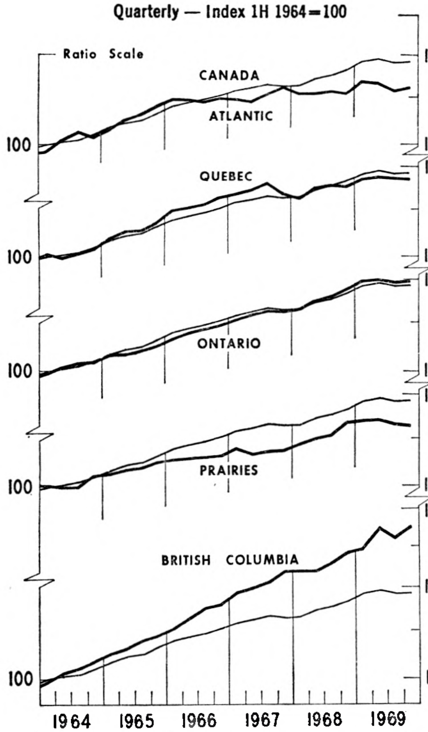
Annual — Dollars



1. Broken lines indicate mid-year intentions for 1969. Actual outlays are not yet available by regions.

EMPLOYMENT

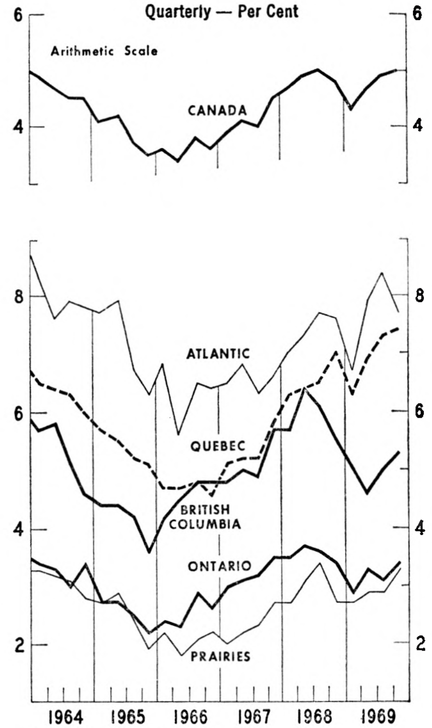
Quarterly — Index 1H 1964=100



Seasonally adjusted : Based on Labour Force Survey.

UNEMPLOYMENT RATES

Quarterly — Per Cent



Seasonally adjusted.

PROVINCIAL UNEMPLOYMENT RATES

(per cent)

	Annual				Fourth quarter[1]	
	1966	1967	1968	1969	1968	1969
Newfoundland	7.9	8.4	9.7	10.3	8.4	8.9
Prince Edward Island	5.6	5.6	5.6	5.3	2.8	5.3
Nova Scotia	5.2	5.6	5.9	5.4	4.7	4.7
New Brunswick	6.9	6.9	7.2	8.5	6.8	6.3
Quebec	4.7	5.3	6.5	6.9	6.0	6.3
Ontario	2.5	3.1	3.5	3.1	2.7	2.8
Manitoba	2.5	2.5	3.5	2.7	3.2	2.2
Saskatchewan	1.5	1.8	2.3	3.1	2.3	3.8
Alberta	2.1	2.4	3.0	2.7	2.3	2.8
British Columbia	4.5	5.1	5.9	5.0	5.5	5.3
Canada	3.6	4.1	4.8	4.7	4.2	4.3

(1) Not seasonally adjusted.

Saskatchewan; in Quebec the rate increased for the fourth successive year, though more slowly than in 1968.

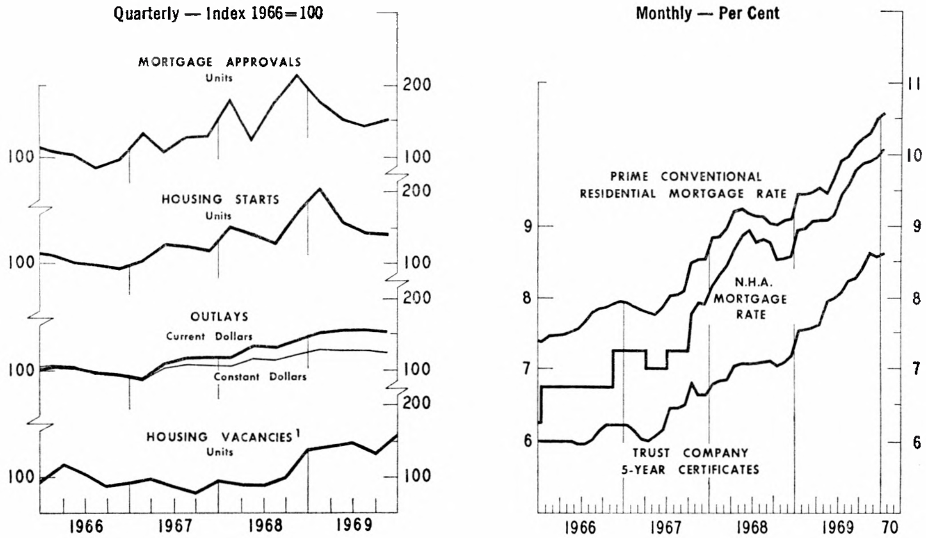
The foregoing developments are summarized in the charts on the two preceding pages. These charts also show that the inflation of recent years, as reflected in rising consumer prices and average weekly wages and salaries, has been shared by all regions to a strikingly similar degree.

SPENDING AND FINANCING BY MAJOR SECTORS

HOUSING SECTOR. The strongly rising trend of residential construction activity which began in 1967 continued until the early part of 1969 and the volume of outlays remained at a record level until late in the year, when there was some easing in activity.

Housing starts reached a very high seasonally adjusted rate in the early months of 1969. Subsequently, the number of starts dropped back but, for the year as a whole, they totalled 210 thousand units compared with the previous year's record of 197 thousand; most of the increase was in apartments and row housing. There were 196 thousand completions in 1969, 25 thousand more than in the previous year. The number of newly completed but unoccupied dwellings, which had been at a very low level until the latter part of 1968, was

HOUSING AND MORTGAGE MARKET



Seasonally adjusted at annual rates.
1. Newly completed only, unadjusted.

appreciably higher throughout 1969, suggesting a slight easing in the backlog of unsatisfied demand. Despite the slowing in starts, there were more units under construction at the end of 1969 than a year earlier.

While the slowing in housing activity in recent months reflects some reduction in the availability of mortgage financing, the rising costs associated with housing have also probably acted to limit effective demand. Construction costs continued to increase rapidly, though less sharply after mid-year as lumber prices eased. Financing costs also rose substantially in 1969. Typical interest rates on prime conventional mortgages increased from about 9 per cent at the end of 1968 to 10½ per cent at the end of 1969.

For the year as a whole, the total value of new residential mortgage approvals by financial institutions and CMHC was almost as high as in 1968, although there was a declining trend through most of 1969 from the extremely high level reached in the latter part of 1968. CMHC's direct lending rose from $456 million to $549 million in 1969, and there was a major change in the orientation of its activity; loans for low income housing almost doubled, from $228 million to $423 million. Loans approved by private institutions declined by $107 million in 1969 following a substantial rise of $694 million in the previous year. The value of mortgage loans approved by the chartered banks (including their mortgage lending subsidiaries), which had increased markedly

GROSS RESIDENTIAL MORTGAGE LOAN APPROVALS

(millions of dollars)

	Semi-annual				Annual		
	1968		1969				
	1st half	2nd half	1st half	2nd half	1967	1968	1969e
New housing							
Private financial institutions(1)							
Conventional loans	478	485	628	359	745	963	987
NHA insured loans	393	439	383	318	356	832	701
Sub-total	871	924	1,011	677	1,101	1,795	1,688
CMHC	154	302	183	366	685	456	549
Total new housing	1,025	1,226	1,194	1,043	1,786	2,251	2,237
Existing housing	295	324	399	333	697	619	732
Total	1,320	1,550	1,593	1,376	2,483	2,870	2,969

e: Estimate.

(1) Includes: life insurance companies, chartered banks, trust and mortgage loan companies, Quebec savings banks, fraternal and mutual benefit societies.

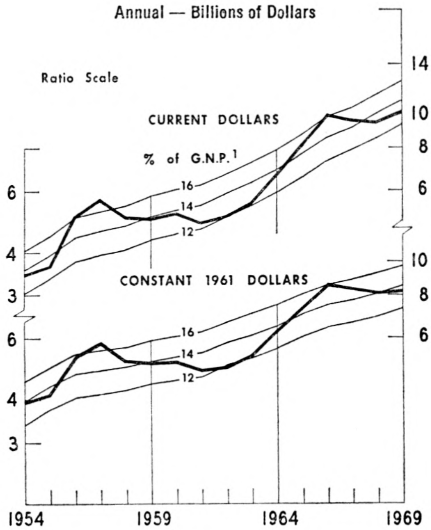
in 1968, decreased somewhat in 1969 and approvals by life insurance companies declined substantially. Indeed, the trust and mortgage loan companies were the only group of private lenders to increase significantly their approvals on new construction in 1969 and there was also an appreciable increase in their loans on existing houses.

Tight credit conditions have not had as great an impact on the supply of mortgage money as might have been expected on the basis of past experience. The trust and mortgage loan companies were able to attract a substantial volume of term deposits in 1969 (see page 58). Other factors helping to sustain the flow of funds into housing in 1969 were the greater flexibility of mortgage interest rates and the willingness of borrowers to pay very high rates, no doubt in part because of continued inflationary expectations.

In the course of the year further changes were made in the conditions of lending under the National Housing Act. In April the regulations were amended to permit the reduction of the original term of NHA insured mortgages to five years and to increase the amount of the maximum mortgage for new houses. At mid-year the Act was amended to eliminate the ceiling on the maximum interest rate on loans insured under the Act and to increase the maximum mortgage obtainable under the NHA on existing houses.

BUSINESS SECTOR. Business investment in new plant and equipment, which declined slightly in 1967 and 1968 after several years of very rapid increase, rose moderately again in 1969 to just above the 1966 peak. Such investment in 1969 was almost 7 per cent higher in value terms than in 1968. Non-residential construction outlays, which earlier had been expected to rise by as much as 15 per cent, were considerably affected by work stoppages during the summer and are now estimated to have risen by about 5 per cent. The sharp increase in construction costs more than accounted for this rise. Investment in machinery and equipment appears to have largely fulfilled earlier expectations, rising by about 8½ per cent. Prices of equipment rose only moderately and there was an appreciable rise in the physical volume of equipment put in place. On balance, the physical volume of total business investment increased only slightly and in relation to GNP continued to run at a level that was mid-way between the highs and lows of the 1960's. (See chart)

BUSINESS FIXED INVESTMENT
Excluding Housing



1. The contour lines enable one to see the ratio of investment to GNP in each year.

Business investment in inventories did not increase substantially after the first quarter of the year. Labour disputes, especially in heavy industry, interrupted supplies of many important materials and there was pressure to economize on inventory as credit conditions tightened. The stocks-to-shipments ratio in manufacturing was quite moderate at year-end.

The increase in dollar outlays on capital investment by the private sector occurred at a time when internally generated cash flow was slowing as a result of the squeeze on profits. While total funds from current operations were higher for the year as a whole than in 1968, available cash was reduced by the acceleration of corporation income tax collections announced in the October 1968 budget of the Government of Canada and in Ontario by a similar provincial measure in March 1969. In the event, funds raised externally by business during 1969 were considerably higher than in 1968—increasing by almost one third from identifiable sources.

