External Affairs Canada | Affaires extérieures Canada

Statements and Speeches

No. 75/4

REVIEW OF CANADA'S ECONOMY IN 1974 and OUTLOOK FOR 1975

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Highlights of 1974

Almost alone among the industrialized countries of the world, Canada again achieved a significant rise in overall production and employment in 1974. The gross national product (GNP) in Canada increased by about 4 per cent in real terms compared to zero growth for OECD countries as a whole and a decline in output in the United States. Employment also rose by about 4 per cent.

In dollar terms, the GNP rose to nearly $140 billion, an increase of over 17 per cent. Much of this rise was accounted for by the high rates of inflation now facing the industrial world. While the rate of inflation in Canada was somewhat below the average of other industrial countries, it was still considerably above 1973 rates.

Much of the increase in output occurred as a result of rising industrial activity early in the year. In more recent months, the upward tempo in economic activity has slowed in response to the international economic climate.

This change to a slower pace followed more than three years of above-average rates of growth, during which the Canadian economy has operated at levels close to capacity.

Labour markets

Favourable business conditions supported a generally strong labour-market situation in 1974. Employment again rose faster than in most postwar years. There were about 350,000 additional jobs, representing an increase of about 4 per cent over 1973.

Despite this increase in jobs and a high job-vacancy rate, unemployment remained at about 5.5 per cent of the labour force, about the same rate as in 1973. The labour force continued to grow at an unusually high rate.

Major domestic demand influences

Canada's superior economic performance was due principally to the continued strength of domestic demand. A major stimulus was provided by a 21 percent increase in total capital investment, and more particularly a 38 percent increase in investment by manufacturing firms, which went largely to expand plant capacity and thus to eliminate shortages.

Residential construction was strong in the first half of 1974, but activity slackened perceptibly in the housing industry towar the end of the year because of sharply higher mortgage interest rates and a reduction in available mortgage credit in the privat sector.

Consumer expenditures maintained their upward trend, in part bec of a further advance in real disposable income *per capita*. Large price increases, particularly for food, had some limiting effect on the increase in consumer expenditures in real terms.

But, in sharp contrast to the situation in the United States, th volume of Canadian car sales was only a little lower that the record level set in 1973. Canadians also increased their spendir over the previous year for non-durable goods and consumer servic The demand for urban housing accommodation remains high even aft record rates of construction in each of the past three years.

Government expenditures continued to be a major stabilizing fact While rising quite strongly in dollar terms, government expendit on goods and services declined slightly as a proportion of the G

International influences

The international framework for the Canadian economy in 1974 has been one of increasing uncertainties. Because of the wholly chan oil-supply and -price situation, those major overseas countries dependent on imported oil for their energy needs have been faced with trade deficits of unprecedented magnitude.

Another problem has been the rate of inflation, which accelerate on a world-wide scale in 1974. The concerted effort by major inc trial countries to deal with inflation and contain their balance payments deficits has led to a sharp curtailment of economic gro and thus to reduced demand for Canadian exports.

The decline in industrial output in the United States has natura been of special concern to Canada. The exceptional weakness of automobile sales and of housing construction impinges particular on the automobile and lumber industries in Canada.

Nevertheless, world markets continued strong throughout most of year for many mineral products, and for most food products and capital goods.

Foreign trade

In dollar terms, Canada's exports rose by about 28 per cent over 1973 levels, to about $32 billion in 1974, an increase even lar in percentage terms than the record increase achieved in 1973. was mainly owing to large price increases in a number of Canada major commodity exports, such as wheat and other grains, petrol wood pulp, copper and zinc. The physical volume of Canada's total exports declined somewhat from 1973 levels.

Export sales to the United States, Canada's principal trading partner, increased in value by close to one-quarter, or about the same as in 1973. Again, this increase reflected higher prices only. In volume terms, Canadian exports to the United States declined, one of the few times that this has occurred in the period following the Second World War. The fall-off in this key market clearly reflects the current recession in the United States, and especially the weak United States market for new cars and houses.

