THE EFFECT OF THE WAR ON CANADIAN FOREIGN TRADE

by

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Chapter One

IMPORTANCE OF FOREIGN TRADE TO CANADA

a) Trade in the history of Canada

Canadian history from the beginning can almost be written in terms of her foreign trade. It was not only the inquisitive interest in discovery, the lust for adventure, and the sudden patriotic fervour that sent the little wooden ships across the Atlantic to Canada, from France and later from England, to poke tentatively around the Maritime coast and sail up the St. Lawrence; it was trade. In the same way that the famous East India and French East India Companies with their strong mercantile backing opened India and the treasures of the East to Europe, so French businessmen (such as DeChastes, Deionts, and LaSalle) and the Hudson's Bay and North West Trading Companies were responsible for the opening and early development of Canada. At every step we find a trading interest responsible for Canadian growth. Indeed, on many an occasion, such as the dispute between Frontenac and Bishop Laval over the liquor trade with the Indians, and Governor Murray's trouble with the merchants, the domestic interest of the colony came into conflict with

the trading interest, controlled from abroad; and the latter usually won out.

From the opening of the West as a result of the competition in the fur trade between the Hudson's Bay Company and the North West Trading Company, through the early struggles of the Dominion over protection and reciprocity with the United States, through the large capital imports at the beginning of the twentieth century with the development of the wheat, fish, and pulp and paper staples, to the present position where eleven and a half million people carry on five billion dollars worth of foreign trade annually, trade has been essential to Canadian growth. Canada has been built by foreign trade and she will live by it. It is the significant factor in her development. Her whole politics and economic policy are closely bound up with it.

b) Canadian position in world trade

To-day, on a per capita basis, Canadian foreign trade exceeds that of any of the world's large economic powers. On this basis, in certain interwar years, she was the world's largest exporter and second largest importer. During the interwar period with only 1/200 of the world's population Canada regularly accounted for 1/30 of its international trade! Even ignoring her small population Table 1 shows how large has been her share of the world's commerce. It shows that before the second World War

Canada was the world's fifth trading nation; and in 1944 she moved up to second place in exports and third in total trade.

Table 1

PERCENTAGES OF WORLD TRADE FOR SEVEN LEADING COUNTRIES

Country	1926	1929	1932	1937	1938
United Kingdom	14.0	13.1	13.2	13.5	13.8
United States	14.7	13.8	10.8	11.7	10.7
Germany	7.6	9.4	9.3	8.6	10.0
France	6.2	6.2	7.2	5.0	4.7
Canada	3.7	3.7	3.3	3.6	3.5
Belgium	2.3	2.7	3.2	3.4	3.2
Japan	3.3	2.9	2.8	3.7	3.2

Source: Compiled from "League of Nations Monthly Bulletin of Statistics". Basis - recorded values of merchandise trade converted to U.S.A. old gold dollars.

It is no inexplicable phenomenon that Canada has reached this position in world trade, that her external trade grew from $120 million in 1867 to $1,900 million in 1939. It is explained by the nature of her economy. In that period her share in the world's commerce increased 200%, while the United States' increased 50%, and the United Kingdom's decreased 30%. Of course that is one way of saying Canada reached economic maturity later than the other two countries; but it also reflects the importance of foreign trade in the development of the Canadian economy. All the great strides Canada has made

towards economic maturity have been dependent on her foreign markets and suppliers (of capital as well as merchandise). Undoubtedly, as we shall shortly see, there has been a close relationship between foreign trade and national income, production, volume of business, and other such indexes of economic conditions.

c) Aspects of the Canadian economy particularly affecting trade

If we study the nature of the Canadian economy these relationships are just the kind of thing we should expect. Certainly foreign trade has been closely associated with the growth of that economy; it has been a sort of "sine qua non". More particularly, there are certain aspects peculiar to the Canadian economy that are intimately connected with the nature of its foreign trade, and as such are important of mention here.

Geography makes Canada more or less of an addition to the American economy with a resulting inclination for intercourse to flow in a North-South direction, a tendency our forefathers have attempted to counteract in order to save the national honour. They have attempted to make the political International Boundary a truly economic one - no mean feat. Consequently, at various times, in order to overcome the natural direction of activity and to direct commerce along an East-West channel, tariff and other such barriers have been erected.

The frequent erection and pulling down of these barriers has only aggravated the fluctuation in external trade.

Another point is population. Unhappily the foreigners' conception of Canada as a country of empty and snowy wastes is all too true. The country is sparsely settled, with stretches of unsettled, little-developed territory between the small conglomerations of population. The difficulties of intercourse between centres within the various areas, except for the lower St. Lawrence valley and the Niagara peninsula, are bad enough; but those between the four main areas are serious. The Maritimes are separated from the industrial central region by 500 miles of rugged and economically poor Appalachians. The separation of the sparsely-settled, agricultural Prairies from the Niagara peninsula is no better - about 900 miles of almost unpopulated, rough wastes. Then the formidable Rocky Mountains thrust themselves between the Prairies and the Pacific coast. These barriers are admittedly a source of natural wealth, particularly mineral, but they certainly do not facilitate a speedy flow of commerce across the Dominion and a simple integration of a full economy. In many cases the movement of goods to and from foreign is cheaper than to and from domestic markets. The transporting of Pennsylvania as against Nova Scotia coal to central Canada is an obvious case.

The climate is also a serious handicap. It puts a severe strain on, or entirely closes, large parts of the transportation system five months every year; and is generally responsible for the high seasonal variation of Canadian business.

In the past the Canadian productive effort has been confined to large quantities of a few staple products. The economic production of those staples has presupposed the use of large amounts of capital (from foreign sources) and advanced techniques; and this has been the basis of Canadian economic life. What is more, this kind of production requires large foreign markets and a relatively free system of multilateral trade, with a resulting dependency of export trade on the policies of other countries.

This kind of productive machine has not been entirely one of choice. It has been largely dictated by the capital and resources available, resources that have been fashioned by the same geography and climate that are the cause of so many troubles. Few countries could count their extremes of natural wealth so great. The quantity of Canada's agricultural, forest, non-ferrous metal, fishing, and hydro-electric resources is immense. And the quality thereof is no less imposing. Lack of variety seems to be the trouble. Many important staples are lacking. Under those conditions the Canadian economy

grew too quickly to become a fully rounded one.

d) Necessity of imports

Just as in some directions the country is faced with a surplus it can't possibly consume, in others it is faced with a deficit it must import. Canada lacks in sufficient quality and quantity many basic materials, particularly those of a tropical or semi-tropical nature. An immensely wealthy agricultural country she grows no rubber, cotton, or many basic fibres. With rich and varied mineral deposits the fires in the homes and factories of her populous central regions are kept going on imported coal. All this, not to mention the lack of tin, oil, sulphur, wook, silk, and many other products.

Others still she has imported because the small market has made it too costly to manufacture them (machinery stands out in this connection); or the state of her industrial development has permitted her only to finish the manufacturing process. Consequently much of Canadian industry has depended on imported raw or partly finished materials; hence imports have tended to fluctuate widely with industrial activity. The extent to which Merchandise Imports have followed Manufacturing is shown in Chart I. It will be noted that the two have moved very much in concert indeed, intimating not only how dependent on industrial activity has been import trade but how much that trade has been composed of articles used by Canadian

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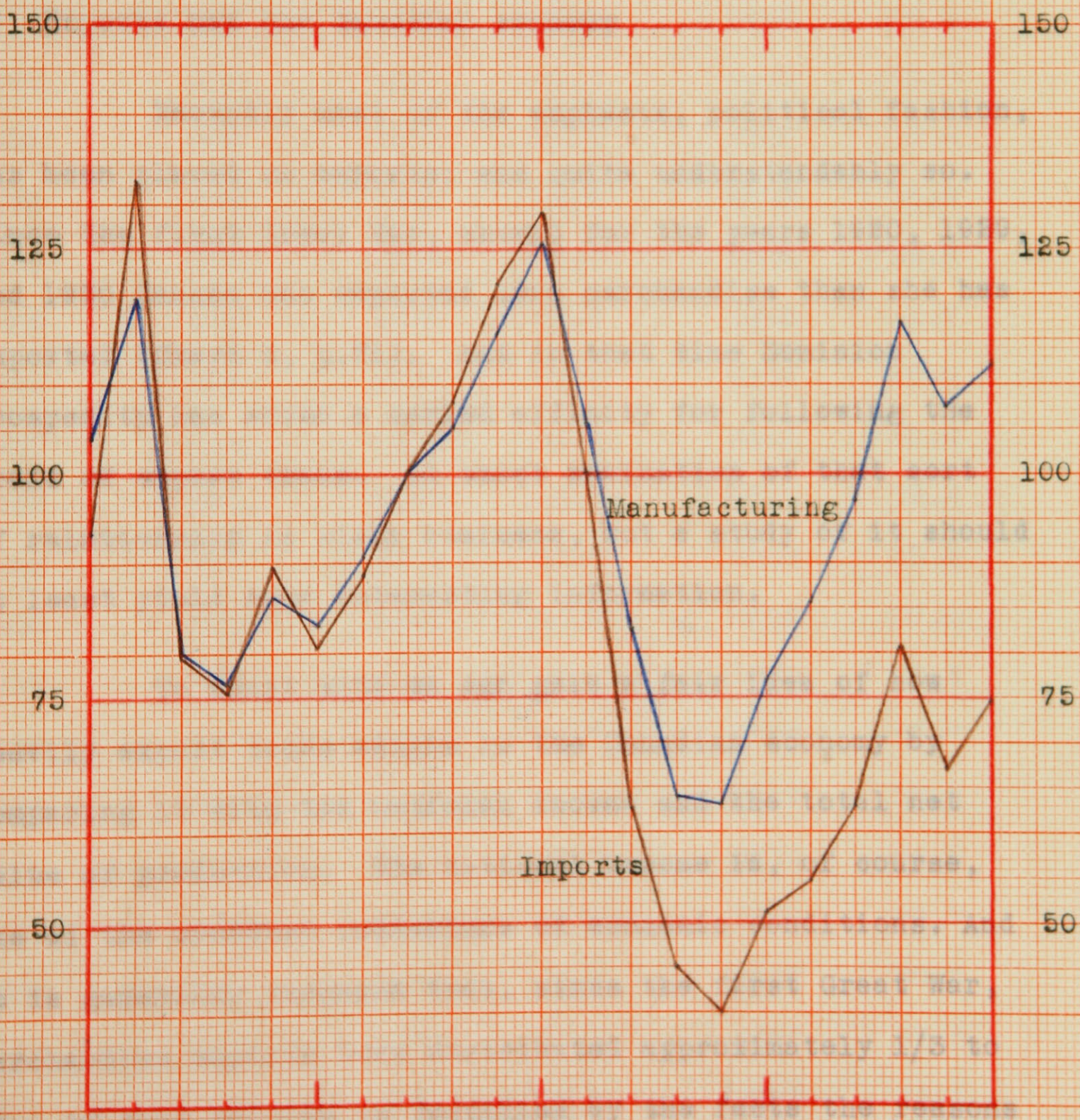
Chart 1

INDEXES OF GROSS VALUE OF MANUFACTURING AND VALUE OF MERCHANDISE IMPORTS 1919-1939

(1926=100)



Source: Appendix I

manufactures. As a matter of fact, Canadian imports have consisted largely of producers' goods and luxury consumers' goods (Chap. 3 sect. d, and Chap. 4 sect. c). Consequently, as studies have shown[1], changes in the value of merchandise imports have been very sensitive to changes in national income.

e) Exports and the Canadian economy

Recently most of the emphasis, political fashion, has been placed on exports; and quite understandably so. Since the first Great War, except for the years 1920, 1929, and 1930 Canada has exported more merchandise than she has imported (Chart X, p.71). And in that time Dominion prosperity has shown a marked affinity for following the trend of export trade. An exact evaluation of that sort of relationship is risky business, but a study of it should at least yield some interesting information.

To start with we can gain a fair idea of how heavily export trade weighs in the Canadian economy by comparing it with the national income and the total net value of production. The national income is, of course, one of the soundest indicators of economic conditions. And it is generally reckoned that, since the first Great War, merchandise exports have contributed approximately 1/3 to it. If this opinion is justified by the facts the reasons

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1 "Imports and Income in the United States and Canada" by I. deVegh in "Review of Economic Statistics", August 1941

Table 2

MERCHANDISE EXPORTS IN NATIONAL INCOME AND NET VALUE OF PRODUCTION 1919-1939

(values in $ million)

Year	Mdse. Exports	Nat. Inc.	% Exp. of N.I.	Net Value Production	% Exp. N.V.P.
1919	1295	3816	33.9	3313	39.1
1920	1303	4598	28.3	3408	38.2
1921	817	3507	23.3	2415	33.8
1922	898	3671	24.5	2537	35.4
1923	1029	3847	26.8	2793	36.9
1924	1070	3865	27.7	2686	39.9
1925	1283	4239	30.3	2988	42.7
1926	1289	4507	28.6	3156	40.9
1927	1242	4738	26.2	3461	35.8
1928	1381	5269	26.2	3514	39.2
1929	1211	5273	23.0	3658	33.1
1930	905	4452	20.3	3252	27.8
1931	629	3580	17.6	2562	24.6
1932	554	2813	19.7	2155	25.7
1933	603	2723	22.1	1949	30.9
1934	766	3147	24.3	2219	34.5
1935	838	3371	24.9	2350	35.7
1936	1028	3827	26.9	2645	38.9
1937	1125	4368	25.7	2992	37.6
1938	957	4291	22.3	2975	32.1
1939	1099	4554	24.1	3224	33.9
Average 1919-1939			25.1		35.1

Sources: Merchandise Exports and National Income - Appendix I; Net Value of Production - "Canada Year Book".

for the importance attached to export trade by certain Canadian politicians and economists are obvious. The actual part played by exports in national income and net value of production during the interwar period is shown in Table 2. Although there is some fluctuation in the Merchandise Exports % of National Income and of Net Value of Production (high in prosperous years and low in depression years), the average Merchandise Exports % of National Income is slightly over 25; and if we add the value of handling, transporting, and general facilitating of those exports the total % of national income contributed by merchandise exports would be in the neighbourhood of 33 1/3.