While about the same amount of funds was obtained from non-resident direct investment in Canada as in 1968, investment by Canadian companies abroad was appreciably higher than in the previous year. Canadian direct invest-

MAJOR SOURCES OF EXTERNAL FUNDS OBTAINED BY NON-FINANCIAL BUSINESS

(millions of dollars)

	Semi-annual				Annual		
	1968		1969				
	1st half	2nd half	1st half	2nd half	1967	1968	1969
Net new issues of:							
Stocks	200	370	473	270	374	570	743
Convertible bonds	49	10	116	25	7	59	141
Other bonds	374	260	234	272	802	634	506
Commercial paper and bankers' acceptances	53	47	138	164	85	100	302
Sub-total	676	687	961	731	1,268	1,363	1,692
Increases in loans:							
Chartered banks(1)	366	269	1,111	194	602	635	1,305
Sales finance companies	127	119	79	107e	144	246	186e
Industrial Development Bank	21	21	23	31	34	42	54
Sub-total	514	409	1,213	332e	780	923	1,545e
Net direct investment from abroad	200	275	205	165	566	475	370
Total	1,390	1,371	2,379	1,228e	2,614	2,761	3,607e

e: Estimate.
(1) Total business loans excluding provincially-guaranteed loans to utilities, plus foreign currency loans to residents.

ment in the United States was substantially higher and accounted for about two thirds of the outflow in 1969; there was also some increase in investment in developing countries largely offset by a decline in investment in developed overseas countries. Borrowing by business was particularly high in the first half of the year. In this period business loans from chartered banks rose very strongly and accounted for about one half of total business borrowing. In the second half of the year there was a substantial reduction in the amount of new external funds obtained by business, particularly from the chartered banks.

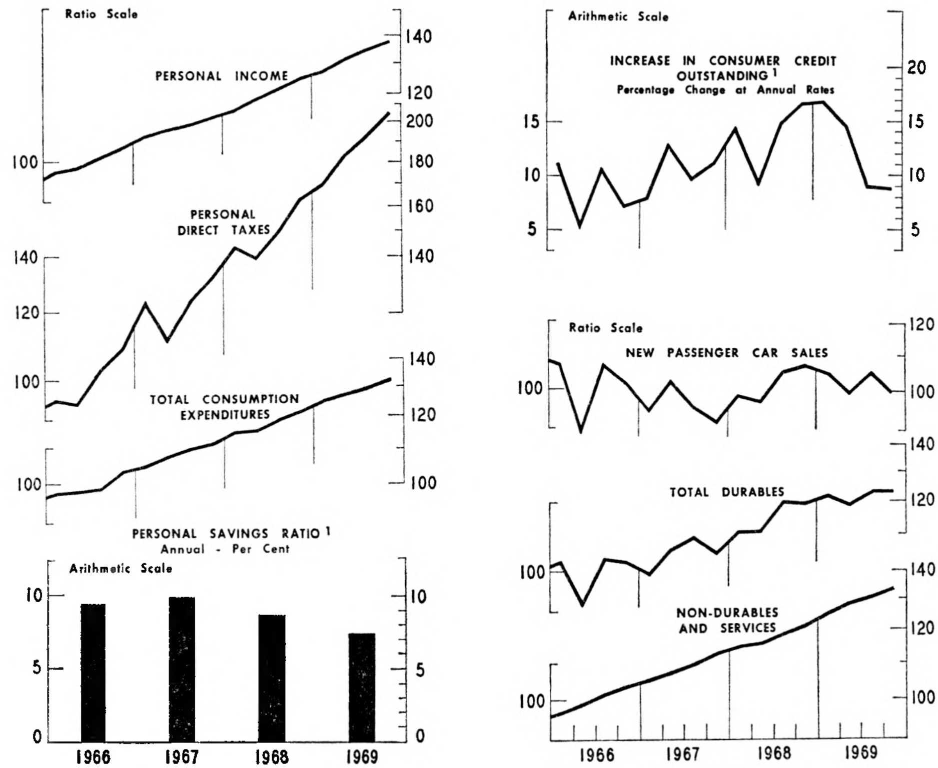
The form in which funds were raised in financial markets reflected a growing preference by Canadian investors for equities and short-term instruments, as distinct from long-term bonds. To the extent that business continued to borrow in the latter form, there was increased reliance on convertible bonds, on providing investors with early redemption options and on foreign markets. Sales of equities to non-residents also increased significantly. The geographic distribution of all corporate placements is shown in the table on page 61.

A comparison of the borrowing requirements of non-financial businesses to meet capital outlays with the external borrowing undertaken in 1969 suggests that there was again a substantial addition to their holdings of financial assets, though probably not as large as in 1968. It seems likely that part of the addition to liquidity last year was unintended and resulted from unforeseen delays in investment programmes.

PERSONAL SECTOR. Total consumer expenditure in 1969 increased by 9½ per cent, slightly more than in the previous year. The rise occurred despite a levelling off in total expenditure on durable goods, and the transfer of some medical expenses to the public sector. Car sales, which had been very strong, showed clear signs of an easing as early as the second quarter of 1969, and

PERSONAL INCOME AND CONSUMPTION EXPENDITURES

Quarterly — Index 1966=100



Seasonally adjusted.

1. Excluding farm inventories.

1. Fourth quarter 1969 is estimated.

exhibited more pronounced weakness around the end of the year. Outlays on household and other durables rose at about the same rate as in the previous year.

Incomes before taxes rose by over 10 per cent in 1969, slightly faster than in the previous year. A more rapid increase in labour income in 1969 was partly offset by a slowing in incomes from other sources, in particular by an actual decline in net income received by farmers. However, a sharp increase in personal income tax payments held the rise in personal disposable income to 8 per cent, about the same as in 1968. There was a further decline in the proportion of personal disposable income saved.

As shown in the chart on page 43, the growth of consumer credit slowed markedly in the second half of 1969. This was attributable to the restriction of lending by the chartered banks. After rising by $417 million, seasonally adjusted, in the first half of 1969, outstanding chartered bank unsecured personal loans increased by only $67 million in the second half of the year. For the year as a whole, such loans increased by about $200 million less than in 1968, but this was offset by credit extended by other lenders. Thus, as the table below shows, the increase in the total amount of consumer credit outstanding was slightly larger in 1969 than in 1968.

MAJOR SOURCES OF INCREASE IN CONSUMER CREDIT OUTSTANDING[(1)]

(millions of dollars)

	Semi-annual				Annual		
	1968		1969				
	1st half	2nd half	1st half	2nd half	1967	1968	1969
Increase in amount outstanding:							
Chartered banks (unsecured personal loans)[(1)]	264	424	505	– 23[(2)]	519	688	482[(2)]
Consumer loan companies	141	68	97	164	140	209	261
Sales finance companies	12	8	85	69	– 79	20	154
Credit unions and caisses populaires	84	69	45	76[e]	157	153	121[e]
Life insurance companies (policy loans)	40	27	33	59	36	67	92
Quebec savings banks	2	2	5	– 2[(2)]	1	4	3[(2)]
Retail dealers[(3)]	–124	194	– 97	217[e]	42	70	120[e]
Total	419	792	673	560[e]	816	1,211	1,233[e]

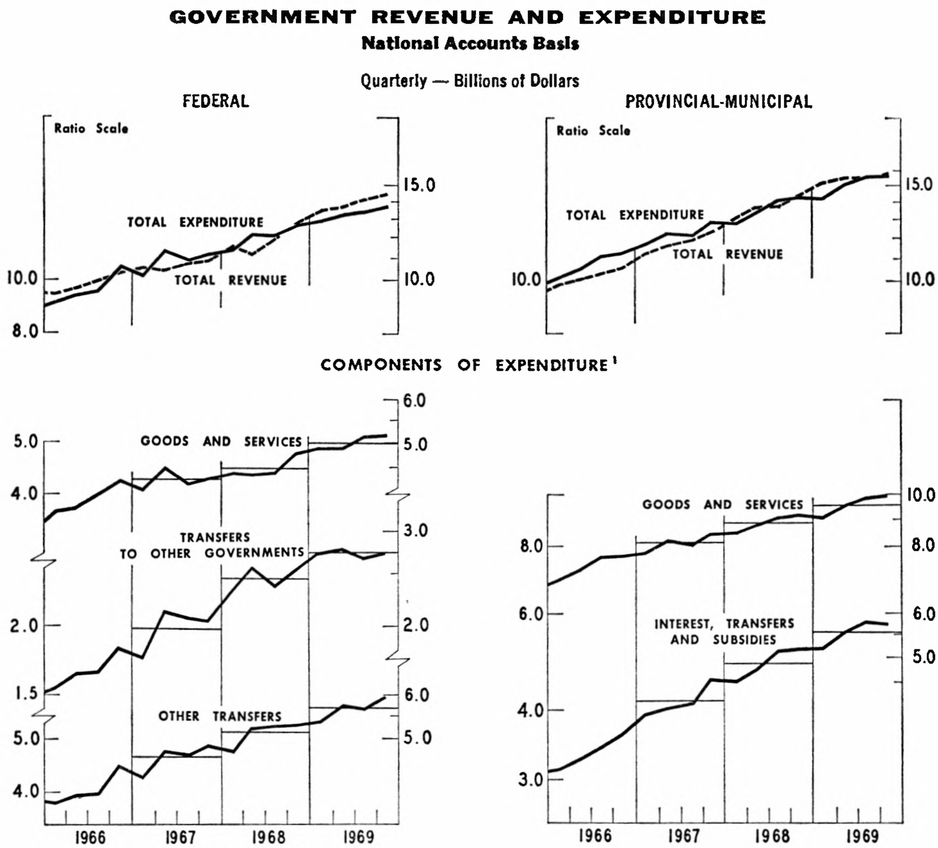
e: Estimate.

(1) Not seasonally adjusted. In the case of chartered bank unsecured personal loans the seasonally adjusted half year figures, in millions of dollars, were 194 and 495 in 1968 and 417 and 67 in 1969.

(2) Not strictly comparable with earlier data since one of the Quebec savings banks became a chartered bank in November 1969.

(3) Includes credit extended by department stores, furniture and appliance dealers, motor vehicle dealers, other retail dealers and oil company credit cards.

GOVERNMENT SECTOR. Outlays on goods and services by all levels of government combined increased by over 9 per cent in 1969, a little more than in 1968. However, as in 1968, most of the increase in spending reflected higher prices rather than an increased volume of purchases. About two thirds of the 20 per cent increase in federal non-defence outlays on goods and services is accounted for by higher salary costs, including large retroactive pay adjustments in the course of the year. Defence spending was little changed from the year before. At the provincial-municipal level, outlays on goods and services increased by about 8 per cent. Higher wages and salaries together with other rising costs, particularly in construction, accounted for most of the increase. In addition, expenditures were augmented by the participation in Medicare of five additional provinces during the year.



Seasonally adjusted at annual rates.

1. Horizontal lines represent annual totals.

Transfer payments, by all levels of government combined, to persons and non-commercial institutions increased nearly as much as in 1968. The consolidated total of expenditure by all governments on the national accounts basis (which excludes substantial non-budgetary disbursements) rose by about 10½ per cent in 1969, about the same as in 1968.

