reserve position at the end of January indicated that Canadian reserves during the month had declined approximately $100 million (U.S.) after taking into account the drawing into our reserves of $250 million (U.S.) by the Bank of Canada through activation of part of its reciprocal credit facility with the Federal Reserve System.

In the early part of February, there was a period of further pressure on the Canadian dollar in the exchange market as the market reacted to the news of the changes in the reserves during January. Later, there was substantial pressure on the dollar again after the adverse vote on the Government's tax bill. The state of our reserves at the end of February... makes clear that there would have been a further reduction in our holdings of exchange that month had there not been an addition to the reserves secured by the drawing upon the International Monetary Fund. If we had not made this drawing, there would have been a reduction of $113 million (U.S.) in our gold and foreign-exchange holdings....

TRADE POSITION STRENGTHENED

In regard to concern over our competitive position, I would like to recall that our trade position last year was stronger than it has been for some years past, and that, by the end of the year, our trade surplus was running at its highest level in over a decade. Indeed, our overall current-account position on the balance of payments in 1967, which I am told will be published later this week, has been considerably stronger than for several years previously. While some of this strength derived from the extraordinary receipts that we obtained from tourist trade because of Expo 67, the net improvement on all our other current international transactions was nearly as large. We can reasonably expect that our current-account balance this year, though it is bound to widen, will still be better than it was in either of the two years before Expo. It will thus represent an improvement in relation to the average deficit of the last 12 years, both in absolute terms and more especially in relation to our now greatly enlarged national output and volume of international transactions.

The present exchange-rate of the Canadian dollar is appropriate to the situation of our economy. We are still experiencing the upward thrust in our economy which began seven years ago, and which has continued without serious interruption to the present. Our export performance has been good, especially in the past few months. Imports have not been increasing disproportionately. Our economy is not significantly under-utilized; indeed, it is still displaying some of the effects of excess demand pressure which had built up over the long expansion. In these circumstances, a lower exchange-rate would add to our inflationary problems by increasing the demand on Canadian production by foreigners and by reducing the use by Canadians of goods and services produced abroad. Domestic demand would have to be further restrained in order to offset the inflationary consequences of these reactions....

Honourable Members will recall that we enjoyed a long period of economic expansion from 1961 through the boom of 1966, when the economy reached capacity. In the latter part of that year and in 1967, the rate of growth slackened, particularly in business capital spending, while employment and production levelled off. We were confronted with the problem of keeping the economy on a stable growth path while pursuing our major economic objectives of full employment, stability of prices, a high rate of growth, a viable balance of payments and an equitable distribution of rising incomes.

PROBLEM OF COST-PRICE STABILITY

During last year, it emerged that our main problem was to achieve stability of prices and costs despite a lessening in the excessive aggregate demands upon our economic resources. We seemed, however, to be plagued by a cost-push type of inflation even after the demand-pull type had subsided. As we look ahead now, I think we shall find there is so much to be done in Canada that is worth doing that it doesn't seem likely that there will be a deficiency of aggregate demands over the next few years, but rather a need for managing that aggregate and assigning priorities to its various components so that we can have enough stability to permit sustainable growth.

In the three months since the budget statement of November 30, one of the most important economic factors has been the increasing evidence of rapid economic expansion in the United States. The pause which the American economy experienced in the first half of 1967 has been left behind. Business-capital investment is now expanding in that country and expenditures by consumers and governments are rising rapidly. There is, indeed, a real possibility of inflationary price and cost increases in the United States such as Canada experienced in the past two years, unless there is a tax increase or other forms of fiscal restraint.

In continental Europe, expansion is to be expected as well. The OECD is now forecasting a renewal of expansion in that area during 1968 at a rate of 3.5 per cent in real terms. The expansion for the whole OECD area including the U.S. and Japan is forecast at 4 to 4.5 per cent.

TRADE SURPLUS UP

These external developments are providing a good market for most Canadian exports. One of the most encouraging features of recent months has been the strong expansion of exports in November and again in December. They have shown strength in all major market areas. Despite the problems encountered in marketing wheat during the past year our merchandise trade surplus for 1967 was substantially higher than that for the two preceding prosperous years.

Industrial production in Canada showed substantial increases in November and December, led by the automotive industry and primary iron and steel. Unemployment has fluctuated narrowly around the 4.5 per-cent level after allowing for the usual seasonal pattern. Its increase during the past year up to this level has reflected, of course, a variety of factors, including, particularly, the failure of capital expenditures by businesses to expand during 1967.

(Continued on P. 5)