The last column of the table, giving the Merchandise Exports % of Net Value of Production in the 9 main branches of production, is almost startling. In some years 40%, and on an average 35%, of the commodities Canadians produce has been exported[1]. An economy whose productive machine is geared to produce for foreign markets to that extent is indeed an exceptional one. By and large, then, we can say that 1/3 of the Dominion's population has been living by its exports.

For comparison the relative positions for the United States and the United Kingdom are shown on Table 3. Although the total value of merchandise exports for these

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[1]This is a very slight overstatement as the Merchandise Export figures include a small amount of foreign produce re-exported.

Table 3

MERCHANDISE EXPORTS IN NATIONAL INCOME IN UNITED KINGDOM AND UNITED STATES

	United Kingdom			United States		
Year	Mdse. Exps. (£ million)	Nat. Inc.	% Exp. of N.I.	Mdse. Exps. ($ million)	Nat. Inc.	% Exp. of N.I.
1925	773	4172	18.5			
1926	653	4142	15.8			
1927	709	4291	16.5			
1928	724	4130	16.8			
1929	729	4307	16.9	5426	82885	6.5
1930	571	4180	13.6	4025	68901	5.8
1931	391	3807	10.3	2585	54310	4.8
1932	365	3686	9.9	1735	40074	4.3
1933	368	3825	9.6	1802	42430	4.2
1934	396	4002	9.9	2282	50347	4.5
1935	426	4209	10.1	2463	58870	4.2
1936	441	4440	9.9	2666	65165	4.1
1937	521	4644	11.2	3585	71172	5.0
1938	471	4654	10.1	3317	63610	5.2
1939	440	4968	8.9	3409	69378	4.9

Sources: for U.K. Exports - "Annual Statement of Trade of the United Kingdom" (merchandise, produce of U.K. only); for U.K. National Income - 1925-1938 from "National Income" by Bawley (national income paid out), 1939 from "Statistics Relating to the War Effort of the United Kingdom", November 1944 (net national income); for U.S. Exports - "Statistical Abstract of the United States" (merchandise exports of continental U.S.); for U.S. National Income - "Statistical Abstract of the United States" (national income produced).

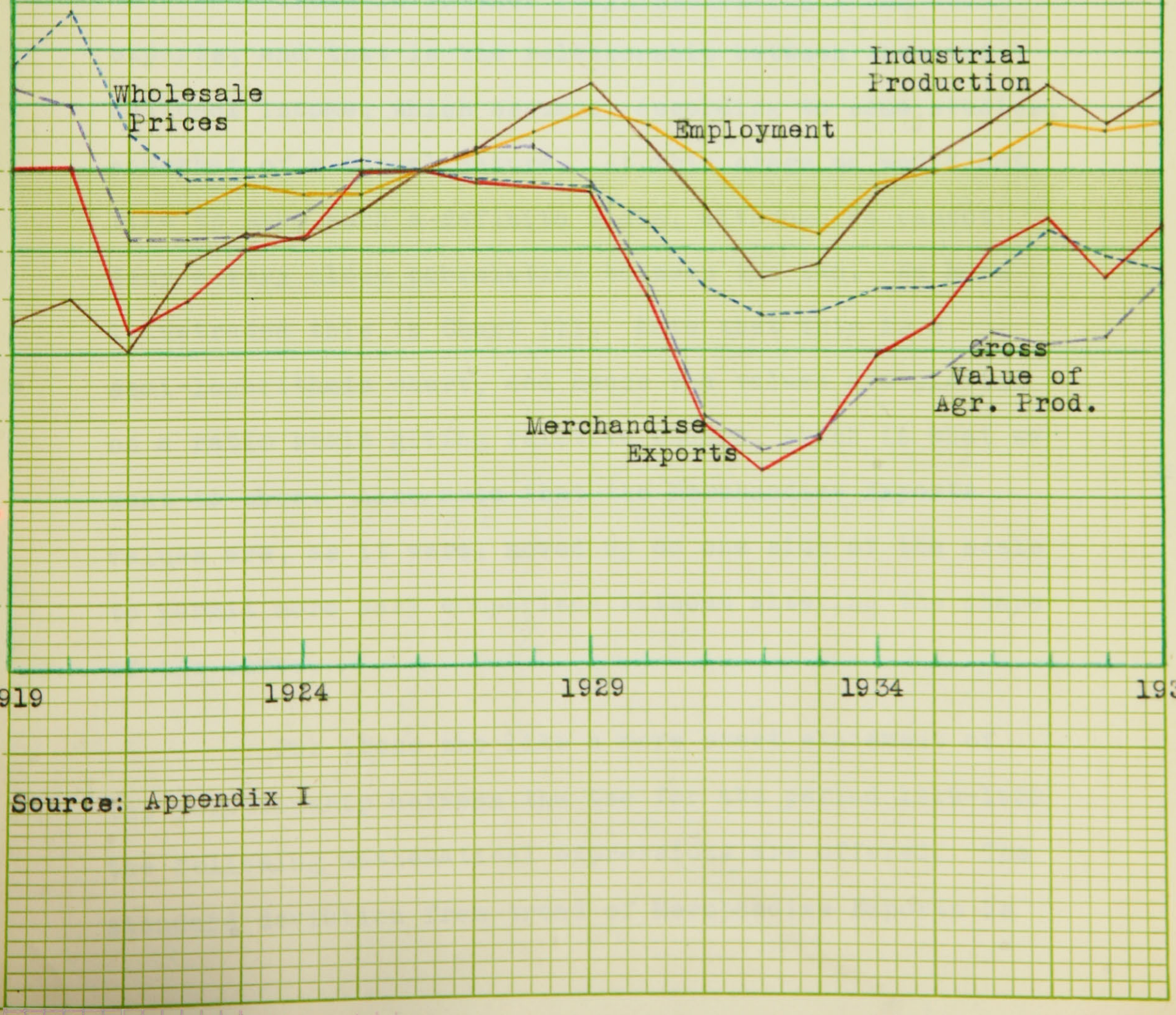
two countries has been considerably in excess of the Canadian figures the corresponding percentages have been much smaller. Export trade has not bulked so largely in their economies. The average Merchandise Exports % of National Income in the United Kingdom for the fifteen year period 1925-1939 was only 12.5, while the average in the United States for the eleven year period 1929-1939 was a mere 5. Compare that with the Canadian position shown in Table 2.

Thus far we have confirmed the seemingly commonly-held belief of the extent to which Canada as a whole depends on export trade and of the large number of Canadians who directly depend on it for a livelihood. What is perhaps not such common knowledge is the extent to which the whole Canadian economy reacts to the vicissitudes of its export trade. On Chart II are plotted indexes for Employment, Wholesale Prices, Gross Value of Agricultural Production, and Industrial Production, taken together, fairly illustrative of the health of the Canadian economy. The chart is drawn to a semi-logarithmic scale, so that the common base year of 1926 makes no difference whatever to the relationships between the curves in later years. The shape of each curve would have been just the same if original values or varying base years had been used. Against them is plotted, in red, the Index of the Value of Merchandise Exports. Without interpreting the various relationships between the curves too carefully

Chart II

MERCHANDISE EXPORTS, GROSS VALUE OF AGRICULTURAL PRODUCTION, EMPLOYMENT, WHOLESALE PRICES, AND INDUSTRIAL PRODUCTION 1919-1939

(1926=100)



Source: Appendix I

at this time, it will be noted how closely the several indexes follow the fluctuations in Merchandise Exports (we say "follow" here because we are emphasizing that particular index). Note not only that the general upward and downward movements are initiated in Merchandise Exports but that the fluctuations tend to be more violent in its case. It would seem to be a ready-made business forecaster.

f) Correlation of exports and national income

There is another very interesting thing about exports, and that is the relationship between them and national income, which assumes, according to some studies, somewhat of a causal nature. At this stage we would not like to make such a definite claim, although we cannot deny a very close correlation between the two. We have illustrated this in Chart III. Note that this is a semi-logarithmic chart, and hence the values are plotted on a ratio scale giving relative change, which is what we want to show. Also note that the Merchandise Exports values are, as it were, moved up on one side of the scale to permit more easy comparison without altering the shape of the curve.

For those who like a more exact statement of the relationship between the two for the period 1919-1939 the following mathematical expressions are offered. The standard deviation from trend of Merchandise Exports is

Chart III

VALUE OF MERCHANDISE EXPORTS AND NATIONAL INCOME 1919-1939

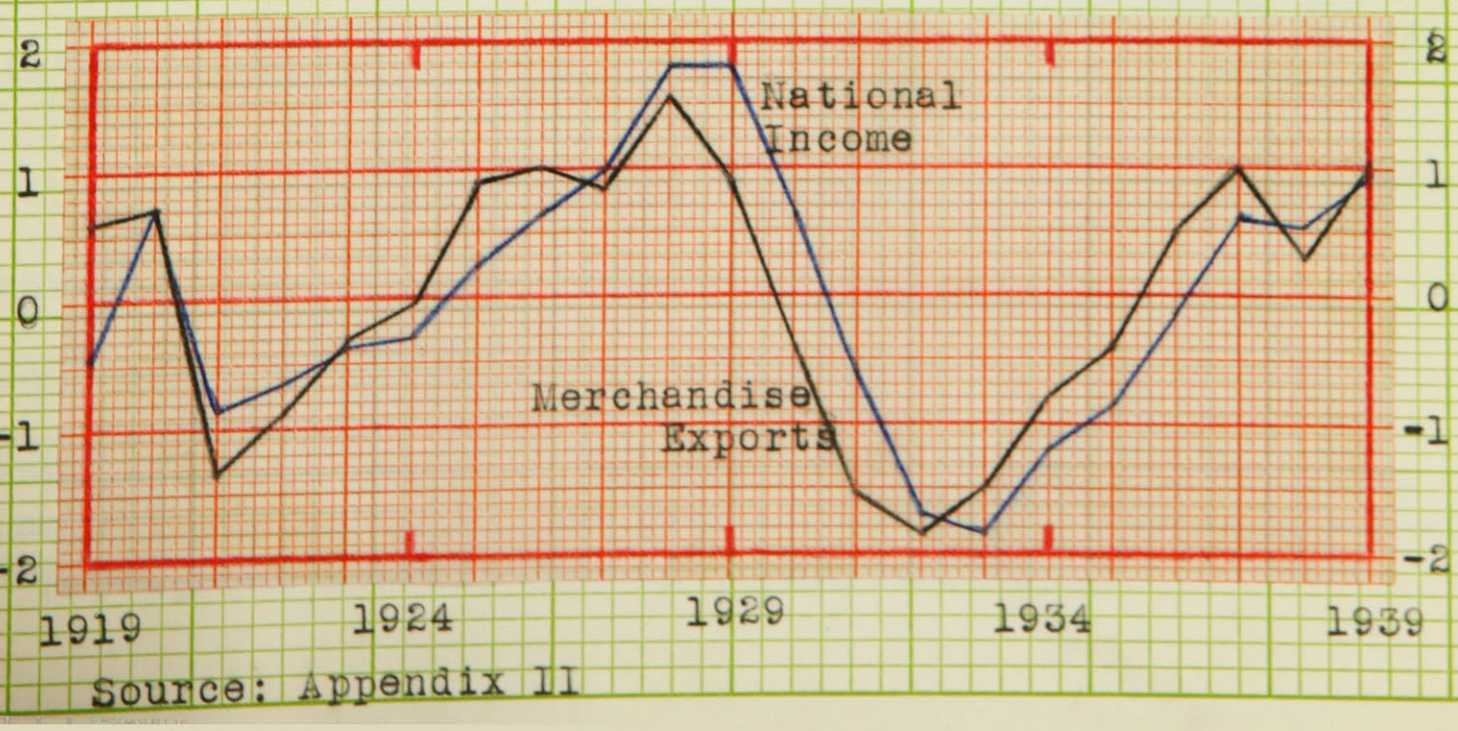
($ million)

Source: Appendix I

Chart IV

MERCHANDISE EXPORTS AND NATIONAL INCOME 1919-1939

IN TERMS OF THEIR STANDARD DEVIATIONS



Source: Appendix II

17.7 and of National Income 15.2. The coefficient of correlation between the two series is plus .85, very high indeed (anything above .50 shows some significance). This last is shown graphically on Chart IV, which shows the differences from trend of the two series in terms of their standard deviations. The complete method and computations for the information in this last paragraph are given in Appendix II.