Total revenues of the government sector on the national accounts basis (excluding net receipts under the Canada and Quebec Pension Plans) rose by 16 per cent compared with 13 per cent in the previous year. This was the result of further tax increases as well as the continued growth in the tax base. At the federal level, the Social Development Tax, which came into effect at the beginning of the year, was an important factor in the faster growth of revenues in 1969 and the substantial movement from a deficit of $165 million on a national accounts basis in 1968 to a surplus now estimated at close to $600 million in 1969. While rising less rapidly than in 1968, provincial-municipal revenues in 1969 again increased more than expenditures and a surplus was recorded at this level for the first time in many years, though most of it was achieved in the early part of the year. The net position of all governments combined (excluding the Canada and Quebec Pension Plans) moved on a national accounts basis from a deficit of $190 million in 1968 to a surplus approaching $1 billion in 1969.*

The swing by the federal Government to a surplus position on the national accounts basis in 1969, combined with the curtailment of its lending programmes (see Appendix Table III) and the acceleration of corporation tax payments, resulted in a cash surplus of $399 million in contrast to a deficit of over $1 billion in 1968. This enabled the Government of Canada to reduce substantially its recourse to financial markets in 1969 while increasing its cash balances. The outstanding amount of Government of Canada domestic securities (excluding those held by Government accounts) rose by $276 million during 1969 compared with an increase of over $1.1 billion in 1968. (For details of debt management operations see pages 60-63.)

At the provincial-municipal level, the improvement in the income-expenditure position slightly more than offset a rise in loans and advances to the private sector and some increase in fixed capital investment by provincially and municipally owned business enterprises. As a consequence, borrowing by provincial and municipal governments (and their enterprises) declined slightly from $2,568 million in 1968 to $2,427 million in 1969. They relied almost exclusively on foreign markets and the Canada and Quebec Pension Plan funds for new money in 1969. Net funds raised by borrowing abroad amounted to $1,056 million, while for the first time in many years the amount of new money raised in the domestic market was negligible.

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* It should be noted that in national income and expenditure accounting, expenditures do not include loans and advances and other increases in financial or existing real assets; at the same time, the balance does include net receipts which arise from certain sources such as superannuation funds even though these result in increased government liabilities.

MAJOR SOURCES OF FINANCING: FEDERAL, PROVINCIAL AND MUNICIPAL GOVERNMENTS AND THEIR ENTERPRISES(1)

(millions of dollars)

	1967	1968	1969
Government of Canada			
Increase in securities outside Gov't accounts:			
— treasury bills	295	360	67
— Canadian-pay market bonds	454	709	– 115
— Canada Savings Bonds	229	40	324
Sub-total(2)	978	1,109	276
Increase (—) in Canadian dollar cash balances	298	– 60	– 675
Total(2)	1,276	1,049	– 399
Provincial and Municipal Governments			
Increase in outstanding Canadian-pay bonds:			
— purchased by Canada and Quebec Pension Plan funds	821	894	1,020e
— other Canadian dollar issues	861	423	26
Increase in loans from:			
— chartered banks	124	– 4	54
— Government of Canada (including CMHC and MDLF)	175	276	231
Increase in short-term paper outstanding	70e	80e	40e
Increase in foreign currency issues outstanding	800	899	1,056
Total provincial-municipal borrowing(3)	2,851	2,568	2,427

e: Estimate.

(1) To obtain a total of combined federal, provincial and municipal financing without double counting, loans from the Government of Canada to the provinces and municipalities would have to be eliminated, as well as changes in provincial-municipal holdings of Government of Canada securities.

(2) Excluding net new foreign currency issues of the Government of Canada which during 1967, 1968 and 1969 were –45, +266 and +14 respectively. The increase in 1968 reflected new issues sold in the United States, Italy and Germany, the proceeds of which were used to bolster official foreign exchange reserves.

(3) To the extent that we have not been able to identify purchases by provincial government accounts of provincial or municipal securities the total of provincial-municipal financing is overstated.

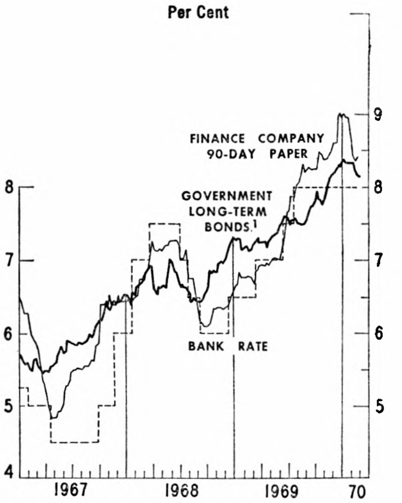
Financial Developments in Canada

GENERAL REVIEW

In an environment influenced by the continued strong demand for funds, entrenched inflationary expectations on the part of borrowers and lenders, and sharply rising interest rates abroad, monetary policy became increasingly restrictive during 1969. As a result, money became more difficult to obtain and its cost rose to very high levels. The Bank of Canada managed the cash reserves of the chartered banks in such a way as to oblige them to meet a considerable part of the strong demand for bank credit by running down their more liquid assets. The Bank also supplemented its traditional techniques of monetary control through cash management by using its power to increase the minimum secondary reserve requirement and by a number of requests to the chartered banks, as described in the opening section of this Report. The increase in total bank assets and in money supply, however defined, was much smaller in 1969 than in 1968. The implementation of monetary policy was facilitated by the improvement in the fiscal position of the Government of Canada. The elimination of the Government's need to add to the total volume of market issues outstanding made it possible for the supply arising from the reduction in the chartered banks' holdings to be absorbed by non-bank holders without putting even greater pressure on financial markets.

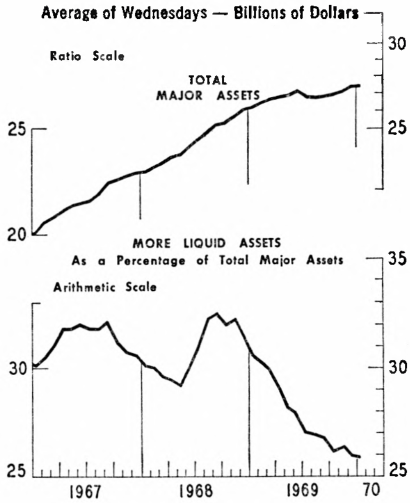
The financing arranged by various sectors of the economy was discussed in the previous section. Excluding the Government, the total was very substantial, particularly in the first half of the year; it is estimated to have amounted to about \$9 billion in 1969 compared with \$8 billion in the preceding year. By far the greater part of this increase was accounted for by the requirements of non-financial businesses. Inflationary expectations, as well as influencing the demand for credit, also had a marked impact on the form of lending. Canadian lenders appeared reluctant throughout most of the year to commit their funds on a long-term basis. In order to raise funds, borrowers shortened the average term of new security issues or in many cases provided the lender with an option between early or late redemption, and had greater recourse to security markets abroad. Businesses also increased their issues of convertible bonds, short-term paper and equities.

INTEREST RATES



1. Average weekly yield on Government of Canada bonds with a maturity of 10 years or over.

CHARTERED BANK ASSETS



Seasonally adjusted.

The tightening of United States monetary policy in 1969 and the pressure which this imposed on short-term interest rates in the Euro-dollar market had consequences for Canada. Interest rates in Canada were importantly affected even though Canadian Government guidelines had been instituted in 1968 in connection with Canada's exemption from the United States balance of payments programme with the objective of limiting the transfer of funds by Canadian investors to countries other than the United States. Canadian banks were able to place funds with banks in the United States at interest rates nearly as high as those prevailing in the Euro-dollar market. In order to shield short-term interest rates in Canada from some of the extraordinary pressures prevailing abroad, the Bank of Canada intervened at mid-year to limit the outflow of "swapped" deposits through the banking system.

BANK OF CANADA OPERATIONS

As indicated in the opening section of this Report, monetary policy again shifted towards severe restraint in the autumn of 1968. The Bank of Canada's cash reserve management was directed towards reducing the liquidity of the banking system. Short-term interest rates rose and the Bank Rate was increased from 6 per cent to 6½ per cent on December 18, 1968 and to 7 per cent effective March 3, 1969. The continued substantial demand for bank credit was met by the banks in part by running down their holdings of liquid assets.

By April 1969 the banks' more liquid assets were over $600 million less than their peak level in the final quarter of 1968 and the ratio of such assets to total major assets was under 29 per cent, a low level by earlier standards. Nonetheless, bank loans continued to increase strongly and in order to add to the pressure on the banks, the Bank of Canada announced on April 11 an increase from 7 per cent to 8 per cent in the minimum secondary reserve ratio required of the chartered banks, effective in June. The resources potentially available to the chartered banks for lending were thus reduced by a further $250 million. Although the rate of growth in bank loans declined in May and June, the banks' more liquid asset ratio fell further to a new low of 27.6 per cent in June.

On June 11 the Bank of Canada raised the Bank Rate from 7 per cent to 7½ per cent. In May and early June there had been a very rapid escalation of Euro-dollar rates to more than 12 per cent and this put strong upward pressure on short-term rates in Canada. On July 15 the Bank of Canada raised the Bank Rate to its present level of 8 per cent and at the same time asked the banks to regard the amount of their "swapped" deposits at that date as a temporary ceiling.* These deposits had risen by over $950 million from the beginning of the year; the increase between mid-April and mid-July alone was $750 million.

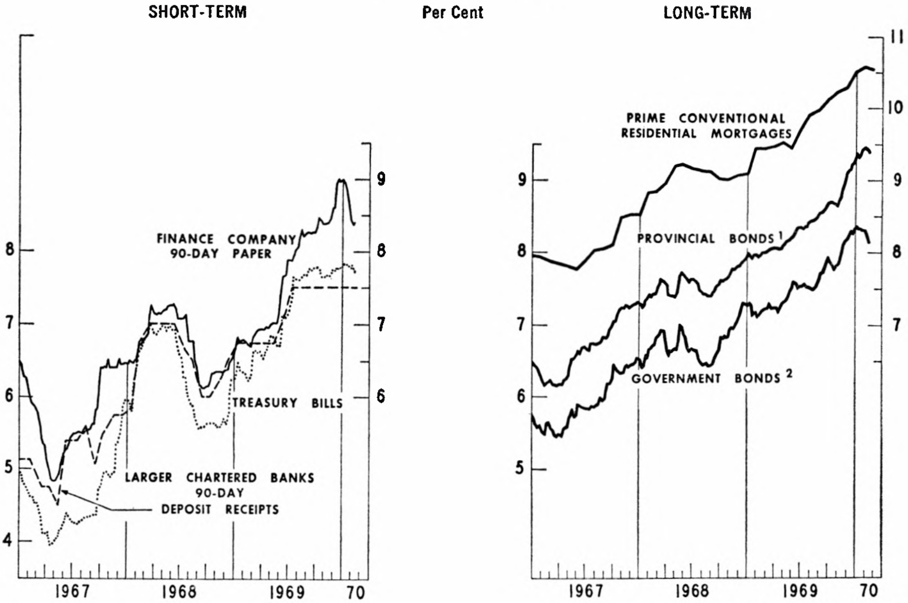
In response to requests of the Bank of Canada, the major banks agreed not to compete aggressively for large Canadian dollar term deposits, and the rate of interest paid on such deposits rose less than other short-term rates. It has remained at 7½ per cent since July and the volume of such deposits has declined considerably. By the end of July, typical short-term market yields had risen by about 1½ per cent from the end of 1968 and the rate on long-term Government of Canada securities had moved up by ¼ per cent over the same period.

During the last six months of the year the tightness of credit conditions was very apparent. Short-term interest rates rose further. The chartered banks' more liquid asset ratio continued to decline and reached a level of 25.9 per cent at year-end. Bank loans increased very little as the banks found it necessary to ration severely their available resources.

There was a marked expansion of the short-term commercial paper market as corporations sought substitutes for bank loans. Excluding paper issued by finance companies and by governments and their agencies, the amount outstanding is estimated to have risen from about $550 million in June to about $850 million in November, about double the rise in the same period of 1968. In December, typical rates offered on such paper rose sharply to reach levels in excess of 9½ per cent, over one per cent higher than at mid-year, and the amount of paper outstanding declined by about $160 million. Although the

* This measure was reinforced in January 1970 when the Bank of Canada wrote to investment dealers and trust companies asking them to co-operate by not arranging similar transactions in other ways.

