CANADA-U.S. FINANCIAL RELATIONS

(Continued from P. 2)

financial authorities in this country (the Bank of Canada and the Department of Finance) – that, in the present state of the economy, it was not desirable to rely too heavily on general monetary and financial measures to control the inflow of capital and a more specific instrument of control might be needed.

REDUCING OF LIABILITIES IN U.S.

I therefore told Mr. Fowler, the Secretary of the Treasury in the United States, when I was Acting Minister of Finance, that the Canadian Government would be prepared, if necessary, to buy outstanding Canadian securities held in the United States, to offset any excess flow of U.S. capital to Canada and thus to maintain the net flow of capital at the level required to finance our balance-of-payments deficit. Instead of adding to U.S. assets in our exchange reserves, we should be reducing Canada's liabilities in the United States. Conversely, if the volume of borrowing by other Canadians were not sufficient to meet the balance-of-payments needs, the Government would itself arrange to borrow in the United States. In this way, our reserves could be maintained at around the desired level without interfering either with trade or with the normal use of the U.S. long-term capital markets by Canadian borrowers. I also agreed that, while our reserves must be expected to fluctuate from month to month, we should regard it as appropriate that such fluctuations take place around a level somewhat lower than the mid-1963 figure, say, approximately $2,600 million (U.S.).

Should it be necessary to borrow in the U.S., I should foresee no great difficulty in obtaining moderate amounts as and when we require them. On the other hand, I believe that there are sufficient Government of Canada securities held in the U.S. market to enable us to do what might be required in buying Canadian securities in the U.S. by using the authority to purchase our own securities that is already granted in the Financial Administration Act.

I should like to tell the House that, since the beginning of 1966, we have purchased about $40-million worth of our outstanding U.S. bonds that were held in the United States. Our purchase of these securities was consistent with the plan I have outlined but was also intended in considerable part to improve the market for the sale of other Canadian issues in the United States this month, when there appeared likely to be a large volume of such issues scheduled for delivery.

A GLOBAL RESTRICTION

The second important measure adopted by the U.S. in December was a voluntary ceiling on direct investment by United States corporations, of whom about 900 will be asked to report regularly on the progress of their co-operation with the United States administration. The guideline, and I will not take time now to give details, does not stipulate how any company shall distribute its direct investment among geographic areas. This is a global restriction. It does not apply to Canada particularly; it applies to the world. Where it is applied is a matter for the business organization itself to decide. Canada is not exempted from this ceiling or guideline as it was from the previous guideline applying to direct investment.

As soon as we learned of the new United States guidelines for direct investment we told them that, while it was very hard for us to assess what its effects on Canada would be because so much depended on the decisions of the businesses, we thought it would cut down some of the flow of such capital to Canada. In so far as it worked in reducing such flow of such capital direct investment it would simply mean a greater need for new issues of Canadian securities in the United States under the arrangements and exemptions provided for long-term issues. We felt that, from a U.S. point of view, there was no reason why the Canadian balance-of-payments deficit with the United States should not be financed by direct investment just as well as by the sale of new issues of securities. Consequently, it seemed to us there was no certainty that the effort to restrict direct investment in Canada would in fact help the U.S. balance of payments at all in the final result.

We also pointed out that the inclusion of retained earnings of subsidiary corporations in the figures used to determine the voluntary quotas for direct investment worked a particular hardship on Canada. U.S.-controlled companies form such a large part of Canadian industry and have been so long established in Canada that they must be regarded as a basic and substantial part of the Canadian economy.

On the basis of these arguments, we suggested that the United States should continue a special exemption for Canada in their guidelines on direct investment or, if they could not see their way clear to do that, they should permit the investment of retained earnings to be outside the quotas.

My understanding is that the American authorities considered the points we put forward, as they said they would, but came to the conclusion that the guideline on direct investment had to be relatively simple and without special exceptions if it was to be effective in meeting the aims of their general programme. They did assure us, however, that these guidelines would not affect in any way the expansion necessary to achieve the purposes of the Canada-United States automotive agreement.

This guideline on direct investment is intended to restrict the outflow of capital from the United States parent companies to branches and subsidiaries in other countries. There is nothing in these guidelines, so far as I can see (and this is an important point), that would prevent Canadian subsidiaries of United States companies from borrowing like other Canadian companies by means of long-term issues in the United States market.

PROJECTS POSSIBLY DELAYED

As I said when these guidelines were announced, they have come into effect at a time when capital investment by business in Canada has been increasing very rapidly and cannot be expected to go on increasing at the same rate. In some measure the restraints

(Over)