No doubt even the unmathematical reader has already noticed in the last two charts the almost parallel movement of merchandise exports one year and national income the following year. As a matter of fact Munzer, in a study of the period 1923-1938[1], deduces an exceptionally close correlation (his coefficient of correlation is plus .989) between exports (including non-monetary gold) one year and national income received the following year. Put in dollars and cents, he estimates an export of $1 in one year was followed in the next year by a national income received of $3.82. On the basis of his statistical analysis he concludes that exports were the most important determinant of the Canadian national income during the interwar period.

Royal Bank studies[2] have indicated that the correspondence between changes in exports one year and changes in national income the succeeding year is 93%

1"Exports and National Income" by E. Munzer in "Canadian Journal of Economics and Political Science", February 1945
2"Royal Bank Monthly Letter", September 1944

for 1925-1940 and almost 100% for a longer period.

G. Jackson estimates that $3.00 of exports adds about $5.00 to the national income above the small basic sum we could achieve if we did not export. In fact he goes so far as to say that "twelve months of exporting on a large scale and at a profit have always been followed by twelve months of prosperity".[1]

It should be mentioned that the relationship between exports and national income is not peculiar to Canada alone. Other studies have shown a corresponding relationship in the United States and the United Kingdom though the relationship is, as one would expect from Table 3 on page 12, less close.

Thus far then, we have seen that there has been a close relationship between exports and national income during the interwar period, and during the last decade that relationship appears to have taken on somewhat of a causal nature. However, it must be admitted that a correlation does not necessarily imply a causal relation. Obviously the amount of foreign trade affects national income. Undoubtedly the level of national income affects foreign trade. And undoubtedly there are other factors that affect both in common. But what we already know of the nature of the Canadian economy, plus the evidence of the relationship between exports and national income

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[1] "The Facts in the Case" by G. Jackson

during the interwar period at least impresses us with the importance of the former to the latter. Therefore, although it is not claimed the movement of exports is a sufficient explanation of the state of Canadian prosperity, the basic part it plays in that prosperity is an undoubted fact.

Chapter Two

MERCHANDISE TRADE
IN THE BALANCE OF INTERNATIONAL PAYMENTS

a) The idea of a balance

Before proceeding with an analysis of Canadian foreign trade it is vitally important to fix the place of merchandise trade in the Canadian balance of international payments. The balance of payments (giving a summary of <u>all</u> commercial and financial transactions between Canada and other countries) is actually the larger picture. When we isolate merchandise trade for study we must remember that we are looking at one only of the items. There are many others, both "visible" and "invisible", involving a demand for or a supply of foreign exchange. As a whole, the sum total of all these receipts or payments of foreign exchange over any given period of time must balance. That is self-evident. For if there is any difference in total debit and credit values of all current transactions, it must be balanced by some sort of borrowing or lending operation. That is, it is axiomatic that the total amounts of foreign exchange bought and sold must be equal. Because it is a balance then, and

because merchandise trade is only one item, we should expect the other items to have an effect on trade, as trade has on them; and that is exactly the position. A short study of the Canadian balance of payments for 1937 will reveal the interdependence in the whole situation.

Table 4

ESTIMATED CANADIAN BALANCE OF INTERNATIONAL PAYMENTS, 1937

($ million)

	Credits (Exports)	Debits (Imports)	Net Credits or Debits
Current Account			
Merchandise trade	1009.7	796.4	213.3
Gold	145.1	.1	145.0
Freight	111.7	137.2	25.5
Tourist trade	294.7	124.4	170.3
Interest and Dividends	78.2	325.0	246.8
Miscellaneous services etc.	25.2	63.9	38.7
	1665.2	1447.0	218.2
Capital Account			
New issues and retirements Canadian securities	89.5	177.9	88.4
Other securities transactions	506.6	511.4	4.8
Other capital movements	24.0	129.6	105.6
	620.1	818.9	198.8
Residual item		19.4	19.4
	2285.3	2285.3	

"Canadian Balance of International Payments, 1939"

b) Current account

It will be noted that in 1937 Merchandise trade (excluding gold) accounted for 54% of total current transactions, making it easily the most important item. And for the period from 1926 to 1937 it accounted for an average of almost 60%. It is obvious, then, that if merchandise trade plays such a large part in the account and if there is a fairly substantial net debit or credit on this item, this net debit or credit must be balanced by, or can balance, other and opposite substantial items. But, as we noted earlier, the merchandise trade balance since 1919 has usually shown a substantial credit. So that this credit has to be balanced by equal debits; or, looked at in another way, it can balance necessary debits.

In the same period Gold has, without exception, shown a net credit, any import of monetary gold being more than offset by exports of the non-monetary variety, particularly during the last few years when the gold policy of the United States has encouraged considerable Canadian gold exports to that country. We may infer then that the credit balance of merchandise trade has not been paid for by imports of gold. It is more natural to think of the product of Canadian gold mines as paying for merchandise imports. This does not mean to say that gold movements (particularly monetary gold imports) could not be a debit balancing item. In the immediate past they haven't. However, it is not intended to enter here into

Table 5

BALANCES OF MERCHANDISE TRADE AND MONETARY GOLD 1926-1937

($ million)

Year	Net Merchandise Trade Balance	Net Monetary Gold Balance
1926	275.6	1.0
1927	138.9	7.2
1928	131.0	48.5
1929	131.3	36.4
1930	122.1	35.7
1931	17.4	33.2
1932	73.7	2.9
1933	146.6	6.0
1934	148.1	4.3
1935	192.7	2.1
1936	322.2	0.0
1937	213.3	0.0

Credit balances in black, debit balances in red
Source: "Canadian Balance of International Payments, 1939"

a discussion and verification of the effect of gold movements on international prices and trade. In passing it might be observed that net imports or exports of monetary gold seem, in the Canadian case, to have borne little relation to the merchandise balance of trade, as Table 5 shows. In this table the Net Monetary Gold Balance, following the system used by the Bank of Canada, includes domestic gold purchased for Canadian monetary stock. If this were excluded the only debit

balance of monetary gold remaining would be in 1930, and that would amount to some $20 million instead of $35 million.

Those readers who have been uneasy about the inclusion of gold in merchandise trade when considering the latter generally but the exclusion of gold from merchandise trade when considering the balance of payments are referred to Appendix III, where the position of gold in trade statistics in this paper is explained.

The Canadian Freight balance has been a debit one. That is, Canadians have owed foreigners much more for transporting their commodities than they have been owed for similar services. Insofar as this tendency continues, though the sum has not been great, it will help balance credit items.

A great deal of attention has been given recently to the importance of the credit balance of Tourist trade in paying for merchandise imports from the United States. And rightly so. Without this substantial credit item in the Canadian balance with the United States, meaning a ready supply of U.S.$, many essential imports would have to be done without or financed in some more difficult way. In other words, because Americans are willing to come to Canada and spend U.S.$ shooting moose, bull, and whatnot, Canadians are able to use those U.S.$ to buy American aircraft, gas,

coal, cotton, and propaganda. Of course in multilateral trade this does not mean that Canada must spend her substantial tourist expenditure credit, largely made up with the United States, in that country. It can be, and is, used to balance debit items with the rest of the world.

Outside of Interest and Dividends, the other items on Current account grouped under Miscellaneous services etc., such as Government expenditures and receipts, Immigrants' remittances, Charitable and missionary contributions, Advertising, Motion picture royalties, Immigrant and emigrant capital, and Earnings of Canadian residents employed in the United States and American residents employed in Canada, are of lesser influence and do not require mention here. Although Interest and Dividends are naturally associated with capital the item is put in Current account, that is, that part of the balance that deals with international transactions in <u>goods and services</u> for the period, for the following reason. They are current and obligatory payments for services rendered by capital, though that capital may have been invested in the past. Certainly it is a current obligation, and has been a heavy one at that. Very rarely (once in the period 1926-1939) has the credit balance of Merchandise trade been larger than the debit balance of this item. Of course it has been merely a reflection of past heavy investment in Canada,

and means that Canadians were paying their creditors the return on their money. The obvious way to meet this debit was, of course, a handy merchandise export surplus. And that is the way the thing worked.

c) Capital account

In this particular year (1937) the Current account showed a net credit of $218.2 million, which meant that, on current goods and services, foreigners owed Canadians more than Canadians owed them to the extent of $218.2 million. This in turn meant that this credit would have to be financed by Canadians loaning $218.2 million abroad. If we turn to Capital account, that is, to the remaining international transactions, we should expect to see some such thing. We do.

Note that many more Canadian securities were retired than new ones issued. Even in the international trading of Outstanding securities Canadians were more inclined to invest abroad than foreigners were in Canada. Likewise Other capital transactions showed an outward flow of Can.$. In all, capital debits amounted to $198.8 million, the residue of $19.4 million being due to errors and omissions in the balance. So that a surplus outflow of Canadian goods and services was possible because Canadians were in a position to, and did, invest their capital abroad. The credit balance on Current account was possible because of the debit balance on Capital

account, and vice versa.

d) Interdependence of items

It is admitted that throughout the foregoing discussion the emphasis has been placed on Current account, particularly on Merchandise trade. We have rather assumed that the conditions of the Current account were there, and the balance was worked out through the Capital account. But this need not necessarily be so. An increase in any item in one column would tend to decrease the other items in that column and increase all items in the other column. There is a mutual interdependence between all items. For instance, in 1937 there might have been a credit balance on Current account <u>because</u> Canadians had ready capital and found it profitable to invest abroad, hence supplying foreigners with a surplus of Can.$ which they could use to buy Canadian goods and services, or <u>because</u> Canadian goods and services were a good buy for the rest of the world, hence creating a demand for Can.$ which Canadians found profitable to loan. The impulse of the thing might just as easily have come from the foreign investment side as from commodity trade.

Indeed in the past it has. Before the first Great War import surpluses were the general rule in Canadian merchandise trade; and these were particularly marked from 1902 to 1915, a period of large foreign investment in Canada. Foreign investors evidently

considered Canada a profitable field; certainly the potential natural resources of the country promised much, and capital flowed in. Because capital flowed in Canada was able to buy the things she needed to develope her resources. It was a period of construction. It was a period of large debit balances of merchandise trade as goods flowed in to build the productive machine which would grind out the products she would eventually sell. These debit balances were merely a reflection of the inflow of capital.

During that period foreign investment in Canada was no doubt the dominant influence in the Canadian balance of payments. Although, as we have shown, all items are interrelated, the key to the whole thing seems to have been capital movements. The flow of commodities was a result rather than a cause of them. From Confederation till the twenties Canadian prosperity followed a passive balance of trade[1] rather than an active one as it has more recently. Canadian boom years were ones of expansion generated by capital importing. In more recent years, as Canada approached economic maturity and the flow of investment dried up, there were interest and dividend payments to meet and, if conditions permitted, securities to be redeemed. And the only way to do it was with merchandise exports that earlier capital imports had helped finance. Hence it is no catch phrase

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[1] "Statistics of Foreign Trade" by K. W. Taylor in "Statistical Contributions to Canadian Economic History", Vol.2

that all foreign liabilities must in the end be paid for by goods and services.

What we have been trying to say is that - without minimizing the basic importance of foreign trade to the Canadian economy and to its foreign mirror the balance of payments - the character, amounts, and direction of this trade cannot be considered without at the same time keeping the balance of payments for the period in mind.

Chapter Three

MERCHANDISE TRADE 1919-1939

a) Tenor of interwar world trade

In the first chapter we justified the commonly-held belief in the importance of foreign trade to Canada. Now, so that we may have some basis for a comparison of wartime changes and their probable effect, we turn our attention to a much fuller study of the exact nature of Canadian foreign trade during the interwar period. We gain little by going further back, for Canadian trade did not come of age until the first Great War. Certainly this period is not famous for its international economic stability and freedom; but we have no guarantee that the end of the second World War has suddenly ushered in an age of international economic cooperation. Quite the contrary; we know that the problems in that connection are even more severe than they were in 1919, even if we grant that the will to solve them is stronger. The solution hangs very much in the balance. Perhaps the unsettled autarky of 1919-1939 was more "normal" than we would like to believe. The struggle Canadian trade made through the obstacles of interwar international economic

restrictions and the level it attained contain many fruitful lessons for the future.