INTEREST RATES



1. Average weekly yield on the 10 provincials included in the monthly series published by McLeod, Young, Weir and Co. Ltd.
2. Average weekly yield on Government of Canada bonds with a maturity of 10 years or over.

evidence of strain in this market was related in part to usual year-end liquidity demands in both domestic and foreign markets, it may also have indicated that the earlier rate of expansion was somewhat overdone.

Yields on long-term securities also rose, especially in the closing months of the year when they were influenced by similar but more pronounced movements in the United States. In the early part of 1970 there has been a moderate decline in short-term market interest rates partly because of the easing of year-end tensions and partly because of a downward movement of interest rates in the United States. Long-term rates followed a similar pattern.

Beginning in January 1969 the chartered banks were required to meet their statutory average cash reserve requirements on a half-monthly rather than a monthly basis. The new arrangement was intended to increase the predictability and the rapidity of the response of chartered banks to the cash management policy of the central bank and it has worked satisfactorily.

Reflecting the persistent pressure on the banking system the chartered banks had advances outstanding from the central bank on 35 business days in 1969 compared with 14 business days in 1968. The average amount of advances outstanding on business days was $1.2 million in 1969 compared with $0.2 million in 1968. Over the same period securities held by the Bank under purchase and resale agreements with money market dealers were outstanding on 93 business days, compared with 35 business days in 1968 and averaged $9.4 million on a daily basis in 1969 compared with $4.3 million during the previous year.

Changes in the Bank of Canada's holdings of Government of Canada securities for each month in 1969 are summarized in Appendix Table I. There was a net increase in the Bank's portfolio over the year of $170 million, virtually all as a result of transactions with the securities market. From time to time the Bank undertook temporary swaps of foreign currency assets with the Exchange Fund Account for cash management purposes. Appendix Table II indicates the main changes in the Bank's balance sheet each month in 1969. Bank of Canada notes in circulation increased by $217 million over the course of the year.

FINANCIAL INSTITUTIONS

The major assets of the group of financial institutions shown in the table below grew by nearly 8 per cent in 1969 compared with 13 per cent in 1968. Virtually all of this slower growth was attributable to the chartered banks; the annual rate of growth of the other financial institutions as a group was about 12

MAJOR ASSETS OF SELECTED FINANCIAL INSTITUTIONS

	Millions of dollars Dec. 1969	Increase in millions of dollars		Percentage Increase			
		1968	1969	Average 1963-66	1967	1968	1969
Chartered banks(1)(2)	27,503	3,258	1,285	8.3	14.2	14.2	4.9
Quebec Savings Bank(1)	522	62	36	7.3	9.0	14.6	7.4
Trust and mortgage loan companies	8,462e	780	1,019e	18.6	9.8	11.7	13.7e
Sales finance and consumer loan companies	5,269e	447	654e	11.9	6.5	10.7	14.2e
Credit unions and caisses populaires	3,900e	356	291e	14.8	15.0	10.9	8.1e
Total	45,656e	4,903	3,285e	10.8	12.5	13.1	7.8e
Total excluding chartered banks	18,153e	1,645	2,000e	15.2	9.9	11.3	12.4e

e: Estimate.

(1) For comparability the assets of the Quebec Savings Bank which became a chartered bank in November 1969 are included with chartered bank assets in each period shown.

(2) Major Canadian dollar assets plus net foreign currency assets; average of Wednesdays.

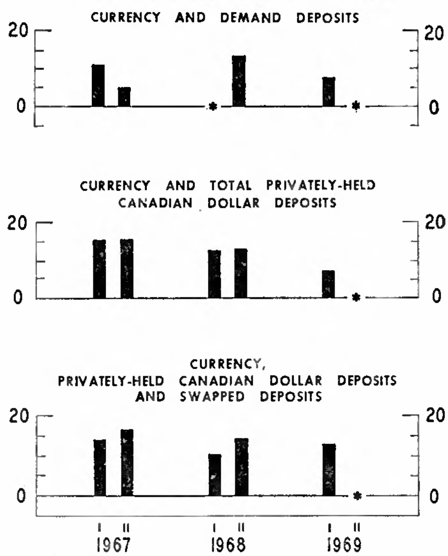
per cent in 1969 compared with about 11 per cent in the previous year. Partly as a result of the improvement in their competitive position arising from the 1967 Bank Act revision the banks grew by 14 per cent per annum in 1967 and 1968. However, their total major assets increased by only 5 per cent in 1969. In absolute terms the combined assets of all these institutions increased by $3,285 million in 1969, $1,618 million less than in 1968.

The competition for funds among financial institutions in 1969 resulted in substantially higher deposit rates. Rates offered by chartered banks on non-chequable savings deposits rose from 5 per cent in late 1968 to 6½ per cent in mid-1969 and since then have remained at that level. Rates on similar deposits at trust and mortgage loan companies followed the same pattern. The rate on large short-term deposits at the banks increased from 6½ per cent in December 1968 to 7 per cent in June and to 7½ per cent in July but as already indicated the rate on these deposits was influenced by requests made by the Bank of Canada. The banks, however, competed vigorously for large foreign currency "swapped" deposits. The rates on such three-month deposits, which had also been at 6½ per cent at the end of 1968, rose to about 8½ per cent at mid-July largely influenced by the rapid rise in Euro-dollar rates and the rates available to Canadian banks in New York. At that time the Bank of Canada requested the chartered banks to regard the level of "swapped" deposits as a ceiling. The three-month rate climbed to a peak level of over 9½ per cent by the end of December as New York rates were rising and the forward discount on the U.S. dollar was narrowing. Trust companies also bid actively for short-term deposits. Rates offered by these institutions on 90-day deposits were between 7¼ per cent and 7½ per cent at mid-year and moved up to a range of 8¼ per cent to 9 per cent at year-end.

The increase in the general public's holdings of bank deposits and other liquid claims on banks was considerably less in 1969 than in 1968. Currency and demand deposits rose by 3.9 per cent compared with 6.7 per cent in 1968. The growth in currency and total privately-held Canadian dollar deposits was 3½ per cent.

SELECTED MONETARY AGGREGATES CURRENCY AND CHARTERED BANK DEPOSITS

Half Yearly Percentage Changes at Annual Rates



Seasonally adjusted.
* Change negligible.

GENERAL PUBLIC HOLDINGS OF CERTAIN FINANCIAL ASSETS

	Millions of dollars December 1969	Percentage increase			
		Average 1963-1966	1967	1968	1969
Currency	3,279	5.9	9.8	9.2	9.7
Chartered bank demand deposits	5,924	6.1	7.2	5.3	0.9
Sub-total	9,203	6.1	8.1	6.6	3.9
Other chartered bank Canadian dollar deposits(1)	18,515	9.3	21.0	16.8	3.3
Sub-total	27,718	8.0	16.1	13.2	3.5
Chartered bank foreign currency deposits of residents					
— swapped	1,592	17.8	12.2	– 5.5	88.4
— other	1,671	23.0	27.5	13.0	40.1
Sub-total: Currency plus all chartered bank deposits shown above	30,981	8.7	16.4	12.6	7.5
Credit unions and caisses populaires deposits	2,310e	13.5	18.0	13.7	13.7e
Quebec Savings Bank deposits(1)	494	7.1	8.7	15.1	7.9
Trust and loan company deposits	7,585e	19.2	10.4	11.9	13.9e
Short-term paper holdings of residents	2,551e	14.0	14.0	39.4	19.1e
Canada Savings Bonds	6,683	7.1	3.8	0.6	5.1
General public holdings of the above assets	50,604e	10.1	13.3	11.7	8.9e

e: Estimate.

(1) For comparability the deposits of the Quebec Savings Bank which became a chartered bank in November 1969 are included with chartered bank deposits in each period shown.

A summary of the various other types of liquid assets held by the general public is presented in the above table. The public's holdings of chartered bank foreign currency deposits (both "swapped" and other) and of deposits at credit unions and caisses populaires, and trust and loan companies showed relatively large increases in 1969, partly offsetting the slower growth in the public's holdings of Canadian dollar bank deposits.

THE CHARTERED BANKS. With an increase of only 5 per cent in their total major assets during 1969 the banks found it necessary to dispose of liquid assets on a large scale to finance a 13½ per cent increase in their loan portfolio. Holdings of liquid assets as a percentage of total major assets had risen to about

CHARTERED BANK MAJOR ASSETS AND LIABILITIES*

(average of Wednesdays — seasonally adjusted)

	Millions of dollars Dec. 1969	Increase in 1969: millions of dollars 1st half	2nd half	percentage at annual rates 1st half	2nd half	Percentage increase 1968	1969
Total major assets	27,366	1,098	255	8.4	1.9	14.2	5.2
More liquid assets	7,098	−644	−455	−15.7	−12.0	17.5	−13.4
Less liquid assets	20,262	1,689	740	18.9	7.6	12.8	13.7
of which: general loans	14,925	1,522	252	23.1	3.4	10.9	13.5
(business loans)(1)	(8,754)	(833)	(251)	(21.7)	(5.9)	(9.4)	(14.1)
(unsecured personal loans)(1)	(4,155)	(417)	(67)	(22.7)	(3.3)	(23.1)	(13.2)
loans to grain dealers	1,267	− 55	380	−11.7	85.7	49.4	34.9
residential mortgage loans(2)	1,310	151	125	29.2	21.1	24.0	26.7
(More liquid assets ratio at end of period, per cent)	(25.9)	(27.9)	(25.9)				
Total Canadian dollar deposits	25,773	1,070	195	8.7	1.5	14.3	5.1
Demand deposits	5,763	192	−137	6.7	− 4.6	5.3	0.9
Personal savings deposits	15,151	758	701	11.1	9.7	15.8	10.6
of which: chequable(2)	5,636	−332	−615	−10.1	−19.7	−13.3	−14.4
non-chequable(2)	5,663	705	618	32.5	24.5	56.4	30.5
fixed-term(2)	3,594	601	454	47.3	28.9	101.3	41.6
Non-personal term and notice deposits	3,688	−157	−636	− 7.0	−29.4	20.3	−17.6
Government of Canada deposits(2)	1,437	− 53	604	−12.0	145.0	29.7	62.2
Swapped deposits(1)(2)	1,551	717	71	187.9	9.6	−15.8	103.3
Other foreign currency deposits of residents(1)(2)	1,712	245	191	38.4	25.1	22.2	34.2

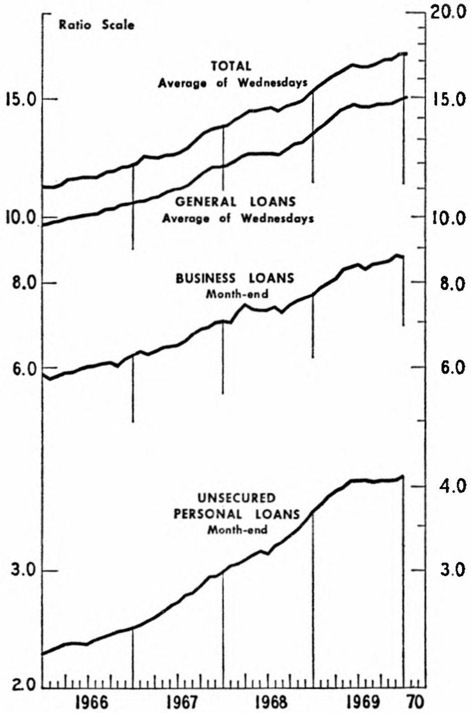
(1) Month-end figures.
(2) Not seasonally adjusted.
* Includes data as at December 31, 1969 for theQuebec Savings Bank which became a chartered bank in November 1969; excluding this bank, total major assets rose by 4.9 per cent in 1969.