Overseas markets have shown a larger percentage rise in Canadian export purchases than the United States, although economic slow-downs in several of the major industrial countries have meant that the actual volume has risen only slightly, if at all. Exports to Latin America have shown the largest increase on a percentage basis, followed by quite substantial gains in the value of exports to the European Economic Community, Japan and Commonwealth markets outside the United Kingdom. Canadian exports to the United Kingdom rose at a slower pace than those to any of our other principal markets.

Commodities contributing most to higher export values in the past year included wheat, copper, crude petroleum, natural gas, wood pulp, newsprint, fertilizers, petroleum and coal products and aluminum. Increases in the volume of exports were shown for such commodities as wood pulp, but most notably for machinery and equipment.

Continuing economic growth in Canada, although at a moderating pace, has sustained high import demand. The value of imports rose about one-third in 1974, to about $31 billion, reflecting a moderate increase in import volume and in import prices. There has been a major upward shift in the value of imports from oil-producing countries because of the tripling in oil-prices that has taken place since late in 1973.

The faster rise in imports than in exports has meant a decline in Canada's merchandise-trade surplus, to less than $1 billion in 1974 compared to a surplus of over $2 billion in 1973. Owing to the smaller trade surplus and a small increase in the "invisibles" deficit, Canada's current-account payments deficit with other countries has widened in 1974 to a total of somewhat under $2 billion from a total of less than one-half billion in the preceding year. This deficit is modest, however, compared with the huge imbalances incurred by most OECD countries in 1974.

Industrial trends

Despite a levelling-out in business trends following the opening

few months of the year, production of goods and services in 19
was again higher than in the previous year. The volume of indus
production was up between 3 and 4 per cent over 1973 levels, al
this was a reduction from the annual increases of about 8 per c
in each of the two preceding years. An important element in the
slower output rise was the extensive loss of production owing t
industrial disputes.

Earlier in the year, the industrial economy operated close to capacity. However, as the year progressed there were indicatio increasing slackness in several major industrial sectors, with offs and reduced hours of work more in evidence in the late fa than has been usual in the past two or three years.

Transportation-equipment industries remained close to the very tempo of activity reached in 1973. Motor-vehicle production fe only a little short of last year's 1.6 million units. While ou of passenger-cars was down slightly for the year, commercial vehicles showed a significant increase. There were also higher levels of production in the railway rolling-stock and shipbuil industries.

Continuing strength in business-capital investment bolstered activity in Canada's industrial- and electrical-equipment indu and in machinery manufacture. These sectors have shown solid i creases in 1974, and were sustaining high levels of activity a year drew to a close.

Owing to very high demand for steel in domestic and internatio markets primary steel production has again advanced and reache record level of almost 15 million tons for the year. Aluminum duction also showed a significant gain over 1973 levels.

In the non-durable sector of manufacturing, there were importa increases in production of chemicals, leather, fertilizers an petroleum and coal products.

Primary and resource industries have shown mixed trends over t past year. In general, market demands continued to be strong f pulp-and-paper products, and the industry operated at a higher of capacity than in 1973. The lumber and plywood sectors, on th other hand, have experienced slackening demand and falling pri for their products. Metal-mining and -processing industries (o than steel and aluminum), which were under great pressure of d last year, have also seen a falling-off in orders and a down-t in prices as a result of the economic slowdown in several majo industrial countries.

Canada's economic prospects in 1975

It is evident that the rate of economic growth in Canada has lost some of its earlier momentum in recent months following an extended period of rapid advance. At the same time, there are clear indications of considerable resilience in important domestic market demand sectors, which may be expected to support continuing real growth in 1975, although at a somewhat slower pace than in 1974. The Canadian economic performance is expected to continue to be superior to that of our principal trading partners, as it has been in the past year.

nternational factors

The principal threat to the growth of production and employment in Canada in 1975 comes from abroad. No matter what may be done by Canadian Governments to stimulate domestic demand, Canada, with its heavy dependence on sales to world markets, cannot fully escape the effects of an international recession.

The current expectations are that a widespread recovery in economic growth will not occur in Canada's major trading partners until well into 1975. Any major external stimulus to the Canadian economy will be similarly delayed.