The first interwar decade witnessed a succession of economic conferences sponsored by the League of Nations and the International Chamber of Commerce which strongly recommended the abolition of tariffs, commodity controls, and all restrictive trade practices. Although there was a surprising amount of agreement with these principles, the recommendations remained largely ineffective. No one really took the bull by the horns. Although there was some spotty relaxation of controls, many countries were in such a weak financial condition that they were forced, for selfish reasons, or in pure self-defence because of a lack of generous international cooperation, to maintain their controls, or even to increase them after sporadic attempts at their removal. In such an unsettled atmosphere, when the World Depression ushered in the second interwar decade, the world easily and quickly followed the Hawley-Smoot Tariff of the United States on a narrow path of outright protectionism. The extent to which these policies perpetuated the precipitous decline in world trade during the World Depression is shown in Table 6. The value of world trade did not start to recover until 1936, and then only slightly. The folly of high tariff and restrictive trade policies was painfully discovered and various rapprochements, admittedly of a very circumscribe nature, initiated.

Table 6

VALUE AND QUANTUM OF WORLD TRADE 1924-1938

(1929=100)

Year	Value	Quantum
1924	82.8	75.7
1925	94.3	83.2
1926	90.4	85.2
1927	95.1	91.9
1928	98.2	95.2
1929	100.0	100.0
1930	81.0	93.0
1931	57.9	85.5
1932	39.1	74.6
1933	35.2	75.4
1934	34.0	78.2
1935	34.7	81.8
1936	37.5	85.8
1937	46.3	96.5
1938	40.4	88.8

League of Nations "Review of World Trade, 1938"

A saner policy had scarcely got under way when the second World War sent the various national economies back to harbour.

Under such conditions it would not surprise us greatly to learn that Canadian trade languished. It did. Using League of Nations statistics of world trade,

which express values in terms of U.S.A. old gold $, we find that Canadian trade accounted for 3.66% of total world trade in 1925. It rose to 4.03% in 1928, declined to 2.91% in 1933, then regained its lost ground to 3.95% in 1936[1]. These figures demonstrate the sensitivity of Canadian trade to world conditions. If world trade was good, Canadian trade was better; but if world trade was poor, Canadian trade was poorer. Canada was near the end of the pendulum.

However, when compared with the stagnant position of many other countries, Canadian trade did not fare too badly. In spots it even flourished, which was due mainly to three factors. First, the currency remained comparatively sound and stable. Second, trade consisted largely of basic raw materials or manufactures which in the long run would suffer less than luxury goods from various national attempts at self-sufficiency. And third, Canadian trade was concentrated in countries which either pursued a relatively stable (if protectionist) policy or gave her a certain amount of preference. Nevertheless, it cannot be too strongly emphasized that the interwar flourishing aspect of Canadian trade was all too spotty. Fluctuations were extremely severe, which, considering the importance of trade to the economy,

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[1] Computed from "League of Nations Monthly Bulletin of Statistics". These figures can merely be considered very close approximations because of the translation of all currencies into U.S.A. old gold $ at questionable rates, and because of the various national systems for reporting trade statistics.

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Chart V

CANADIAN MERCHANDISE TRADE 1919-1939

($ million)

Source: Appendix I Including non-monetary gold

presented much hardship. Certainly trade does not seem to have kept pace with the rising potential of production.

b) Trend of interwar Canadian foreign trade

Canadian interwar foreign trade is shown on Chart V. Two aspects immediately stand out - 1) the country generally exported more than it imported, and 2) trade was grossly unstable. In connection with 2) it should be remembered that price movements (Chart II p. 14) can account for some of the apparent fluctuation in value, the fluctuation in actual volume of trade being not quite so severe as that of value. In 1920 total merchandise trade amounted to $2640 million; one year later it amounted to $1616 million! By 1928 it had climbed back to $2603 million; but three years later it had dropped to $1007 million - some 61% in three years! During the four years 1933-1937 total trade increased from $1004 million to $1934 million! Surely the actual volume of goods traded did not vary to that extent.

The relationship between value and volume of trade is illustrated in Charts VI and VII, on which are plotted indexes of the real volume of merchandise imports and exports for the period. The Volume indexes are determined by dividing the Import and Export Value indexes by their respective Price indexes. All indexes are based at 1926; and, although the Import and Export Price indexes use an average of the quantities imported and exported

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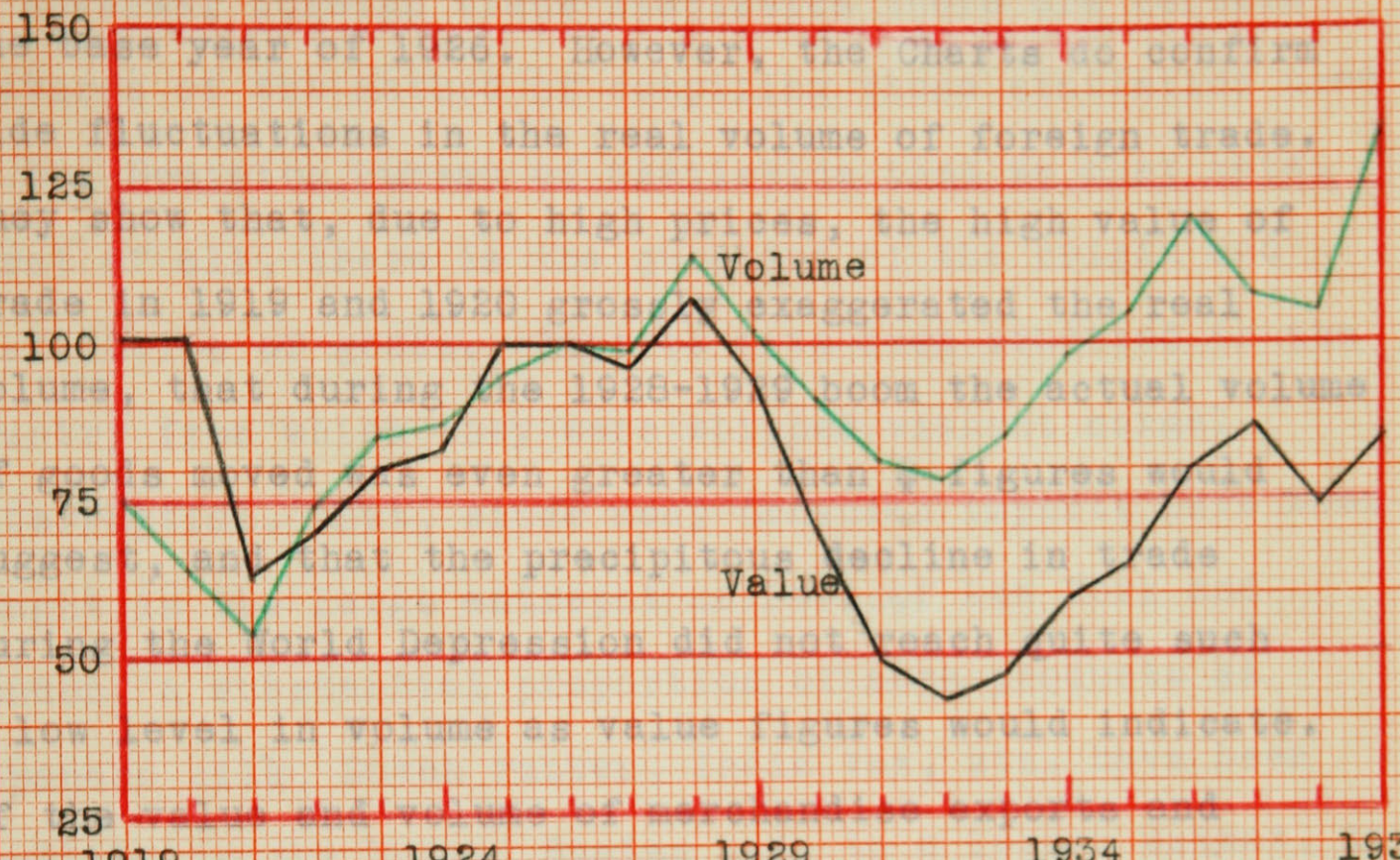
Chart VI

VALUE AND VOLUME OF MERCHANDISE EXPORTS 1919-1939

(1926=100)

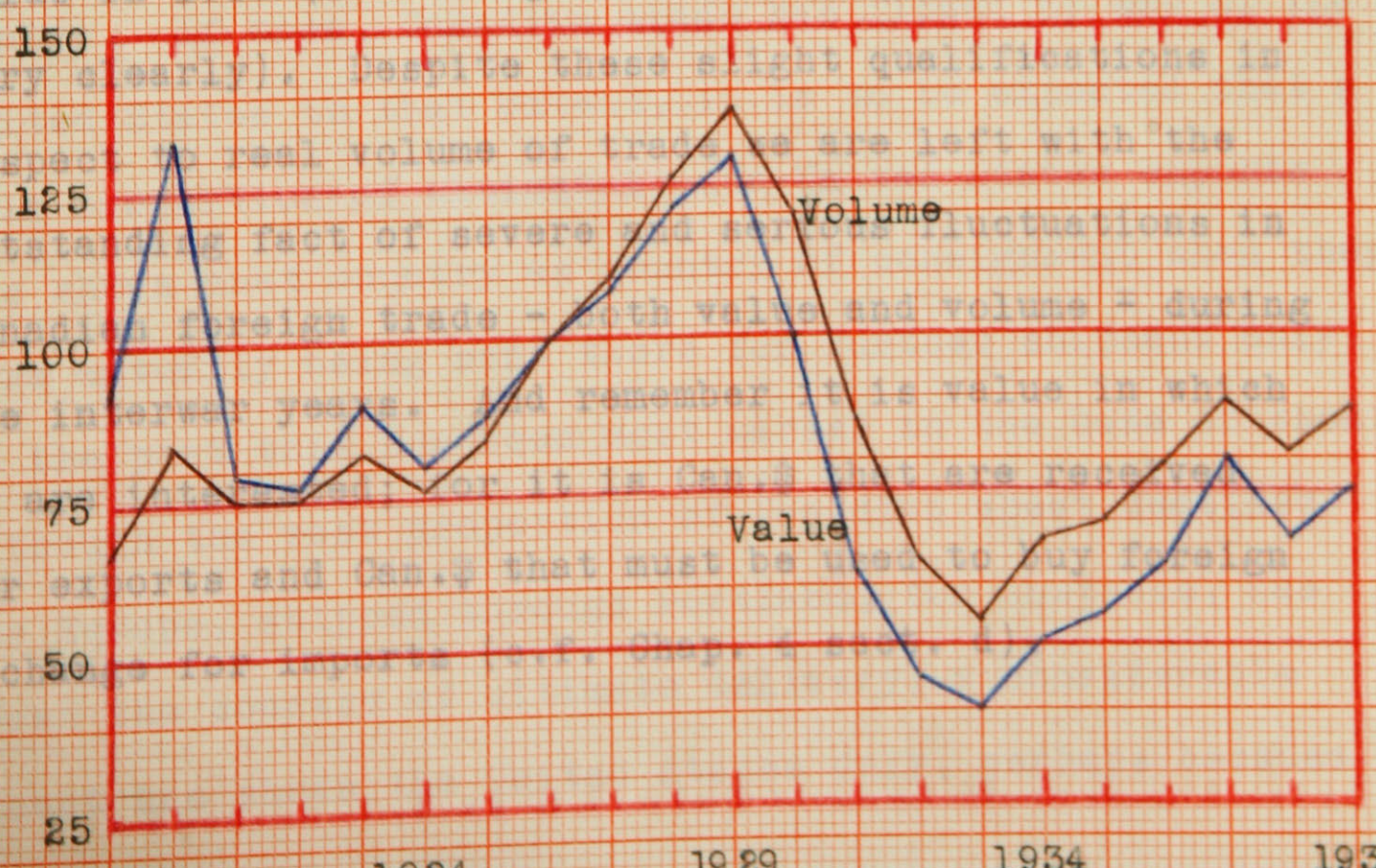


Source: Appendix I

Chart VII

VALUE AND VOLUME OF MERCHANDISE IMPORTS 1919-1939

(1926=100)



Source: Appendix I

for the years 1926-1931 for their weights, due to the change in the character of merchandise trade the Volume indexes become less accurate the further one moves from the base year of 1926. However, the Charts do confirm wide fluctuations in the real volume of foreign trade. They show that, due to high prices, the high value of trade in 1919 and 1920 grossly exaggerated the real volume, that during the 1928-1929 boom the actual volume of goods moved was even greater than ₹ figures would suggest, and that the precipitous decline in trade during the World Depression did not reach quite such a low level in volume as value figures would indicate. If the value and volume of merchandise exports and imports were plotted for the thirties with 1936 as a base it would be noted that the volume neither sinks as low as value in 1932 (though the two are closer than Charts VI and VII indicate) nor does it rise as high as value in 1937 (something that our Charts do not show very clearly). Despite these slight qualifications in respect to real volume of trade we are left with the outstanding fact of severe and serious fluctuations in Canadian foreign trade - both value and volume - during the interwar years. And remember it is value in which we are interested; for it is Can.$ that are received for exports and Can.$ that must be used to buy foreign exchange for imports (c.f. Chap. 4 sect. d).

c) Compilation of merchandise trade statistics

Before proceeding further with an interpretation of interwar foreign trade statistics there are certain features of the method of compiling those statistics used by the Dominion Bureau of Statistics that we must note. First of all, there is the question of the origin and destination of goods. Imports have been credited to the country from which they were shipped without normal interruption. But, since many Canadian imports have been bought in the large entrepot markets of New York and London, a substantial proportion of such products as Japanese silk, Dutch rubber, India tea, etc. have been credited to the United States and, to a lesser extent, to the United Kingdom. In the same way exports have been credited to the country of consignment, not the country of ultimate delivery. During the interwar period some 26% of Canadian overseas exports was shipped via the United States. If then, Canadian trade has flowed by way of the United States to that extent, it is to be expected that a fair proportion of ultimately non-United States exports has shown that country as country of consignment when they were actually being sent there for further shipment only. In the past this has been most marked in the case of wheat. Although the vast proportion of Canadian wheat destined for Europe, shipped through Portland, for instance, has shown the country of ultimate delivery, a considerable amount has shown the United States only, perhaps because

when the wheat left Canada it had not yet been determined whether the ultimate consignee was the Netherlands or Belgium.