32 per cent in the fourth quarter of 1968 but by the end of 1969 this ratio had declined to the historically low level of 26 per cent. Between November 1968 and December 1969 the banks reduced their holdings of more liquid assets (including net foreign assets) by about $1,195 million to $7,119 million (before seasonal adjustment). Of the December 1969 total the amount of required cash and secondary reserves was $3,768 million.

Rising rates of interest in securities markets and the difficulties of raising funds in the capital market contributed to a strong demand for business loans in

CHARTERED BANK LOANS

Average of Wednesdays — Billions of Dollars



Seasonally adjusted.

1969. Most of the increase in business loans was, however, concentrated in the first half of the year when they rose at a seasonally adjusted annual rate of 22 per cent. The rate of increase fell to 6 per cent in the second half of the year.

Consumer loans were also strong in 1969 increasing at an annual rate of nearly 23 per cent in the first half of the year. In the second half of the year, however, the rate of increase in these loans was just over 3 per cent. Residential mortgage loans continued to rise markedly in 1969 as they had the previous year. Grain loans, which include loans to the Wheat Board to finance its marketing operations and an extended advance payment programme for farmers, showed a large increase in 1969, as a result of the heavy build-up of grain stocks.

The cost of bank loans rose substantially during the first half of the year. The prime lending rate, which was 6¾ per cent in the closing months of 1968, rose to 8½ per cent by the middle of 1969 and has since remained at that level.

With the co-operation of the chartered banks the Bank of Canada initiated in November 1968 a quarterly survey of chartered bank lending rates. The survey covers all loan transactions, whereby a customer's account is credited with funds whether under existing, new or renewed authorizations. The survey specifically excludes unsecured personal loans, residential mortgage loans, day loans, call loans and loans to grain dealers. The banks selected a broadly representative sample of branches which report the details of all their loans made on three consecutive days near the middle of each quarter. A total of 125 branches have been involved and they have reported on approximately 5,000 loans each quarter.

The following table shows the average interest rate on new demand loans in the sample weighted by the dollar volume, as well as the distribution of these loans, between those made at the prime rate and those above it. The average

DISTRIBUTION OF NEW DEMAND LOANS BY INTEREST RATES CHARGED(1)

Date of survey	Prime rate	Average rate on new demand loans(2)	Percentage distribution of dollar volume: At prime	At prime plus ¼%	At prime plus ½%	At prime plus ¾%	Exceeding prime plus ¾%
1968							
Nov.	6.75%	7.15%	39	23	17	8	13
1969							
Feb.	7.00%	7.35%	45	17	17	9	12
May	7.50%	7.78%	54	11	17	9	9
Aug.	8.50%	8.79%	53	8	21	10	8
Nov.	8.50%	8.78%	60	7	16	7	10

(1) The term "new" loans in this survey is defined as any transaction whereby a customer's account is credited with funds during the three selected survey days, whether under existing or renewed authorizations.

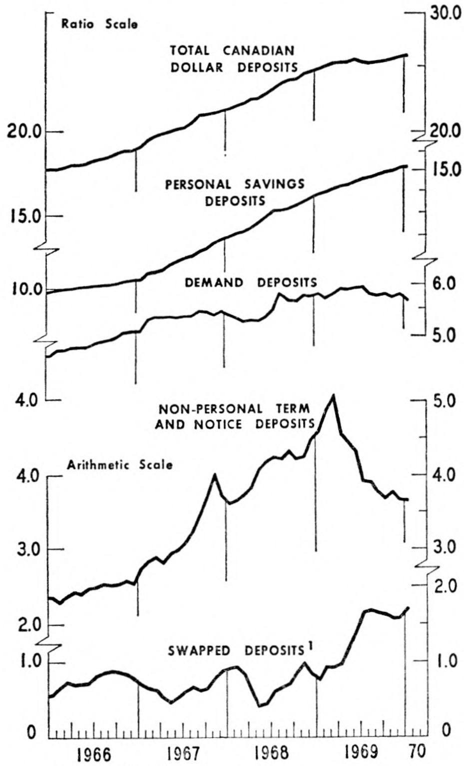
(2) Weighted by dollar volume.

rate charged on all new demand loans rose from 7.15 per cent in November 1968 to 8.79 per cent in August 1969 and remained at about that level in the November 1969 survey.

On the liability side of the banks' balance sheets only the personal savings and foreign currency deposits showed substantial increases. Within the personal savings category there was, however, a continued shift from chequable savings deposits into non-chequable and fixed-term deposits which pay higher rates of interest. Non-personal term and notice deposits declined by over $1 billion from their peak in the first quarter of 1969 as the rates paid on such deposits became less competitive. Many depositors moved their funds into "swapped" deposits and other foreign currency deposits at the chartered banks as well as into other short-term instruments.

SELECTED CHARTERED BANK LIABILITIES

Average of Wednesdays — Billions of Canadian Dollars



Seasonally adjusted.

1. Unadjusted.

TRUST AND MORTGAGE LOAN COMPANIES. The major assets of the trust and mortgage loan companies rose by nearly 14 per cent in 1969 compared with almost 12 per cent in the previous year. Net mortgage lending increased substantially reflecting the large volume of loans approved in the latter part of 1968 and throughout most of 1969. Most of the funds for mortgage lending came from the issue of fixed-term deposit-type instruments. The typical rates offered by the trust companies on five-year fixed-term certificates rose from just over 7 per cent to a range of 8½ per cent to 8¾ per cent in the course of the year.

TRUST AND MORTGAGE LOAN COMPANIES
MAJOR ASSETS AND LIABILITIES

	Millions of dollars Dec. 1969e	Percentage Increase			
		Average 1963-66	1967	1968	1969e
Total major assets	8,462	18.6	9.8	11.7	13.7
Cash and short-term investments(1)	742	17.8	17.5	32.6	8.5
Federal, provincial, municipal and corporate bonds	1,532	11.2	10.6	7.2	6.4
Mortgage loans and sales agreements	5,805	22.4	9.0	10.5	17.1
Other assets	383				
Total major liabilities	7,585	19.2	10.4	11.9	13.9
Demand and savings deposits	1,709	16.1	5.5	7.2	2.1
Guaranteed investment certificates, debentures and other term deposits	5,876	20.4	12.2	13.6	17.8

e: Estimate.

(1) Short-term investments include: Government of Canada treasury bills, term deposits in chartered banks and trust and loan companies, short-term notes of sales finance companies and commercial paper.

SALES FINANCE AND CONSUMER LOAN COMPANIES. For the second consecutive year, the major assets of the sales finance and consumer loan companies grew strongly. Their business lending rose less than in 1968 but their consumer loans increased quite sharply. Very late in the year there were some signs of slackening in the rate of growth of consumer loans mainly reflecting the weakness in new car sales. Loans from parent and affiliated companies and an increase in short-term paper outstanding were the principal sources of funds to the industry during the year.

SALES FINANCE AND CONSUMER LOAN COMPANIES MAJOR ASSETS AND LIABILITIES

	Millions of dollars Dec. 1969e	Annual percentage increase 1967	1968	1969e
Total major assets(1)	5,269	6.5	10.7	14.2
of which:				
Investments in securities	128	89.7	−11.8	32.0
Gross receivables	5,095	5.4	11.8	13.4
consumer receivables	3,052	2.6	9.5	15.7
business receivables	2,043	9.8	15.3	10.0
Total major liabilities	4,302	0.8	9.7	14.5
Bank loans	385	−10.7	−13.1	23.4
Short-term paper	1,559	− 0.9	33.5	18.9
Loans from parent and affiliated companies	856	− 5.0	2.3	19.7
Long-term debt, with original term of more than one year	1,502	9.1	2.5	5.8

e: Estimate.
(1) Includes receivables net of allowance for bad or doubtful accounts.

LIFE INSURANCE COMPANIES. During 1969 there were marked adjustments in the pattern of investment by the life insurance companies. The volume of net mortgage lending and new mortgage loan commitments undertaken by the life insurance companies declined quite sharply in 1969, although they provided an increased volume of funds through equity participation in new projects. Holdings of bonds changed little; but the industry substantially

SELECTED CANADIAN ASSETS OF SIXTEEN LIFE INSURANCE COMPANIES(1)

	Millions of dollars Dec. 1969e	Percentage increase Average 1963-66	1967	1968	1969e
Total Canadian assets	12,308	7.1	5.6	5.9	5.0
of which:					
Federal, provincial, municipal and corporate bonds	4,122	3.2	3.4	1.8	0.5
Mortgage loans	6,224	10.0	5.4	6.3	4.2
Real estate	543	6.3	7.7	6.8	15.3
Policy loans	575	5.0	6.4	14.9	20.5
Preferred and common stocks	687	20.5	26.5	24.6	21.1

e: Estimate.
(1) Relates to the life branch assets of 16 life insurance companies whose net premium income in Canada in 1968 was 80.9 per cent of the total of all companies registered under the Federal Insurance Acts.

increased its investment in short-term paper and common stocks. There was also a continued increase in the amount of policy loans in 1969. For the year as a whole total assets (held in Canada) by the insurance companies shown in the table on page 59 grew by about 5 per cent compared with almost 6 per cent in the previous year.

SECURITIES MARKETS FINANCING

Governments and private corporations issued a total of $4.7 billion of new securities net of retirements in 1969, about $800 million less than the previous year. Net new borrowing by the Government of Canada declined by more than $1 billion while net new issues by others rose from $4.2 billion in 1968 to $4.5 billion in 1969. Among the major suppliers of funds to the new issues market only the non-bank financial institutions and non-residents increased their purchases of securities. The chartered banks' security holdings fell by $481 million during 1969, compared with a net increase of over $1 billion in 1968. Direct purchases of securities by other residents were down slightly despite the successful Canada Savings Bond campaign. The holdings of provincial and municipal securities by the Canada and Quebec Pension Plans continued to rise during 1969.

As noted earlier in the discussion of spending and financing by major sectors, there were marked shifts in borrowing and in the type of security offered by various borrowers in 1969. The details of many of these changes may be seen in the table on the following page.

GOVERNMENT OF CANADA DEBT MANAGEMENT OPERATIONS

The continued rise in the trend of the general level of interest rates in 1969 created an unsettled environment for debt management operations but the problem was eased by the much improved fiscal position of the Government of Canada and the relative stability in foreign exchange reserves.

Debt management operations in market securities were generally confined to the refunding of maturing issues in the domestic market. There were five market bond offerings totalling $1,390 million against retirements and cancellations of $1,576 million. Details are provided in the table on page 63. In addition to the offerings of three-month and six-month treasury bills at the regular weekly tenders, special bills of up to one year were issued on three occasions each connected with a refunding of maturing securities. Treasury bills outstanding rose by $70 million. The net decline in total Canadian dollar market securities was, therefore, $116 million.

NET NEW ISSUES OF SECURITIES

(millions of Canadian dollars)

	1967	1968	1969
Funds raised through new issues of:			
Government of Canada bonds and treasury bills....	934	1,375	290
Provincial and municipal securities...............	2,552	2,296	2,142
Corporate bonds — convertible..................	17	64	152
— other.......................	973	822	693
Corporate short-term paper......................	70	407	536
Corporate stocks.............................	507	598	932
Total funds raised and supplied.............	5,053	5,562	4,745
Funds supplied by increase in holdings of:			
Bank of Canada			
— Government of Canada market issues.........	334	135	170
Chartered banks			
— Government of Canada market issues.........	740	943	– 480
— Provincial and municipal securities...........	84	48	– 7
— Corporate securities.......................	45	107	6
Total chartered banks....................	869	1,098	– 481
Non-bank financial institutions			
— Government of Canada market issues.........	– 4	63	115e
— Provincial and municipal securities...........	143	19	– 47e
— Corporate bonds and short-term paper.......	274	191	266e
— Corporate stocks.........................	90	130	253e
Total non-bank financial institutions........	503	403	587e
Canada and Quebec Pension Plans			
— Provincial and municipal securities...........	821	894	1,020e
Other residents			
— Canada Savings Bonds.....................	229	40	324
— Government of Canada market issues.........	– 253	– 68	154
— Provincial and municipal securities...........	683	524	109
— Corporate bonds and short-term paper.......	632	739	447
— Corporate stocks.........................	369	296	422
Total other residents.....................	1,660	1,531	1,456
Non-residents			
— Government of Canada market issues.........	– 112	262	7
— Provincial and municipal securities...........	821	811	1,067
— Corporate bonds and short-term paper.......	109	256	662
— Corporate stocks.........................	48	172	257
Total non-residents......................	866	1,501	1,993
of which:			
U.S. investors................	894	1,034	1,374
Other investors..............	– 28	467	619

e: Estimate.

