These report on initial negotiated settlements of base rates. The rates do not include the effects of COLA (cost-of-living allowance) clauses. Moreover, many of them are still subject to AIB decisions. The data show that the rates of increase proposed in the first year of new collective agreements have come down to 13.4 per cent in the settlements in the second quarter of 1976, compared with 21.8 per cent in the first nine months of 1975. The average increase in negotiated base rates in these data, for all contracts currently in force, was 12 per cent in the second quarter of 1976, compared with 13.8 per cent during the first nine months of 1975.

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Profits

In the first half of 1976, profits before taxes were actually lower than in the second half of 1975 and only 5.5 per cent above the level of the first half of 1975. This increase compares with an increase of 16.4 per cent for labour income. The share of profits in the GNP has therefore fallen. Many firms have been reporting revenues below the levels allowable under the program, either because of market conditions or because of the wish of firms to ensure that their pricing decisions were in conformity with the regulations.

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Rents

All the provinces now have implemented rent-control systems and rent review or appeal panels. Guidelines for maximum yearly increases, ranging from 8 to 10.6 per cent, exist in eight provinces. Two provinces have guidelines with no specified maximum rent increases. All but one of the provinces exempt new housing from control for some initial period. Since the implementation of the provincial rent-control measures, the average rate of rent increases has slowed. The rent component of the CPI increased at an annual rate of 8.4 per cent in the six months prior to the initiation of the anti-inflation program. In the latest six-month period the rate of increase declined to 5.2 per cent.

It appears certain that the increase in the CPI in the year ending October 1976, will be less than the target of 8 per cent....

The current goal for the second year of the program is to reduce inflation to 6 per cent....

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Government spending

The key to our fiscal strategy is restraint on government spending. The Government's targets have been set out clearly and specifically. In launching the anti-inflation program, the Government's white paper stated that the trend of expenditure growth should be no higher than the trend of the gross national product. The budget of May 25 stated: "Based upon planned total outlays of $42,150 million, our target rate of increase for this fiscal year works out at about 14 per cent. Our forward planning for 1977-78 is based on a growth rate of the order of 11 per cent. For both 1976-77 and 1977-78, these increases are less than the expected growth of GNP."

The targets, which leave little room for real growth in the spending of the Government, still stand. They will be achieved only with the greatest persistence and perseverance. Only the most essential of the many proposals for desirable new programs can be considered....

In my May budget speech, I indicated that real growth in the national economy in 1976 would be about 5 per cent. This continues to be my expectation.

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Price and profit guides

We have examined various modifications of the pricing and productivity rules. It has proved extremely difficult to structure them in such a way to ensure that the benefits accrue only to those firms which have in fact improved their productivity or held their costs down by the pursuit of economies. Those firms which are not in a position to benefit would feel that they have been treated inequitably. The attempt to tailor such provisions more specifically to a particular target group threatens to build more complexity into an already complicated program.

I have, therefore, decided to approach this whole set of problems connected with incentives in a different way. The proposed pricing and productivity rules for firms under Part 1 of the guidelines will not be introduced. In their place, I propose an investment credit for such firms. Eligible investments will be defined for this purpose in the same way as for the present investment credit in the tax system, with some additional categories. Firms engaging in such investment in Canada will be able to deduct 50 per cent of the value of such investment from excess revenue up to a maximum amount of 10 per cent of allowable profits. This credit will be available against non-distribution profits, as was the case in the pricing and productivity rules which it replaces. It will provide such firms with a general incentive to increase productivity in the competitive circumstances we anticipate over the life of the program and with the opportunity of earning additional funds to finance their investment, while maintaining the necessary degree of restraint on prices.

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The main features of the new price and profit regulations may be summarized as follows....

(1) All firms will be subject to a net margin test.

(2) All firms will be able to choose as a base period either the five fiscal years prior to October 14, 1975 or the most recent fiscal year ended prior to May 1, 1976.

(3) Firms in the non-distribution sector will be required to limit their net pre-tax profits as a percentage of sales to 85 per cent of the base period margin. Firms in the distribution sector will be required to meet a similar net margin test of 95 per cent.

(4) While no test will apply at the level of the product line, firms will be expected to price individual products in a manner which bears a reasonable relationship to the costs of producing them. The Board will continue to obtain the information it needs and will have the power to request reductions in price increases on individual products where they are clearly disproportionate to the increases in related costs.

(5) All firms will be permitted to earn a minimum rate of return of 8 per cent on their equity, regardless of their base period experience.

(6) A new investment credit will be provided. This will enable firms in the non-distribution sector to deduct from excess revenue one-half of their expenditures on a wide range of new investments in Canada, up to a maximum of 10 per cent of allowable earnings.

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