Despite the recent very effective efforts to keep this kind of errors to a minimum they are the most important source of error in trade figures, and are well to keep in mind when considering American-Canadian trade in particular. But we must remember that the system, if not exact in other respects, does tell us how much of what kind of foreign exchange Canadians bought and sold, which is what we want to know. It doesn't matter who ate a certain bushel of Canadian wheat; if American dollars were received for it, it is the latter fact that entered into the international financial situation so far as Canada was immediately concerned.

Other errors have been introduced through customs valuations. To start with, imports have been valued at the fair market value in country of origin, not at their Canadian selling price. Even to arrive at a c.i.f. value more would have to be added to the value of goods coming from distant than from neighbouring countries. Furthermore, with the intent of preventing dumping, the Government has had the power to set arbitrary valuations above invoice valuations. This clause in the Customs Act introduced considerable errors between 1931 and 1935 especially. These errors did not tend to be minimized by

the method of currency valuation. When a foreign currency has been depreciated relative to the Can.$ customs values, with a few exceptions, have been calculated at normal par; whereas when it has been appreciated the current rate has been used. This has naturally overvalued imports from depreciated currency countries. This was particularly marked for imports from the United kingdom between 1931 and 1933, when the £ was at a discount of 15-25% most of the time.

These features obviously introduce a certain caveat in interpreting too closely trade statistics. It is, of course, impossible to estimate the exact amount of error introduced by these elements, but it is well to bear them in mind.

The remaining two features we have already mentioned in Chapters 1 and 2. One is the inclusion in merchandise exports of foreign produce imported into Canada ostensibly for home consumption but actually re-exported. Recently the total amount has been very small, running from 1 to 2 % of total merchandise exports annually (c.f. Appendix I). Nevertheless in the following analysis of merchandise exports we shall include those of domestic origin only.

The other feature is gold. As mentioned in Chapter 2 and Appendix III we shall now treat gold as an item rather separately, though heretofore we have

included it in merchandise export totals when considering exports in relation to production and national income. Where conditions warrant it we shall exclude gold entirely or note any outstanding developments in its connection, particularly in respect to the balance of payments. At any rate note that non-monetary gold exports are included in merchandise exports in this chapter unless specifically noted to the contrary.

Having cleared up these general considerations our next task is to determine what Canada has traded and with whom. The most concise and clear way to present this information is in tabular form; so that the following pages present mainly tables showing the nature of Canadian foreign trade during the interwar period with brief explanations pointing out the salient features. We shall leave a discussion of the effects to the next chapter.

d) Nature of import trade

The general character of Canadian import trade during the interwar period is shown in Table 7, which gives the percentage distribution of the nine classes of merchandise in total imports for five representative interwar years, namely the fiscal years 1928, 1928, 1932, 1936, and 1939. The choice of these five years to show the general trend was made for obvious reasons. First of all it should be remembered that the fiscal year ends

Table 7

IMPORTS BY CLASSES OF MERCHANDISE, FISCAL YEARS 1922, 1928, 1932, 1936, AND 1939

(% by each class)

Classes	1922	1928	1932	1936	1939
Agr. & veg. products ..	23.1	21.5	22.2	19.6	18.4
Animals & products	6.6	5.9	4.3	4.3	3.7
Fibres & textiles	18.7	16.9	14.5	16.0	12.9
Wood & paper	4.8	4.7	5.5	4.1	4.9
Iron & its products ...	14.7	23.4	17.1	20.3	23.4
Non-ferrous metals & products	4.0	5.4	5.9	6.0	5.5
Non-metallic minerals & products	18.4	13.8	17.7	18.5	18.4
Chemicals & allied products	3.3	3.0	5.3	5.3	5.3
Miscellaneous	6.8	5.4	7.5	5.6	7.5

Source: "Canada Year Book"

March 31st, thus actually contains very little of that particular calendar year. Consequently the fiscal year 1922 is in the trough of the depression following the first Great War, yet is sufficiently far removed from 1918 to preclude war merchandise. 1928 is near the height of "good times" without being at the top. 1932 is almost at the bottom of the World Depression. 1936 is on the way up to the minor recovery of 1937. And 1939 is the last prewar fiscal year.

A glance at Table 7 reveals that import trade was largely composed of four classes - 1) Agricultural and vegetable products, 2) Fibres, textiles, and textile products, 3) Iron and its products, and 4) Non-metallic minerals and their products. Agricultural and vegetable products played a very slowly but steadily declining role during the thirties, till in 1939 they were no longer the most important class of imports. Similarly Fibres, textiles, and textile products declined, noticeably between 1934 and 1939, to a point where they were almost of minor importance, accounting for only 12.9% of total imports in the fiscal year 1939. Iron and its products displayed a rather fluctuating tendency, though always maintaining a most important position. Indeed, before the second World War this class had established itself as the largest class of Canadian imports. Non-metallic minerals and their products also showed a tendency to fluctuate slightly after very rapid growth during the twenties to a point where they accounted for as large a portion of imports (over 18%) as Agricultural and vegetable products. It is worth mentioning that this was due largely to the heavy increase in petroleum imports and the relative decrease in imports of agricultural products that could be produced in Canada.

The merchandise imports picture is further clarified in Table 8, which classifies according to rank

Table 8

TEN LEADING COMMODITY IMPORTS, FISCAL YEARS

1922, 1928, 1932, 1936, AND 1939

($ million)

1922		1928	
Coal	78.3	Coal	58.3
Sugar & products	44.4	Machinery exc farm	48.6
Cotton goods	36.2	Alcoholic beverages	45.5
Fruits	29.5	Rolling-mill products	44.1
Woolen goods incl carpets	26.1	Sugar & products	38.8
Alcoholic beverages	24.5	Automobiles	34.4
Machinery exc farm	24.1	Fruits	34.4
Rolling-mill products	20.1	Petroleum crude	34.1
Silk goods	19.3	Automobile parts	33.2
Cotton raw	16.3	Farm implements	29.6
Total Imports	747.8	Total Imports	1109.0

1932		1936	
Coal	35.5	Petroleum crude	35.6
Alcoholic beverages	25.9	Coal	33.8
Machinery exc farm	24.4	Rolling-mill products	24.8
Petroleum crude	24.2	Automobile parts	22.7
Fruits	22.5	Machinery exc farm	21.9
Sugar & products	22.4	Fruits	20.3
Rolling-mill products	20.5	Sugar & products	19.2
Electrical apparatus	15.7	Cotton raw	17.2
Petroleum refined	13.5	Cotton goods	13.0
Cotton goods	13.8	Vegetable oils	12.1
Total Imports	578.5	Total Imports	562.7

1939

Petroleum crude	41.5
Coal	35.9
Machinery exc farm	35.3
Rolling-mill products	23.5
Automobile parts	23.5
Fruits	21.2
Sugar & products	20.3
Farm implements	18.1
Books & printed matter	15.3
Grain & products	15.1
Total Imports	658.2

"Canada Year Book"

the ten leading commodities in each of the five years. These ten regularly accounted for 35-40% of total imports, showing a certain amount of concentration in Canadian import trade. A glance at the tables will show another unexpected feature. The makeup of the top ten did not really change a great deal during the twenty years! Evidently the Canadian economy, despite many minor changes during the interwar period, was geared to operate importing a few important commodities consistently in fairly large quantities (c.f. Chap. 1 sect. d). The importance of six in particular stand out - Petroleum, Sugar & products, Fruits, Coal, Machinery except farm, and Rolling-mill products. The first three are almost "essential imports", Canadian resources in no way being able to supply them for natural reasons. The extensive commercial production of Canadian oilfields is still very problematical, and before the second World War these oilfields had progressed little beyond the stage of mere existence. Coal, because of quality and transportation costs, really comes under the same category. And although the rolling-mill products and heavy machinery industries showed some growth during the period, before 1939 they were relatively minor industries in Canada, being quite unable to supply little more than half the market.

A few other points are worth mentioning. The sudden drop in importance of imports of Alcoholic

beverages after 1935 was not due to a successfully militant Temperance League. It is partly explained by the fluctuations of a luxury good. Domestic production rose to a like extent during the boom, and fell just as precipitously during the depression. But it is mostly explained by the fact that the value figure was influenced by the inclusion from 1921 to 1935 of an excise duty which was very large. The growth of the textile and automobile industries in Canada were naturally reflected in a decrease in imports of finished textiles and an increase in imports of automobile parts. Similarly booms in agriculture - all too few - gave rise to sudden increases in imports of farm implements despite the growing industry in Canada.

Table 9 shows the six leading sources of Canadian imports for the five years. The top six countries regularly supplied over 80% and sometimes as much as 90% of total imports. Here again Canadian trade ran in deep and fairly regular grooves. The overwhelming importance of the United States and the United Kingdom as suppliers is unmistakable; but we shall study that feature more closely in Chapter 4, section c. Until the World Depression France and Japan, and more recently Australia, British India, and the Straits Settlements have been important suppliers. This change of the channels of trade was largely a result of the Ottawa Conference, which stimulated Empire trade at the expense of others. However,

Table 9

SIX LEADING SOURCES OF MERCHANDISE IMPORTS, FISCAL YEARS 1922, 1928, 1932, 1936, AND 1939

($ million)

1922		1928	
United States	516.1	United States	718.9
United Kingdom	117.1	United Kingdom	186.4
France	13.5	France	26.5
Cuba	13.0	Germany	17.1
Switzerland	8.7	Japan	12.5
Japan	8.2	Belgium	9.9
Total Imports	747.8	Total Imports	1109.0

1932		1936	
United States	351.7	United States	319.5
United Kingdom	106.4	United Kingdom	117.9
France	13.6	Germany	9.9
Germany	11.7	British India	7.5
Japan	6.0	Australia	7.3
Netherlands	5.8	Straits Settlements	7.2
Total Imports	578.5	Total Imports	562.7

1939

United States	412.5
United Kingdom	115.6
Straits Settlements	10.6
Germany	10.1
Australia	8.8
British India	8.0
Total Imports	658.2

Sources: "Canada Year Book" and "Trade of Canada, fiscal year ending March 31, 1939"

by 1939 Canadian importers, aided by some reductions in non-Empire tariffs, had resought their evidently more accustomed and profitable sources as Table 10 shows, though the Empire still held a more favourable position

Table 11

DOMESTIC EXPORTS BY CLASSES OF MERCHANDISE, FISCAL YEARS 1922, 1928, 1932, 1936, AND 1939

(% by each class)

Classes	1922	1928	1932	1936	1939
Agr. & veg. products ..	42.9	45.2	35.5	28.6	19.7
Animals & products	18.3	13.5	11.9	11.9	13.1
Fibres & textiles	0.6	0.9	1.0	1.2	1.4
Wood & paper	24.3	23.2	30.5	21.4	23.1
Iron & its products ...	3.8	5.1	2.7	6.2	6.4
Non-ferrous metals & products	3.8	7.4	12.0	25.0	29.4
Non-metallic minerals & products	3.1	2.1	2.3	2.3	2.7
Chemicals & allied products	1.3	1.4	1.8	1.9	2.2
Miscellaneous	1.9	1.2	2.3	1.5	2.0

Source: "Canada Year Book"

vegetable products, Animals and their products, Wood, wood products, and paper, and Non-ferrous metals and their products. The first - Agricultural and vegetable products, once the standby of Canadian export trade - played an alarmingly steady, relative decrease in importance; till just before the second World War it actually stood third. Animals and their products, despite a tendency to follow the general world stagnation in agricultural trade, strengthened towards the end of the period largely due to meat and fish exports. Non-ferrous metals and their

Table 12

TEN LEADING COMMODITY EXPORTS, FISCAL YEARS 1922, 1928, 1932, 1936, AND 1939

($ million)

1922

Wheat	180.0
Newsprint	64.8
Wheat flour	53.5
Planks and boards	39.0
Wood-pulp	35.9
Meats	29.8
Fish	29.4
Cheese	25.4
Oats	18.7
Furs, raw	14.8
Total Dom. Exports	740.2

1928

Wheat	352.1
Newsprint	129.2
Wheat flour	59.9
Planks and boards	55.4
Wood-pulp	47.3
Fish	33.5
Automobiles	24.8
Meats	24.5
Furs, raw	24.0
Barley	23.5
Total Dom. Exports	1233.9

1932

Wheat	115.7
Newsprint	103.0
Wood-pulp	27.7
Fish	23.6
Wheat flour	18.9
Planks and boards	18.8
Copper in forms	13.7
Furs, raw	13.1
Nickel	12.1
Whisky	12.1
Total Dom. Exports	600.0

1936

Wheat	148.6
Newsprint	90.8
Non-monetary gold	83.4
Nickel	41.6
Wood-pulp	28.1
Planks and boards	27.6
Fish	24.4
Meats	24.2
Automobiles	23.9
Copper in forms	23.7
Total Dom. Exports	849.0

1939

Newsprint	107.4
Non-monetary gold	87.6
Wheat	84.5
Nickel	49.6
Copper in forms	42.2
Planks and boards	37.1
Meats	35.4
Wood-pulp	26.8
Fish	25.6
Aluminum	24.8
Total Dom. Exports	927.0

Source: "Canada Year Book"

products showed an enormous growth since the first Great War, expanding continuously, till they were easily the most important class of export in 1939, much larger even than the Wood products class, which held a dominant position throughout the period. If non-monetary gold were excluded the percentage accounted for by Non-ferrous metals in 1932, 1936, and 1939 would be 9.8%, 16.3%, and 21.3% respectively with a corresponding addition to the other classes. In that case, in the fiscal year 1939 Non-ferrous metals dropped to third place, very close behind Wood products and Agricultural products.