Net redemptions of Canada Savings Bonds were heavy prior to October as yields on other instruments available to investors became more attractive, but the 1969/70 issue was very successful and the total of Canada Savings Bonds outstanding increased by $324 million.

A marked shift in the distribution of marketable Government of Canada securities outstanding occurred in response to monetary policy: chartered bank holdings fell by $480 million while resident general public holdings (including investment dealers) increased by $269 million. Bank of Canada holdings rose by $170 million.

The new Government of Canada bond issues offered were short and medium term to meet investor preferences. In March and again in September investors were offered five-year bonds with an option to extend the term through exchange into longer maturities. Advance refunding of near maturities with the Bank of Canada formed a part of three operations.

The Canada Savings Bond campaign was the major debt operation of the year. The 1969/70 Series, which was dated November 1, 1969 to mature in nine years, offers investors yields ranging from 7 per cent in the first year up to 8¼ per cent by the fourth year for an average annual yield of 8 per cent when held to maturity and carries an optional compounding feature. Many holders of outstanding series took advantage of the record rate of return to convert their holdings into the new series and, as a result, gross sales of the 1969/70 Series in the fourth quarter of 1969 amounted to $4,741 million.

SUMMARY OF DIRECT AND GUARANTEED NEW ISSUES AND RETIREMENTS
GOVERNMENT OF CANADA MARKETABLE SECURITIES*

Date	Issues offered	Amount delivered (millions of dollars par value)	Term to maturity	Yield to maturity	Amount retired (millions of dollars par value)
		(Payable in Canadian dollars)			
1969					
Mar. 14					100(1)
Apr. 1	7% May 1, '70	125	1 yr. 1 mo.	7.09	
	7¼% Apr. 1, '72	235	3 yrs.	7.29	
	7¼% Apr. 1, '74(4)	125	5 yrs.	7.25	
		485			410
June 27	Treasury bills	175	308 days	7.46	150
July 1					300
July 2	7¾% July 1, '70	130	1 yr.	7.75	
	8% July 1, '78	125	9 yrs.	8.00	
	Treasury bills	20	268 days	7.50	
		275			
July 25					75(5)
Aug. 15	7¾% Oct. 1, '70	40	1 yr. 1½ mos.	7.88	
	8% Feb. 1, '73	110	3 yrs. 5½ mos.	8.00	
		150			
Sept. 15					120(6)
Oct. 1	8% Oct. 1, '70	30	1 yr.	8.00	
	8% Oct. 1, '71	45	2 yrs	8.00	
	8% Oct. 1, '74(7)	225	5 yrs.	8.00	
		300			350
Nov. 28	Treasury bills	75	364 days	8.01	75
Dec. 15	8% Dec. 15, '70	75	1 yr.	8.11	
	8% Oct. 1, '71	125	1 yr. 9½ mos.	8.14	
		200			210
Dec. 31					11(8)
		(Payable in foreign currency)			
Jan. 15	6⅞% June 1, '88(2)	16	20 yrs.	6.60	
Apr. 15					1(3)
Oct. 15					1(3)

* Excludes three-month and six-month treasury bills.

(1) Cancellation of 5% bonds due July 1, 1969 held by Securities Investment Account.

(2) Part of the June 11, 1968 U.S. $100 million issue which was delivered on January 15, 1969.

(3) Partial redemption at par of U.S. pay 5% October 15, 1987 for the Sinking Fund.

(4) Exchangeable into 7½% bond to be dated April 1, 1974 and to mature April 1, 1984.

(5) Cancellation of 5¾% bonds due October 1, 1969 held by Securities Investment Account.

(6) Includes $70 million of Canadian National Railway Company 2⅞% bonds due September 15, 1969 and cancellation of $50 million 5½% bonds due October 1, 1969 held by Securities Investment Account.

(7) Exchangeable into 8% bond maturing October 1, 1986.

(8) Cancellation by Purchase Funds of the following Canadian National Railway bonds: $3.7 million of 5½% Dec./71; $1.7 million of 5% May/77; $2.0 million of 5¾% Jan./85; $3.5 million of 5% Oct./87.

Canadian Balance of International Payments

SUMMARY

The current account deficit in Canada's balance of payments widened in 1969 despite the continued rapid growth in world trade and the slowing in the growth of domestic demand after the first quarter. Major industrial disputes in Canada substantially reduced exports through much of the year, in contrast to the situation in 1968 and early 1969 when exports were boosted by abnormal demands resulting from strikes in the United States. Other factors which adversely affected exports in 1969 were the slowing of business expansion in the United States and the depressed state of the world wheat market. Imports, on the other hand, were at a substantially higher level in 1969, although they grew very little after the first quarter of the year. There was also an appreciable increase in the net deficit arising from tourist expenditures. The outcome was an increase in the current account deficit to about $725 million from the unusually low level of $60 million in 1968. There was a small reduction in the deficit with the United States but a large decrease in the surplus with other countries, notably Britain and Japan. The financing of the deficit in 1969 was facilitated by a continued substantial inflow of long-term capital, arising mainly from the sale of Canadian bonds in the United States and Germany, and by a marked shift in Canadian investor preference in favour of Canadian over American equities. The long-term inflows were sufficient to cover both the deficit on current account and a large net outflow of short-term funds and to permit a slight increase in official international reserves in 1969.

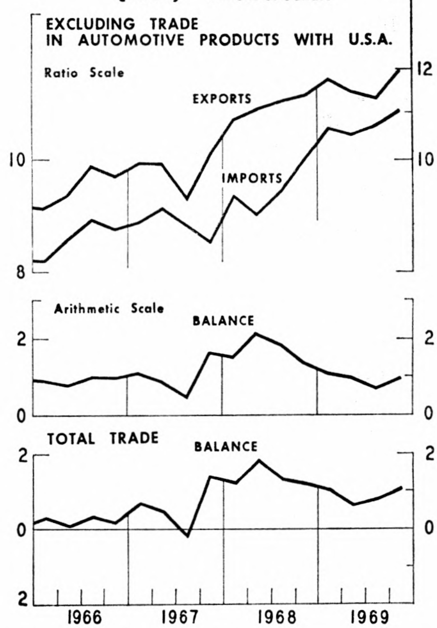
CURRENT ACCOUNT

Canada's merchandise exports rose by 10 per cent from 1968 to 1969, while imports rose by 15 per cent. Rapidly rising trade in automotive products with the United States again made a substantial contribution to the growth in both exports and imports, as they have done every year since the signing of the Canadian-United States automotive agreement in 1965. Excluding this trade, exports rose by 4½ per cent compared to 13½ per cent in 1968. There was, in fact, little or no increase in the volume of these exports in 1969 since there was an appreciable rise in prices, particularly for a number of key industrial materials. The growth in exports was depressed in the second and third quarters of 1969, mainly by strike disruptions and declining wheat sales, but was resumed in the final quarter.

Labour disputes have distorted the pattern of our trade, particularly with the United States, over much of the past two years. United States demand for Canadian copper, aluminum, iron and steel was boosted in late 1967 and the first half of 1968 by strikes or the threat of strikes in that country. In early 1969 some United States demand for imports was probably diverted to Canada because of dock strikes in the United States. During the last three quarters of 1969 strikes of varying duration in Canada sharply reduced exports of iron ore, steel, nickel and shipments of commodities through British Columbia ports. Partly in consequence, non-automotive exports to the United States rose by only 8 per cent in 1969 compared with a 17 per cent increase in 1968. While it is difficult to measure the effects of the strikes on trade, it does appear that the growth in exports to the United States of goods not so affected was fairly well maintained considering the slowing of the expansion in that country's economy.

MERCHANDISE TRADE

Quarterly — Billions of Dollars



Seasonally adjusted at annual rates.

Exports to overseas countries declined slightly in 1969. Shipments of wheat and flour fell by nearly 30 per cent; sales to most major markets were moderately lower, but the greatest part of the decline was in exports to the Soviet Union and to China. The recent signing of new contracts with these two countries assures some recovery in wheat shipments in 1970. Exports of commodities other than wheat rose less rapidly than in 1968. Shipments to Britain declined, although that country's total imports were higher in 1969, and sales to other overseas markets increased by 10 per cent, somewhat less rapidly than in 1968; these changes were attributable in part to the strikes. Canada's share of the market in Continental Europe appears to have been maintained, but our share of the rapidly expanding Japanese market fell.

The value of merchandise imports excluding United States automotive products increased by 14 per cent in 1969 following a 7 per cent increase in 1968.

MERCHANDISE TRADE[1]

(millions of dollars)

	1967	1968	1969
Exports			
To the United States			
Automotive products	1,544	2,410	3,265
Other products	5,733	6,706	7,235
Total	7,277	9,116	10,500
To other countries			
Wheat	776	745	536
Other products	3,285	3,677	3,850
Total	4,061	4,422	4,386
Total	11,338	13,538	14,886
Imports			
From the United States			
Automotive products	1,977	2,748	3,298
Other products	5,869	6,119	6,811
Total	7,846	8,867	10,109
From other countries			
Total	2,926	3,295	3,909
Total	10,772	12,162	14,018
Balance			
With the United States			
Automotive products	– 433	– 338	– 33
Other products	– 136	587	424
Total	– 569	249	391
With other countries			
Wheat	776	745	536
Other products	359	382	– 59
Total	1,135	1,127	477
Total	566	1,376	868

(1) Balance of payments basis.

However, much of the larger annual increase reflected the rapid growth up to the first quarter of 1969; there was little net increase thereafter, despite the continued upward movement in import prices to a fourth quarter level some 4 per cent to 5 per cent higher than a year earlier. For the year as a whole, imports from the United States rose by 11½ per cent while imports from overseas countries rose by 18½ per cent. The largest increase in total imports occurred in capital goods in response to rising business investment; there were also substantial increases in most other categories of imports, including automobiles from overseas countries and steel during the strike in that industry. Imports were also encouraged by the scheduled reduction in tariffs under the Kennedy Round at the beginning of the year and by the accelerated reduction announced in June as an anti-inflationary measure.

The surplus on Canada's merchandise trade fell by about $500 million from 1968 to 1969. The trade balance with the United States, which had strengthened by about $800 million in 1968, improved by a further $140 million in 1969. The change in 1969 was more than accounted for by a reduction in Canada's trade deficit on automotive products. Our trade surplus with other countries, which had exceeded $1 billion a year since 1963, dropped by $650 million in 1969. Of this decline, over $200 million resulted from lower wheat shipments. The remaining $450 million was due chiefly to the large increases in imports already noted; about half of this decline was with Britain and the rest was virtually all with Japan, other Asian countries and Australia.