The slack in world industrial economies suggests less-intense upward pressure on world prices in the coming year. Other factors indicating a modest slowing in inflation are the apparent elimination of most material shortages, a reasonable likelihood of better harvests, and the possibility of better productivity performance once world economies resume growth. These factors, together with the decline that has already taken place in the prices of some industrial commodities and a marked easing in the rate of increase in energy and food costs, make the prospect increasingly favourable for a generally more moderate rise in prices in 1975. However, upward pressures on costs are expected to continue and the rate of inflation will remain high by historic standards.

estic demand factors

As in 1974, the strongest element in Canada's domestic demand in 1975 is likely to be business-capital investment. Important indicators of business intentions, and the large volume of work already in progress, signal a continuation in 1975 of vigorous business-capital spending trends, despite increased uncertainities about costs and softer markets.

An October survey by the Department of Industry, Trade and Commerce of 220 large corporations representing a substantial part of Canadian industry indicates substantial new growth in capital spending. These large corporations plan to raise their expected outlays on new construction, machinery and equipment by 30 per cent in 1975, which would imply a somewhat greater advance in volume than had been estimated for 1974. All industrial sectors, other than oil and gas pipelines, indicate upward revisions of inten over those indicated in a similar survey made earlier in the y The increases in intentions are largest for manufacturing, oil gas, and electrical utilities sectors. Relatively few business seem to have allowed recent changes in the business climate at home and abroad to exert a negative influence on their capital spending intentions. The general view appears to be that curre adverse factors are predominantly short-run in nature.

This further expansion in business investment, as well as the strengthening of disposable incomes of Canadians through incom tax cuts and increased transfer payments, will be an important stimulus to the economy in 1975. Lower interest-rates and a nu of measures to provide stronger incentives for new home buildi should bring about some recovery of residential construction, slackened during the latter months of 1974. Taken together, th factors will sustain private expenditures and promote a furthe increase in real output in 1975.

Foreign trade

Canada's foreign-trade prospects in 1975 continue to be affect by the temporary lack of growth in the economics of our princi trading partners, notably the United States, Japan and the Uni Kingdom. Modest recovery in most of these markets may be expec to be under way during the course of the coming year, assuming easing in policies of restraint. Initially, however, the resur of economic activity abroad is likely to be slow and may provi only limited additional demand in volume terms for Canada's ex products in 1975.

In dollar terms, a further substantial increase in exports ma expected in spite of softening prices for some of Canada's re exports. An increase in value terms of somewhat more than half obtained in 1974 may be expected in 1975.

Meanwhile, Canada's economic performance in 1975 should contri to a continuing strong import demand. This is likely to be re forced by the ambitious capital-investment program now under w since many of the investment goods required will be imported.

Lack of major growth in export markets and persistent firmness imports are likely to mean further deterioration in Canada's c dity trade balance, which may shift from a moderate surplus of under $1 billion in 1974 to close to balance next year.

Policy challenge

In the past year, the international, financial and economic s ture has had to withstand severe problems created by inflatio fluctuating exchange-rates and massive imbalances in trade re ing from high oil prices. The challenge will continue in 1975 beyond. This strain, accompanied by mounting international debts, may tempt some countries to try to eliminate their deficits at the expense of others. To yield to this temptation would be self-defeating and would only worsen the world economic situation.

For its part, Canada continues to place the highest priority on the liberalization and enlargement of international trade. The international situation requires a continued patient building of bridges between nations rather than the erection of new trade barriers.

The Canadian Government supports the International Monetary Fund and the World Bank and looks to them to provide the focal-points around which to maintain and strengthen the international co-operation needed in present circumstances in relation to such problems as balance-of-payments adjustments, recycling of "petro-dollars" and aid to less-developed countries. The Government also supports the General Agreement on Tariffs and Trade, which it is hoped will be embarking in the coming year on a new round of negotiations to improve access to world markets. It is a major instrument aimed at providing a stronger framework within which world trade can develop.

We are fully conscious of our primary responsibility to further the growth of Canadian trade. All departmental resources are committed to the support of co-operative arrangements among nations to meet the challenge of these critical international problems.

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