The character of merchandise exports is further delineated if we draw up, as we did with imports, the ten leading commodity exports for each of the five years. Several interesting facts immediately become available. First of all, the ten top exports accounted for 55-65% of all domestic exports! That is an exact mathematical expression of our earlier contentions concerning the concentration of Canadian effort in the production and export of a few staples. However, there is an interesting point to note. The trend was away from this concentration. Each year the leading ten accounted for a slightly smaller share in the total. Canadian export trade was very slowly broadening, even during the difficult interwar years.

Despite this general tendency there is a second fact to note, and that is the importance of five particular

items - Wheat, Newsprint, Planks and boards, Wood-pulp, and Fish - all important Canadian staples. The first two between them almost carried export trade. Meats and Wheat flour were also very heavy exports, though the latter, with Wheat, declined steadily in relative importance. Just prior to the second World War the displacement of Wheat by Newsprint as Canada's largest export is most significant, and was due not so much to the growth of the newsprint market as to the serious decline of the world wheat market. Though Wheat was still important, it was a mere shadow of its former self.

Despite the prominence of these few exports, leading exports as a whole tended to change more than leading imports (c.f. Table 8 on p.44). The Empire market for automobiles (protected) was equally responsible with the domestic market for the growth of the automobile industry. And the growth of Non-ferrous metals was reflected in the growing importance of gold, nickel, copper, and aluminum exports.

So far as markets are concerned a glance at Table 13 reveals that 80-90% of Canadian Domestic Exports went to the leading six markets, a concentration similar to the one we noted in import sources. And these markets were pretty regular customers. The United States and the United Kingdom absorbed almost the whole portion of Canadian exports (c.f. Chap. 4, sect. c); but Japan too

Table 13

SIX LEADING MARKETS FOR DOMESTIC EXPORTS, FISCAL YEARS 1922, 1928, 1932, 1936, AND 1939

($ million)

1922		1928	
United Kingdom	299.4	United States	483.7
United States	292.6	United Kingdom	410.7
Italy	15.3	Germany	42.2
Japan	14.8	Netherlands	35.5
Belgium	12.4	Japan	33.0
Australia	10.7	Belgium	20.8
Total Dom. Exports	740.2	Total Dom. Exports	1233.9

1932		1936	
United States	257.7	United States	360.3
United Kingdom	174.0	United Kingdom	321.6
France	18.0	Australia	24.0
Japan	16.6	Japan	14.8
Belgium	14.0	British South Africa	13.5
Netherlands	13.5	Belgium	11.1
Total Dom. Exports	600.0	Total Dom. Exports	849.0

1939	
United States	375.9
United Kingdom	325.5
Australia	35.3
Japan	21.0
Germany	17.8
New Zealand	17.0
Total Dom. Exports	927.0

Sources: "Canada Year Book" and "Trade of Canada, fiscal year ending March 31, 1939"

was a steady and important customer, as was Belgium. Australia, with an economy almost competitive to Canada's, also assumed (after the Ottawa Agreements) an important role in Canadian export trade.

The approximate distribution of Domestic Exports during the interwar years among the United Kingdom, the rest of the British Empire, the United States, and other Foreign Countries is given in Table 14. The prominence of the United States and the United Kingdom and the growth of the British Empire market after 1932 are obvious. But we must mention the same reservation we made in Table 10, that although this table presents a fair over-all picture it does not show the extent to which exports to the Empire grew from a low of 33.3% of total domestic exports in 1929 to a high of 50.7% in 1933 (calendar years). The falling off of the Empire market just prior to the War was quite sudden, as the percentage of domestic exports going to the Empire in the year ending December 31, 1938 was 48.5%[1], whereas in the year ending March 31, 1939 it was the 46.2% shown in Table 14.

Table 14

DOMESTIC EXPORTS GOING TO BRITISH EMPIRE AND FOREIGN COUNTRIES, FISCAL YEARS 1922, 1928, 1932, 1936, AND 1939

(% to each market)

	1922	1928	1932	1936	1939
United Kingdom	40.4	33.3	29.0	37.9	35.1
Other British Empire	6.3	7.2	7.8	9.1	11.1
United States	39.5	39.2	42.9	42.4	40.6
Other Foreign Countries	13.8	20.3	21.3	10.5	13.2

Sources: "Canada Year Book" and "Trade of Canada, fiscal year ending March 31, 1939"

[1] "Review of Canada's Foreign Trade, Calendar Year 1938"

Chapter Four

EFFECT OF THE CHARACTER OF CANADIAN FOREIGN TRADE ON THE ECONOMY

a) Characteristics of Canadian foreign trade

The main characteristics of Canadian foreign trade have been drawn from the statistical examination of Chapter 3. Some of these presented peculiar difficulties to the Canadian economy, and, because of their profound influence on the future course of Canadian foreign trade in particular and economic policies in general, are worth further analytical study. This chapter we devote to that study.

First of all, it may be profitable to summarize the main characteristics evident during the interwar period that we discovered in Chapter 3. These were:

1) an extremely large volume of merchandise trade
2) violent fluctuations, more serious in value than volume
3) with few exceptions, an active balance of merchandise trade
4) a fairly high specialization in imports, most of which filled the gaps in Canadian natural resources and production

5) an extremely high specialization in exports, whose total value depended mainly on a few staples

6) a narrow circle of sources and markets with the United States and the United Kingdom outstanding

That kind of a foreign trade situation naturally was part of a very definite set of circumstances, which we described briefly in Chapter 1, and to some particular aspects of which we now turn our attention.

b) Rigidity in the Canadian economy

Instability in the level of foreign trade was serious for the Canadian economy because that economy was most vulnerable to attack from that direction. Without involving ourselves in a circular argument we can grant from Chapter 1 that Canadian prosperity depended largely on the level of foreign trade attained. In wheat, newsprint, and non-ferrous metals Canada supplied an overwhelming portion of the quantities entering into international trade. However, she produced a much smaller portion of total world production in those products. In other words, despite her advantages in production, she was a marginal source of supply in many cases (a disadvantage in a falling market). If a country chose to reduce consumption of, say, wheat, it was its imports, not its domestic production, that it reduced. But Canada only consumed a fraction of her staple production herself. A large external market was a "sine qua non" for competitive

production. Consequently a decline in the world market fell heavily on Canada.

If, then, export trade consisted of a few commodities in large quantities, and the world market in those commodities deteriorated, the Canadian economy suffered. Unluckily, the commodities on which Canada depended so much for export were greatly affected during the economic wars of the thirties. Canadian wheat found fewer buyers in a world aiming at national self-sufficiency. The ordinary qualifications of price and quality just did not apply. And even the Ontario politician now realizes that Ontario factories could not operate to capacity if the prairie farmer were broke.

We intimated earlier that Canadian production depended on the production of a few staples in large quantities. This policy, necessary as it was for development, was of a spiral nature. Canadian productive effort became concentrated. The country produced little else. It became a matter of producing those products or nothing. It was wheat or nothing, newsprint or nothing, nickel or nothing, aluminum or nothing. Effort centered around a few large industries which became mainly export industries. Size and methods of production demanded heavy capitalization with a resulting burden of fixed charges that could not be borne (as in the case of the newsprint-pulp industry) when export markets dropped.

Their difficulties, because of their size, immediately reverberated throughout the economy.

These rigidities in export industries would not have made fluctuations in exports so serious for the rest of the economy were it not for the fact that these industries formed such an integral part of the economy. They only aggravated other rigidities manifest throughout - the specific quality of resources, the immobility of fixed capital and labour because of climate and distance, the massive transportation system - to name only a few.

c) Canadian-British-American triangle

Canadian history in many respects has been an attempt to be alternately neither British nor American. Nevertheless the strength of the spiritual and political British ties and of the economic American ties occasioned by the proximity of such a massive and wealthy economy could not be denied. Though the result of the stress and strain of these two forces has been no doubt peculiarly Canadian, their separate marks have been clearly discernable in almost every phrase of Canadian life, and nowhere more clearly than in Canadian trade relations. This singular relationship with the United Kingdom and the United States complicated further the rigidities we have mentioned.

Although the outstanding positions in Canadian foreign trade assumed by the United Kingdom and the United

States were clear in Tables 10 (p.48) and 14 (p.54), we supplement those tables with Table 15 in order to present a complete picture. The choice of years (calendar) in Table 15 illustrates accurately the swing of the trade pendulum towards the United States during the boom, then the greater swing back towards the United Kingdom during the World Depression followed by the slow return to a more central position after 1935. Despite these minor movements the evidence is irrefutable. Approximately 30% of Canadian merchandise trade was carried on with the United Kingdom and approximately 50% with the United States.

Table 15

CANADIAN MERCHANDISE TRADE WITH UNITED KINGDOM AND UNITED STATES

(% with each country)

	United Kingdom		United States	
Year	Imports	Dom. Exports	Imports	Dom. Exports
1926	16.4	36.1	66.3	36.9
1929	15.0	24.5	68.8	44.3
1933	24.4	43.3	54.2	31.5
1935	21.2	37.2	56.8	43.4
1937	18.2	36.4	60.6	42.3
1938	17.6	37.2	62.6	37.9

Source: "Review of Canada's Foreign Trade, Calendar Year 1938"

Undoubtedly the leading force in these swings in the trade pendulum was tariff policies. It is an undisputed fact that the Hawley-Smoot tariff and the Ottawa Agreements diverted a part of the accustomed American share of Canadian merchandise trade to the United Kingdom, which was later in some measure returned by the Canadian-American trade agreements of 1935 and 1938 abetted by the inability of the United Kingdom to maintain exports just prior to the war. But the character of trade between Canada and the United States and Canada and the United Kingdom was also an important force. Canadian imports from the United States consisted largely of durable producers' goods and Canadian exports to the United States of industrial raw materials, commodities that would be imported in large quantities during periods of high business activity but that would fall off badly during depressions. Whereas Canadian exports to the United Kingdom consisted largely of basic foodstuffs, which, even if they declined slightly in absolute value, would certainly gain a larger share of total trade during trade depressions.

Table 15 reveals to some extent the dependence of Canada on the British and especially the American economies. The United Kingdom was important chiefly as a market, for it took by far the largest share of Canadian farm staples. And normally 2/3 of Canadian imports came from the United States. This list of imports

was not only long, it contained basic needs such as coal, oil, and iron. The importance of British and American trade to Canada is, then, pretty obvious.

The weak part of the Canadian position was the comparative unimportance of Canadian trade to the United Kingdom and the United States. Now admittedly the British standard of living depended greatly on the importation of large quantities of Canadian agricultural and animal products. If these had been stopped the British consumer would have suffered serious shortages of bread, cheese, bacon, and so forth. But all in all Canadian-British trade accounted for approximately 5% only of total British merchandise trade 1919-1939[1]. The position with the United States was no better. Canada supplied a large portion of American newsprint and non-ferrous metals requirements. But Canadian-American trade accounted for approximately 15% of total American merchandise trade 1919-1939[2].

Consequently Canada felt to a much greater degree any changes in trade policy on the part of the other two corners of the triangle. Her poor bargaining position dulled many possible weapons she could have used in her defence. She was in possession of no big

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[1]Computed from "Statistical Abstract of the United Kingdom". After 1932 the annual percentage increased slightly, ranging from 5 to 8 %.

[2]Computed from "Statistical Abstract of the United States".

stick to wave in front of a fire-proof Uncle Sam as he initiated the Hawley-Smoot tariff, when the goods the United States sold to Canada amounted to a mere 18% of American exports and all of 69% of Canadian imports while the goods Canada sold to the United States amounted to 44% of Canadian exports and only 11% of American imports. The difficulties faced by the Canadian economy were only enhanced by the concentration of her trading relations.