The deficit on non-merchandise transactions rose by about $150 million from 1968 to 1969 to nearly $1,600 million. This was more than accounted for by a large increase in the deficit on travel account from about $25 million in 1968 to $200 million in 1969. Expenditures by Canadians travelling abroad increased by 26 per cent while the expenditures of foreigners in Canada rose by only 9 per cent. The net deficit on interest and dividend account remained at about $950 million in 1969; an unusually large increase in receipts last year was large enough to match the increase in payments.

CURRENT ACCOUNT OF THE BALANCE OF PAYMENTS

(millions of dollars)

	1967	1968	1969
With the United States			
Merchandise trade balance	– 569	249	391
Non-merchandise trade balance	– 773	–1,041	–1,101
Current account balance	–1,342	– 792	– 710
With other countries			
Merchandise trade balance	1,135	1,127	477
Non-merchandise trade balance	– 292	– 395	– 489
Current account balance	843	732	– 12
of which:			
with Britain	512	478	263
OECD Europe	– 153	– 249	– 344
other countries	484	503	69
Total current account balance	– 499	– 60	– 722

As a result of these developments in merchandise and non-merchandise trade Canada's current account deficit, which had declined from $500 million in 1967 to $60 million in 1968, rose again to about $725 million in 1969. All of the increase last year was in our transactions with overseas countries, a consequence not only of the drop in the trade surplus but also of an increase in the non-merchandise deficit of $100 million. Almost all of the widening in the non-merchandise deficit was due to sharply increased Canadian tourist expenditures overseas.

CAPITAL ACCOUNT

The published estimates in the table below indicate that the net inflow of capital in long-term forms rose sufficiently in 1969 to finance a larger current account deficit and a larger net outflow of short-term capital and to provide a small increase in reserves.

FINANCING OF THE CURRENT ACCOUNT DEFICIT

(millions of dollars)

	1967	1968	1969
Current account deficit	− 499	− 60	− 722
Capital flows			
Long-term capital	1,347	1,590	2,162
Short-term capital	− 828	−1,181	−1,375
Total	519	409	787
Increase in official international reserves	20	349	65

Most of the increase in net long-term capital inflows was the result of Canadian investors switching from heavy buying of foreign securities in 1968, mainly United States common stocks, to net selling in 1969. Sales of Canadian stocks to non-residents were substantial for the year as a whole, but they were largely concentrated in the first half of the year. Foreign direct investment in Canada remained at about the 1968 level but Canadian direct investment in the United States rose appreciably.

Sales of new Canadian bond issues to non-residents were the most important channel for long-term capital inflows again in 1969. Placements of securities in Europe, chiefly bonds denominated in German marks, were large during the first three quarters of the year when considerations of both price and availability made this market attractive to Canadian borrowers, but towards the end

LONG-TERM CAPITAL FLOWS

(millions of dollars)

	1967	1968	1969
Direct investment: in Canada	691	610	625
abroad	– 125	– 135	– 255
Canadian stocks: net new issues	36	60	196
trade in outstandings	12	112	61
total	48	172	257
Canadian bonds: gross new issues	1,270	1,872	1,861
retirements	– 356	– 394	– 374
trade in outstandings	– 57	– 69	1
total	857	1,409	1,488
Foreign securities	– 432	– 468	96
All other long-term capital	308	2	– 49
Total long-term capital	1,347	1,590	2,162

of the year they dropped off. For the year as a whole, placements by borrowers other than the Government of Canada reached about $525 million, $200 million more than in 1968. During the first part of 1969 costs to some Canadian issuers of long-term bonds were lower in the United States than in Canada and Canadian borrowers raised substantial amounts in New York. Late in the year, when

GROSS NEW ISSUES OF CANADIAN BONDS SOLD TO NON-RESIDENTS

(millions of dollars)

	1967	1968	1969
To United States residents			
Government of Canada	4	94	22
Other borrowers	1,210	1,261	1,300
Total	1,214	1,355	1,322
To other non-residents			
Government of Canada	16	196	12
Other borrowers	40	321	527
Total	56	517	539
Total	1,270	1,872	1,861

costs of new borrowing in the United States market rose more rapidly than in Canada, Canadian sales declined somewhat though some borrowers still chose to borrow in the United States even at rates similar to or higher than those in Canada because funds were more readily available there.

Short-term capital outflows in 1969 were nearly $200 million larger than in 1968. Very high interest rates offered for funds placed on deposit in the United States and Europe attracted a heavy volume of short-term capital from Canada. On the other hand, yields on hedged short-term finance company paper in Canada were appreciably higher than those on comparable investments in the United States, and non-residents increased their holdings of this type of Canadian paper. The balancing item in the balance of payments statistics, which is the difference between the direct estimates of the current and capital accounts, is included with other short-term capital outflows although it may represent unidentified net current payments or unidentified long-term capital outflows; unidentified net payments to non-residents were very large in 1967 and 1968 but were much smaller in 1969.

SHORT-TERM CAPITAL FLOWS

(millions of dollars)

	1967	1968	1969
Canadian treasury bills and short-term paper	− 39	− 80	248
Resident holdings of foreign bank balances and other short-term funds abroad	−284	− 409	−1,609
All other short-term capital (including balancing item)	−505	− 692	− 14
Total short-term capital	−828	−1,181	−1,375

One of the main channels for the international flow of short-term capital is the foreign currency operations of the Canadian chartered banks. The banks' net foreign currency liabilities to Canadian residents rose by over $1,000 million in 1969, mainly through a rapid build-up of "swapped" deposits in response to the very sharp rise in external interest rates; this build-up of "swapped" deposits was halted by the temporary ceiling arranged in July. The banks' foreign currency claims on non-residents, chiefly in the United States, rose by $500 million and there was a $500 million reduction in their own net foreign currency positions.

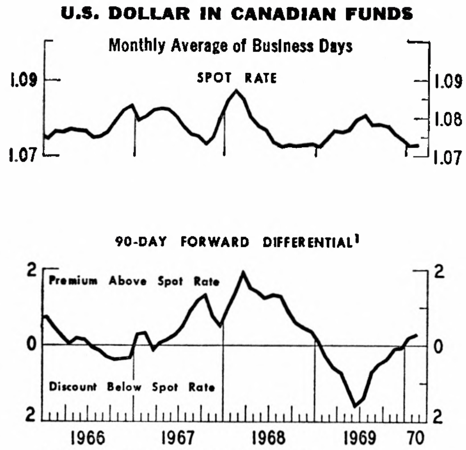
CANADIAN CHARTERED BANKS
HEAD OFFICES AND BRANCHES IN CANADA
NET CHANGES IN FOREIGN CURRENCY ASSETS AND LIABILITIES

(millions of dollars)

	1967	1968	1969	Feb. 1968 to Dec. 1969
With non-residents				
United States residents				
Assets	264	137	811	1,128
Liabilities	75	−302	338	151
Net	189	438	473	977
Other non-residents				
Assets	330	624	1,401	1,893
Liabilities	153	687	1,356	2,041
Net	177	− 63	45	− 148
Total				
Assets	594	761	2,213	3,021
Liabilities	228	385	1,694	2,192
Net claims on non-residents	366	375	519	829
With Canadian residents				
Assets	−112	− 54	214	136
Liabilities	332	85	1,246	1,278
Net	−444	−139	−1,033	−1,142
Chartered banks' own net position	− 78	236	− 514	− 312

The chartered banks continued to operate under the guidelines issued in the spring of 1968 which were designed to ensure that their foreign currency operations would not provide a channel for the flow of funds from Canada or the United States to other countries. The data in the final column of the table above show that at the end of 1969 the banks had borrowed $148 million more than they had invested in overseas countries since the reference date for the guidelines, February 29, 1968.

Demand for Canadian dollars in the foreign exchange markets remained strong in 1969. The spot rate for the U.S. dollar in Canada fluctuated close to the bottom of the permitted range at the start of the year, drifted up to



1. Expressed as a per cent per annum.

the parity level in the early summer and moved down to close to the bottom of the range again by year-end. The forward exchange rate for the U.S. dollar in Canada was at a very small premium at the beginning of the year but moved to a substantial discount around mid-year. The discount on 90-day forward U.S. dollars reached a peak yield of 1.89 per cent per annum in June. Thereafter, as the spot rate on the U.S. dollar declined the forward discount narrowed and in early 1970 the forward rate was at a small premium again.

Canada's official international reserves were recently redefined by the Minister of Finance to include (in addition to gold and U.S. dollars) other convertible currencies, Canada's reserve position in the International Monetary Fund and Special Drawing Rights. On January 1, 1970 Canada received Special Drawing Rights valued at U.S. $124.3 million as its share in the first creation of SDRs and during January and February additional SDRs amounting to U.S. $8.0 million were transferred to Canada.

OFFICIAL INTERNATIONAL RESERVES
(month-ends, millions of U.S. dollars)

	Dec. 1967	Dec. 1968	Dec. 1969	Feb. 1970
Foreign currencies				
U.S. dollars	1,255.2	1,964.9	1,743.6	1,898.3
Other currencies	13.4	11.6	12.3	12.8
Gold	1,014.9	863.1	872.3	879.1
Special Drawing Rights	–	–	–	132.3
Reserve position in the IMF	433.4	206.2	478.1	501.4
Total official international reserves	2,716.9	3,045.8	3,106.3	3,423.9

APPENDIX TABLE I

BANK OF CANADA NET TRANSACTIONS IN GOVERNMENT OF CANADA SECURITIES IN 1969

(delivered basis — par value in millions of dollars)

	Net purchases from (+) or net sales to (−) investment dealers and banks						
		Bonds[1]					
	Treasury bills	3 years & under	3 years to 5	5 years to 10	Over 10 years	Sub-total bills and bonds	Securities under PRA
Jan.	− 15	− 1	–	–	–	− 16	–
Feb.	−106	–	–	–	–	−106	–
Mar.	+ 6	–	–	–	–	+ 6	–
Apr.	+ 26	+ 54	−37	–	–	+ 43	–
May	− 48	+ 40	+19	+11	–	+ 23	–
June	+ 14	+ 8	–	–	–	+ 21	+32
July	+ 40	+ 22	–	−11	–	+ 51	−27
Aug.	–	+ 9	–	− 3	–	+ 6	− 5
Sept.	+ 49	–	–	–	–	+ 49	–
Oct.	+ 26	− 12	+ 2	–	–	+ 16	+38
Nov.	+ 36	–	–	–	–	+ 36	−38
Dec.	+ 44	–	–	–	–	+ 44	+37
Total	+ 71	+120	−16	− 4	–	+172	+37

(1) Classified by years to maturity at time of transaction.

