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## Current Economic Situation in Canada

The Canadian economy's performance was substantially better in 1985 than most observers anticipated. The May 1985 budget forecast growth in real gross national expenditure (GNE) of 3.1 percent in 1985, with employment growth of 2.1 percent and a decline in the unemployment rate to 10.7 percent by year-end. These views were similar to the average of then-current private sector forecasts. However, consumer and investor sentiment became much more optimistic as the year progressed. The optimism resulted from a number of developments: a significant decline in interest rates, a moderate and stable inflation rate, improving prospects for employment, and credible government measures to restore fiscal responsibility and encourage private sector initiative. Consequently, consumption, housing and business investment were all significantly stronger than expected and, as a result, real GNE growth in 1985 was 4.5 percent.

Canada has the highest rate of job creation in the OECD. Employment growth for the year was 2.8 percent, the strongest in over four years. The unemployment rate fell substantially in 1985 to reach 10 percent by December and then declined further this year to 9.8 percent in January and 9.6 percent in March. The Canadian economy showed strength in 1985 despite the weakness of the international economy, particularly in the USA. Real output increased in Canada last year at a faster pace than any other major industrial country except Japan and at nearly twice the pace of the USA and European countries.

While the 1985 economic performance extended the strong recovery that has occurred in Canada since the 1981-1982 recession, its nature and shape has changed substantially. During the first 1½ years of the recovery, final domestic demand in Canada accounted for less than half of real output growth, as exports and inventory changes provided the bulk of the rise in demand for Canadian goods and services. Employment growth, while strong, was typically concentrated in part-time employment, and all regions and sectors did not share equally in the increase of economic activity.

Last year, however, in sharp contrast, the marked recovery in business investment, surging housing expenditures and strong consumer spending on durable goods led to an economic expansion in Canada that is more domestically oriented and much more broadly based. Most sectors of the Canadian economy participated in the economic recovery in 1985. Employment growth shifted substantially towards full-time employment, and all regions of the country experienced gains in employment and declines in the unemployment rate.

After declining through most of 1985, interest rates rose around year-end and for most of early 1986, then declining again beginning in mid-March. Increases in interest rates were related to speculative pressure on the Canadian dollar which saw its value slide to a record low in the US\$0.71-0.72 range before stabilizing.

The rate of inflation, as measured by the CPI, was 4.0 percent in 1985, down from 4.4 percent in 1984. In February 1986, the rate of inflation was 4.1 percent. Wage settlements, at 3.5 percent, remained below the CPI rate of inflation, although the gap between the two shows signs of narrowing, largely as a result of the lower inflation rate. With productivity growth remaining strong at 1.6 percent, unit labour costs increased 2.4 percent in 1985.