If the confining of Canadian merchandise trade to a narrow triangle and the heavy dependence of the Canadian corner on the other two corners made the unstable character of the Canadian economy more precarious, at least the flow of trade in that triangle was of such a character that it maintained itself. Canada exported more to, than she imported from, the United Kingdom; and she imported more from, than she exported to, the United States. Figuratively speaking, she took the £ she received in London for prairie wheat to New York and exchanged them for U.S.$ to buy Pennsylvania coal. The fortunate part about the whole arrangement was that these balances in merchandise trade (a credit one in £ with the United Kingdom, and a debit one in U.S.$ with the United States) were usually just about equal. During the period they ranged from approximately $50 million to $200 million.

This triangular aspect of Canadian trade functioned exceedingly well as long as the £ and the U.S.$

were comparatively stable in relation to each other. When the £ was high the Can.$ also was at a premium in New York, but not as high as the £. When the £ was low the Can.$ dropped in relation to the U.S.$ in the process of bidding it up. This situation was largely responsible for the fact that the Can.$ regularly sought a position about midway between the £ and the U.S.$. The exact position the Can.$ found was not always the same. But for periods of time, as studies have shown[1], it has been definitely measurable.

If, at any time, the £ should not be freely convertible, or it should suffer a severe drop in New York, Canadian imports from the United States would certainly face a serious problem. Even if the British market were maintained to some extent the flow of Canadian trade would obviously have to jump the confines of the triangle.

d) Barter terms of trade

The Canadian situation described in sections b) and c) above was quite satisfactory in a world of free and stable trade relationships. In such a world the country, specializing in the production of those products in which she enjoyed a comparative advantage, could reap the full advantages of a world division of labour. However, it was the kind of a situation that put the

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1 "Bank of Nova Scotia Monthly Review", December 1933

country at the mercy of foreign policies. When those policies turned towards nationalistic self-sufficiency and the markets of the world were no longer fully influenced by costs of production Canadian exports fell precipitously, a fall that was in no way broken by a mobility of resources within the country or by an equal resiliency in imports.

A general decline in prices is a serious matter in any event. Besides the over-all economic hardship caused by falling prices there is the added hardship to particular groups caused by individual prices getting out of line. When prices move, they just won't move in unison. But a price movement that is even worse for any country is one in which (beyond individual inequalities) export prices as a whole drop more than import prices as a whole, particularly when that country finds it more difficult to reduce the quantity of goods it buys from its customers than its customers find it to reduce the quantity of goods they buy from it. And that is what happened to Canada.

The prices of raw materials tend to fluctuate more than the prices of finished products at the best of times. And the economic policies of 1919-1939 only aggravated that tendency. The difficulties through which world trade in basic raw materials floundered in the thirties dwarfed many of the other economic evils of the

time. And remember Canadian export trade was made up predominantly of raw staples. Hence, if prices fell, the country was faced with the necessity of increasing the quantity of its exports to maintain total value and balance its international payments. It was a vicious circle; the more was put on the market for export, the more prices fell. Even in a free market the situation would have been difficult, as the elasticities of demand for the Canadian export staples almost certainly were less than unity. (This was not helped by the tendency of the supply of many agricultural products to be regressive - i.e. as the price drops more rather than less is produced.) And foreign demand was further restricted by nationalistic trade policies. So that if export prices fell the country could not increase the volume of exports sufficiently to make up for the fall in prices (c.f. the wide divergence between volume and value in Chart VI, p.36). Imports on the other hand consisted more largely of manufactured goods, whose prices tended to remain more stable, goods, many of which, Canada found difficult to do without. In the words of the Canadian-British-American triangle Canada had to buy more U.S.$ with less £.

The difference between the composition of import and export trade is shown in Chart VIII. Never were more than 30% of the goods Canada imported in the completely raw form, whereas sometimes almost 50% of

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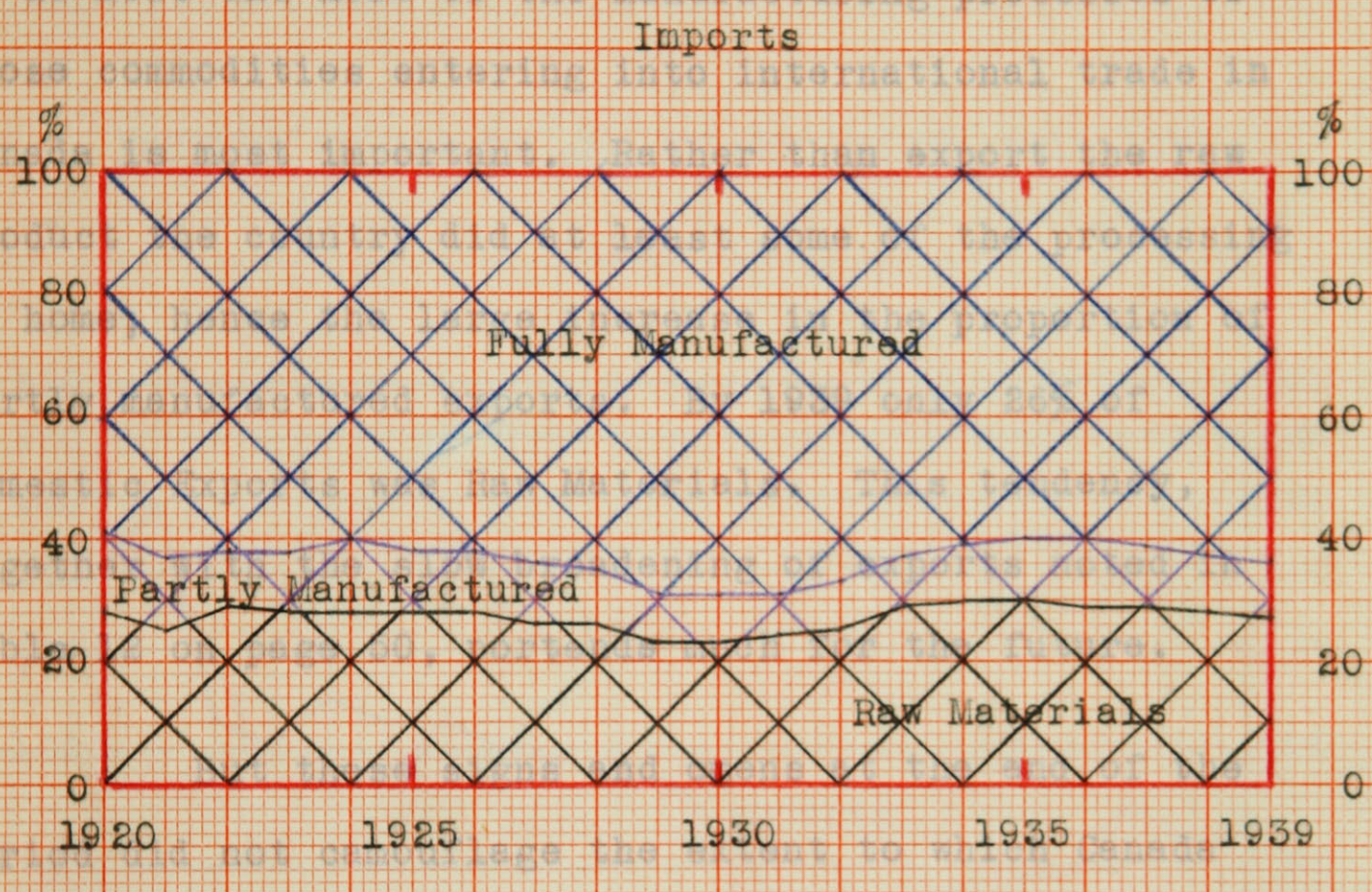
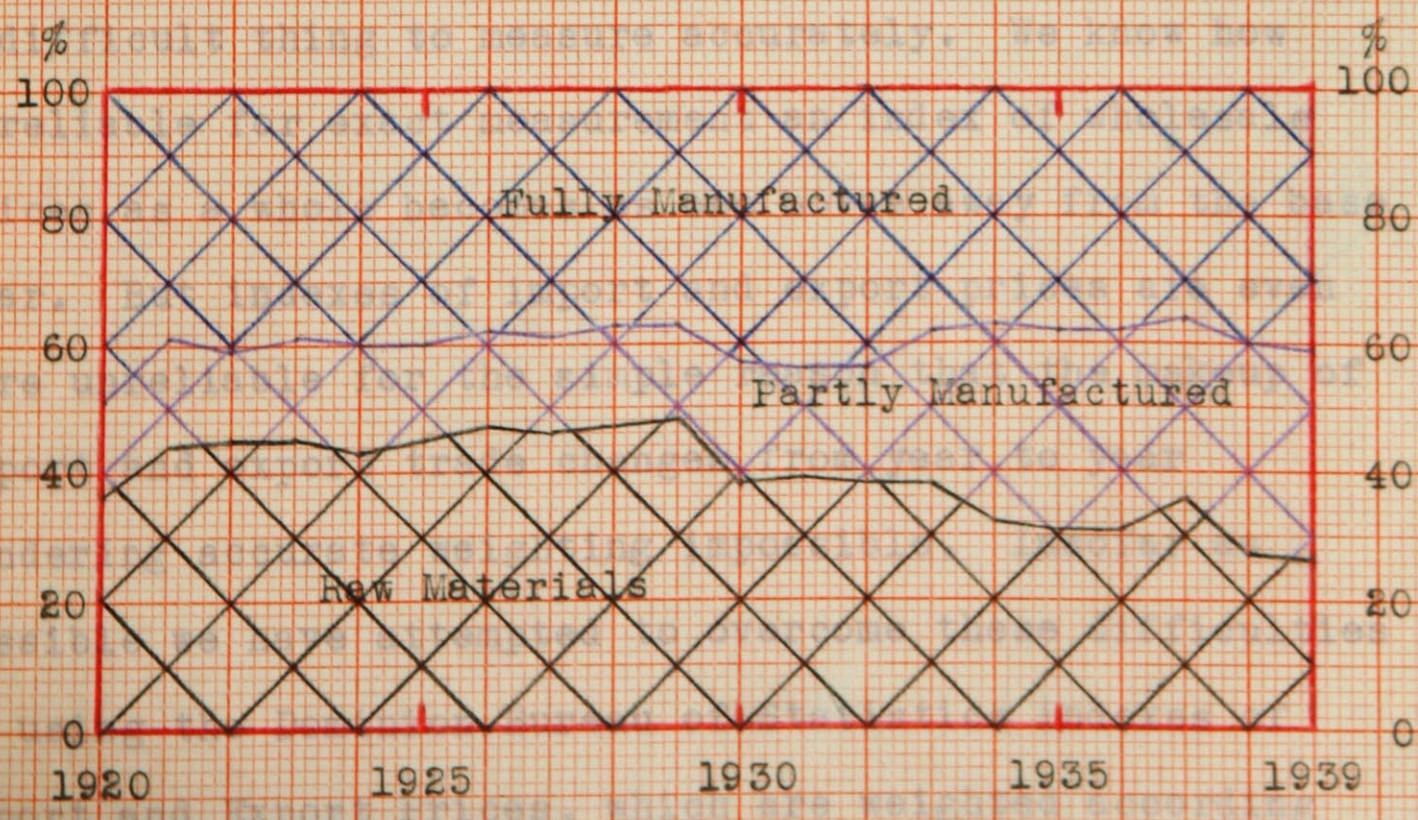
Chart VIII

PROPORTIONS OF TRADE IN RAW AND MANUFACTURED PRODUCTS, FISCAL YEARS 1920-1939





Sources: "Condensed Preliminary Report on the Trade of Canada" and "Canada Year Book"