Net transactions with Government and other client accounts						Net change in holdings of Government of Canada securities		
Purchases (+) of new issues less matured holdings		Net purchases from (+) or net sales to (−)						
		Securities investment acct.		Other Government and client accounts				
bills	bonds	bills	bonds	bills	bonds	bills	bonds	total
+ 49	− 2	−20	–	− 48	− 2	− 33	− 6	− 39
+ 34	–	+20	− 40	− 25	− 1	− 77	− 41	−117
+ 26	–	–	+ 40	− 22	− 1	+ 9	+ 39	+ 48
+ 56	+ 99	–	− 75	− 29	− 5	+ 53	+ 36	+ 88
− 19	–	–	–	− 45	− 3	−112	+ 67	− 45
+ 19	–	–	–	− 43	− 3	+ 15	+ 11	+ 25
+ 74	− 20	–	–	− 30	−14	+ 60	− 26	+ 34
+ 35	+ 75	–	− 75	− 32	− 1	+ 2	+ 1	+ 3
+ 9	–	–	–	− 25	− 2	+ 33	− 2	+ 31
− 77	+ 11	–	–	− 37	− 4	− 57	+ 4	− 53
+102	–	–	–	− 48	− 3	+ 58	− 10	+ 49
+ 44	+ 48	–	–	− 24	− 4	+ 76	+ 69	+145
+351	+212	–	−150	−407	−43	+ 27	+144	+170

APPENDIX TABLE II

BANK OF CANADA ASSETS AND LIABILITIES

(monthly changes — millions of dollars)

	Government of Canada securities at book value	Net foreign currency assets	Investment in IDB	All other assets (net)	Note circulation	Canadian dollar deposit liabilities		
						Chartered banks	Government of Canada	Other
1969								
Jan.	−37	−3	+4	−43	−230	−13	+158	+6
Feb.	−116	–	+2	+15	−4	−1	−86	−8
Mar.	+49	–	–	−112	+57	−65	−53	−1
Apr.	+89	+21	+8	+35	+59	+33	+61	−1
May	−44	+32	+1	+63	+28	+39	−34	+20
June	+24	+55	+4	−10	+113	−13	−20	−7
July	+34	−1	+4	−21	+26	−21	+21	−9
Aug.	+4	−1	+3	+13	−18	+46	−9	–
Sept.	+32	−7	+1	−30	−17	−26	+39	−1
Oct.	−52	−23	+12	+59	−9	+23	−21	+4
Nov.	+45	−41	+3	−76	+29	–	−93	−4
Dec.	+144	+25	+6	+75	+182	−8	+72	+3
Total	+173	+59	+49	−32	+217	−6	+33	+4

APPENDIX TABLE III

GOVERNMENT OF CANADA FINANCIAL ACCOUNTS

(millions of dollars)

	Calendar 1967	Calendar 1968	Calendar 1969
1. Budgetary surplus (—) or deficit	678	732	−609
Adjustments for national accounts basis:			
Funds borrowed (—) from:			
Public service superannuation accounts	−432	−508	−591
Unemployment insurance and old age security funds	−119	− 87	−131
All other adjustments to national accounts basis (net)	129	28	731e
2. National accounts basis surplus (—) or deficit	256	165	−600e
3. Increase in major loans and advances to:			
Central Mortgage and Housing Corporation	678	394	468
Farm Credit Corporation	168	131	96
CNR (incl. Air Canada, excl. debt refunding)	124	130	116
Export Development Corporation	28	42	35
Municipal Development and Loan Fund	66	7	− 7
Veterans' Land Act Fund	60	51	55
1967 World Exhibition (incl. guaranteed notes)	68	8	–
National governments	− 13	61	37
Provincial governments	10	61	23
Other	46	46	40
Sub-total	1,235	931	863
4. Canadian dollars required to finance increase in Government's foreign currency assets (or reduction in liabilities):			
Advances to the Exchange Fund	147	529	−207
Holdings of IBRD and Columbia River Treaty bonds	− 12	− 78	− 32
Subscriptions and advances to international agencies	19	30	30
Foreign-pay securities (outside Gov't accounts)	45	−266	− 14
Demand notes payable to international agencies	2	−229	229
Sub-total	201	− 14	6
5. Funds required for net increase in other assets or reduction in other liabilities(1):			
Refundable corporation tax	−106	82	110
Excess of accrued corporation income tax over collections(2)	−175	56	−759
All other assets and liabilities	−135	−171	− 19e
Sub-total	−416	− 33	−668e
6. Total Canadian dollar financing requirements (sum of items 2, 3, 4 and 5)	1,276	1,049	−399
7. Total Canadian dollar financing requirements were met by:			
Increase (+) in Canadian dollar securities outside Government accounts	978	1,109	276
Reduction (+) in Canadian dollar cash balances	298	− 60	−675
Total (= Item 6)	1,276	1,049	−399

e: Estimate.

(1) Apart from those shown in Item 7.

(2) A contra amount is included in "All other adjustments to national accounts basis (net)" shown in Item 1.

BANK OF CANADA STATEMENT OF INCOME AND EXPENSES

(thousands of dollars)

	1969	1968
Income		
On investments (including deposits)	247,223	203,323
All other income	227	179
Total income	247,450	203,502
Operating Expenses		
Salaries(1)	6,899	6,297
Bank contributions to pension and insurance funds	715	542
Other staff expenses(2)	469	427
Directors' fees	27	30
Auditors' fees and expenses	104	85
Taxes (municipal and business)	1,377	1,306
RCMP guards and electric protection	265	225
Bank note costs	5,043	4,939
Data processing and computer costs	425	344
Other equipment and premises (net)	979	706
Printing of publications	125	107
Other printing and stationery	265	292
Postage and express	269	259
Telephones and telegrams	246	219
Travel and transfer expense	247	206
Interest paid on unclaimed balances	75	68
All other expenses	270	297
Total operating expenses	17,800	16,349
Depreciation on Buildings and Equipment	915	998
Net Income Paid to Receiver General for Canada	228,735	186,155
	247,450	203,502

(1) The number of staff averaged 1,065 in 1969 and 1,045 in 1968.
(2) Includes overtime pay, medical services and cafeteria expense.

ASSETS

	1969	1968
Deposits payable in foreign currencies		
Pounds sterling and U.S.A. dollars	$ 79,134,263	$ 95,765,052
Other currencies	246,712	156,521
	79,380,975	95,921,573
Cheques on other banks	88,924,104	152,236,827
Advances to chartered and savings banks	900,000	5,000,000
Accrued interest on investments	60,416,497	50,940,327
Bills bought in open market, not including treasury bills, at cost	2,580,060	–
Investments — at amortized values		
Treasury bills of Canada	477,687,278	453,368,678
Other securities issued or guaranteed by Canada maturing within three years	1,929,645,504	1,540,915,405
Other securities issued or guaranteed by Canada not maturing within three years	1,650,476,290	1,890,338,307
Debentures issued by Industrial Development Bank — Note	351,344,159	305,041,830
Securities issued by the United Kingdom and the United States of America	81,232,760	10,752,213
	4,490,385,991	4,200,416,433
Industrial Development Bank		
Total issued share capital at cost — Note	52,000,000	49,000,000
Bank premises		
Land, buildings and equipment Cost less accumulated depreciation	24,152,007	22,150,087
Net balance of Government of Canada collections and payments in process of settlement	88,164,836	58,183,461
Other assets	1,401,355	1,716,238
	$4,888,305,825	$4,635,564,946

Note: The audited financial statements of the Industrial Development Bank as of September 30, 1969 show an equity of $71,740,093 at which date the Bank of Canada's investment was $51,000,000.

L. RASMINSKY, Governor
Ottawa, January 26, 1970

A. J. NORTON, Chief Accountant

AS AT DECEMBER 31, 1969
(with comparative figures as at December 31, 1968)

LIABILITIES

	1969	1968
Capital paid up	$ 5,000,000	$ 5,000,000
Rest fund	25,000,000	25,000,000
Notes in circulation	3,446,175,525	3,229,211,295
Deposits		
Government of Canada	80,930,542	47,447,900
Chartered banks	1,108,815,234	1,114,326,553
Other	42,030,347	38,380,403
	1,231,776,123	1,200,154,856
Liabilities payable in foreign currencies		
To Government of Canada	22,688,142	26,983,626
To others	953,270	1,301,224
	23,641,412	28,284,850
Bank of Canada cheques outstanding	155,021,597	146,459,854
Other liabilities	1,691,168	1,454,091
	$4,888,305,825	$4,635,564,946

Auditors' Report • We have examined the statement of assets and liabilities of the Bank of Canada as at December 31, 1969. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances. In our opinion the accompanying statement of assets and liabilities presents fairly the financial position of the Bank as at December 31, 1969.

JACQUES RENÉ DE COTRET, C.A.
of René de Cotret & Cie.

T. C. KINNEAR, F.C.A.
of Price Waterhouse & Co.

Board of Directors

L. Rasminsky, C.C., C.B.E.	*OTTAWA* *Governor* *Member of the Executive Committee*
J. R. Beattie	*OTTAWA* *Deputy Governor* *Member of the Executive Committee*
A. I. Barrow, C.A., R.I.A.	*HALIFAX, N.S.*
E. G. Byrne, Q.C.	*BATHURST, N.B.*
S. E. Green	*CHARLOTTETOWN, P.E.I.*
S. Kanee	*WINNIPEG, MAN.*
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J. L. Lewtas, Q.C.	*TORONTO, ONT.*
W. A. Mackintosh, C.C.	*KINGSTON, ONT.* *Member of the Executive Committee*
D. F. Matheson	*YORKTON, SASK.*
L. Patrick, C.B.E.	*CALGARY, ALTA.*
Maurice Riel, Q.C.	*MONTREAL, QUE.*
J. Taschereau	*QUEBEC, QUE.* *Member of the Executive Committee*
A. Walton	*VANCOUVER, B.C.*

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R. B. MCKIBBIN, *Deputy Governor* — L. HÉBERT, *Deputy Governor*
R. W. LAWSON, *Deputy Governor* — G. K. BOUEY, *Deputy Governor*
B. J. DRABBLE, *Adviser*

L. F. MUNDY, *Director of Administrative Operations*
G. HAMILTON, *Secretary*
R. F. HIRSCH, *Auditor* — A. J. NORTON, *Chief Accountant*

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P. D. SMITH, *Associate Secretary* — C. H. RICHARDSON, *Deputy Secretary*
I. G. L. FREETH, *Chief of Computer Services*
E. L. JOHNSON, *Personnel Officer* — MISS M. K. ROWLAND, *Personnel Officer*
S. S. CARROLL, *Curator, Numismatic Collection*

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R. F. ARCHAMBAULT, *Deputy Chief* — S. V. SUGGETT, *Special Assistant*
E. B. HODGE, *Superintendent of Premises*

Currency Division: H. F. BUTLER, *Chief*
T. D. MACKAY, *Deputy Chief*

Public Debt Division: H. W. THOMPSON, *Chief*
A. ROUSSEAU, *Assistant Chief*

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G. S. WATTS, *Research Adviser*
W. A. MCKAY, *Assistant Chief* — MISS E. M. WHYTE, *Assistant Chief*
D. B. BAIN, *Administrative Assistant* — T. I. NORTON, *Special Assistant*
MISS D. J. POWELL, *Special Assistant* — P. R. ANDERSEN, *Research Officer*
J. E. H. CONDER, *Research Officer* — A. G. KEITH, *Research Officer*
A. C. LAMB, *Research Officer* — G. G. THIESSEN, *Research Officer*
J. S. VACHON, *Research Officer* — C. E. STRIKE, *Graphics Officer*
MISS H. COSTELLO, *Librarian*

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A. CLARK, *Deputy Chief* — J. M. ANDREWS, *Deputy Chief*
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J. A. J. BUSSIÈRES, *Assistant Chief* — D. G. M. BENNETT, *Assistant Chief*
R. C. PAGE, *Securities Officer* — C. G. PERRY, *Securities Officer*
V. O'REGAN, *Securities Officer*

Toronto Division
J. T. BAXTER, *Chief*
J. KIERSTEAD, *Securities Officer*

Montreal Division
T. G. BOLAND, *Chief*
J. E. J. CLÉMENT, *Deputy Chief*

F. FAURE, *Vancouver Representative*

FOREIGN EXCHANGE DEPARTMENT

A. M. JUBINVILLE, *Chief*
A. C. LORD, *Deputy Chief* — A. F. PIPHER, *Foreign Exchange Adviser*

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SAINT JOHN, N.B.	J. C. Fraser, *Agent*
MONTREAL	J. E. R. Rochefort, *Agent* R. Marcotte, *Assistant Agent*
OTTAWA	J. K. Ferguson, *Agent*
TORONTO	R. J. Lillie, *Agent* D. D. Norwich, *Assistant Agent*
WINNIPEG	L. G. Rowe, *Agent*
REGINA	J. F. Smith, *Agent*
CALGARY	W. H. Pyatt, *Agent*
VANCOUVER	J. C. Nesbitt, *Agent*