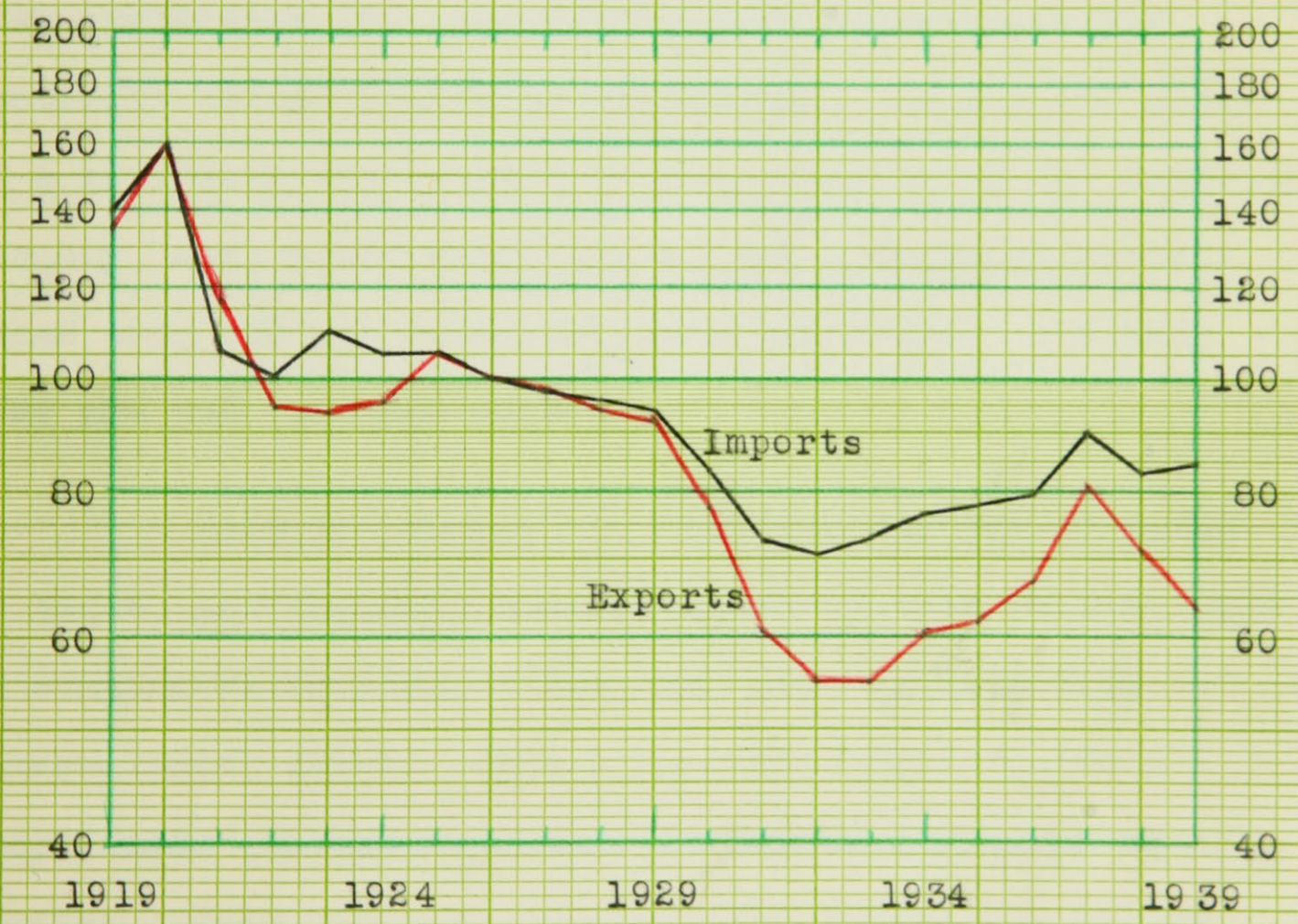
exports were raw materials. At least 60% of imports were fully manufactured, whereas only some 40% of exports were completely finished. However, the tendency, particularly noticeably during the thirties, to do more and more of the manufacturing processes of those commodities entering into international trade in Canada is most important. Rather than export the raw product the country did at least some of the processing at home; hence the large increase in the proportion of partly manufactured exports. By 1939 only 26% of Domestic Exports was Raw Materials. This tendency, together with the slow broadening of exports noted in Table 12 on page 50, portends much for the future.

But these signs and omens at the end of the period did not camouflage the extent to which Canada suffered from the barter terms of trade throughout most of the twenty years. Now the barter terms of trade are a difficult thing to measure accurately. We know how unreliable for exact measurement an index of wholesale prices as a whole becomes as one moves away from the base year. But indexes of import and export prices are even more unreliable for the simple reason that the makeup of import and export trade changes from year to year rendering accurate weighting impossible. Insofar as possible we have attempted to overcome these difficulties by using the Dominion Bureau of Statistics indexes of Import and Export Prices, which are weighted according

Chart IX

INDEXES OF IMPORT AND EXPORT PRICES 1919-1939

(1926=100)



Source: Appendix I

to an average of imports and exports for the years 1926-1931. Further, the indexes are plotted on Chart IX to a logarithmic scale, which shows the relative change from year to year. In that way we can more faithfully portray the changes in the barter terms of trade.

From Chart IX it is noticeable that during bad years, during periods of falling prices, the terms became progressively worse. Instead of cushioning a fall, they aggravated it. But during good years the terms generally became progressively better. It was the kind of a situation very common to many aspects of the Canadian economy, most aptly described by the schoolgirl ditty - "when they are good they are very, very good, but when they are bad they are horrid".

However, it must be admitted the barter terms of trade, particularly when measured in this fashion, are no conclusive measure of the real gain or loss from international trade. Such a measure would require a complicated statistical analysis beyond the scope of this chapter. What is more, we must look behind the barter terms. A supposed worsening of the terms of trade as measured by Import-Export Prices may have been due to improvements in Canadian production whereby export prices were lowered. And, as a matter of fact, the mechanization of Canadian agriculture did have some such effect. In such a case the deterioration in the real terms of trade

would have been somewhat less than that shown by the barter terms. Just the same, in the Canadian case, the barter terms worsened in such a way and to such an extent that they undoubtedly were a further cause of stress to the Canadian economy.

e) Balance of trade

The difficulties Canada experienced due to falling markets for her export commodities are seen in her Balance of Merchandise Trade for the period (Chart X). A country in Canada's position on international account should normally have been paying the considerable sums of interest and dividends due on foreign investment and retiring foreign-held Canadian securities as they matured. That is, she should normally have had an active merchandise trade balance on Current account if she was to maintain a healthy balance of payments. If ever world trade conditions so deteriorated that her trade balance became passive she would either have had to repudiate her foreign-held debts or finance them in some other way.

A glance at Chart X shows us the irony of the situation. The Balance of Merchandise Trade, though normally active, turned passive during exactly those periods when the Canadian economy could least afford it. Luckily, for the greater part of the interwar period the balance remained active to a considerable extent and was reflected in a comparatively sound balance of payments.

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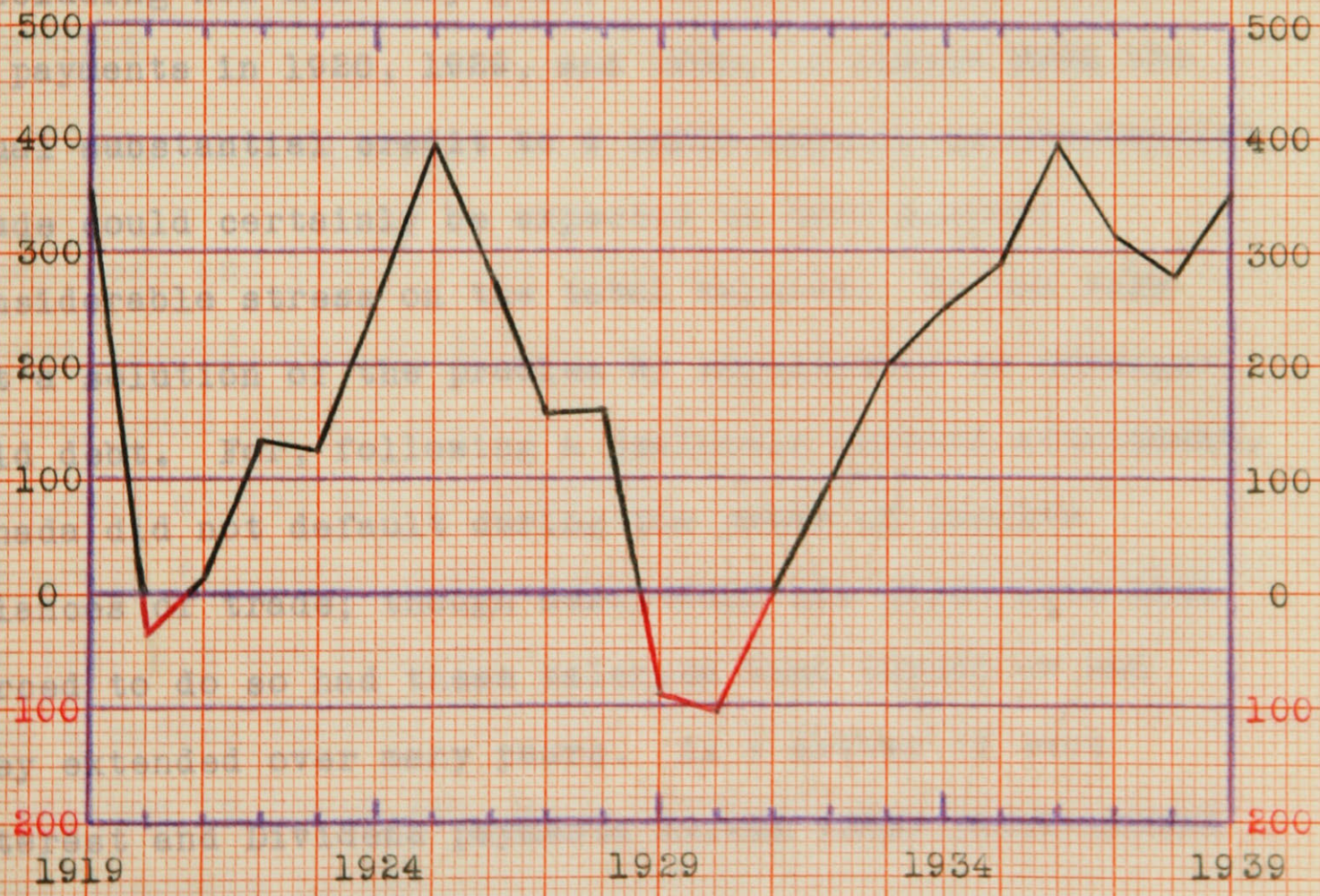
Chart X

BALANCE OF MERCHANDISE TRADE 1919-1939

Credit Balances, Debit Balances

($ million)



Source: Appendix I

Chapter Five

FOREIGN INVESTMENT 1919-1939

a) Solution of passive balance of trade

We drew attention in the last chapter to a very unstable element - a passive balance of merchandise trade (including non-monetary gold) - in the Canadian balance of payments in 1920, 1929, and 1930. A change from the usual substantial credit to a debit balance on merchandise trade could certainly be expected to have exerted considerable stress on the total balance. We can rule out a solution of the problem by repudiation of foreign-held debt. For, following a jealously guarded attainment, Canada did not default during the years of passive balances of trade; though admittedly she might have been forced to do so had these balances been larger or had they extended over many years. As a matter of fact Interest and Dividend payments during those years showed little tendency to sag.

We are left, then, with the solution that there must have been a heavy increase in credits (most probably on Capital account) during those particular years. And that is the way it worked out, as Table 16 shows. Previous to 1929 there had been a marked tendency to

Table 16

ESTIMATED CANADIAN BALANCE OF INTERNATIONAL PAYMENTS

NET BALANCES ON CAPITAL ACCOUNT 1928-1933

Net Credits or Debits

($ million)

	1928	1929	1930	1931	1932	1933
New Issues and Retirements of Can. Securities	7.3	146.6	290.3	2.1	1.0	32.0
Other Securities Transactions	188.0	105.0	13.0	24.0	16.0	51.0
Other Capital Movements	98.7	126.3	38.0	61.8	5.6	51.4
Net Credits or Debits	82.0	167.9	315.3	35.7	11.4	32.4

Source: "Canadian Balance of International Payments, 1939"

float less and less of new Canadian bond and security issues abroad, and to retire more and more of those already held abroad instead of refunding them. A Canadian financial market was growing up. Canadian public and corporate financial needs were being met at home. Figures for 1920 are not available, but those for 1929 and 1930 show a sudden reversal of this tendency. Table 16 shows that on balance in those two years there was a sudden and very heavy increase in new issues abroad while retirements were very small indeed. Canadians resumed their heavy borrowing in foreign quarters while loaning a good deal less abroad. During those years Capital account swung easily to a credit balance, maintaining equilibrium in the balance of

payments. Because Canadian investment appeared a good venture to the foreign lender Canada was able to resume temporarily her role of international borrower on balance, accept a debit balance on Current account, and keep her balance of payments relatively stable.

b) Debtor position 1919

We can see, then, the profound influence Canada's position on capital account has on her merchandise trade. So that a brief examination of Canadian international investment during the interwar period will explain wartime changes and provide an understanding of the position in which Canada finds herself as she enters the postwar world.

By 1919 there was an estimated $4,636.8 million of foreign capital invested in Canada, over 57% of which was British owned[1]. It had come in two bursts of capital importation; the first, from 1900 to 1913 when the United Kingdom invested $1,700 million of a total of $2,500 million invested during the period, the second, from 1914 to 1919 when the United States, as sole investor, invested some $1,000 million.

Against this huge holding of Canadian capital by foreigners ($4,636.8 million) Canadians had invested abroad by 1919 to the extent of some estimated $942 million only[1]. From 1900 Canadian investments had shown

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[1] Excursus on "Canadian Capital Movements and the Canadian Balance of International Payments 1900-1934" by F. Knox in "Canadian-American Industry"

a steady, if slow, growth. In fact during the first Great War they had more than doubled. However, this trickle was not sufficient to balance foreign investment in Canada and prevent the country from being one of the world's largest debtors in 1919.

c) Foreign investment in Canada to 1939

Foreign investment in Canada, particularly American, continued heavily till 1930 when the estimated total foreign investment in the country was $7,613.8 million (c.f. Table 17). It is generally estimated that

Table 17

ESTIMATED FOREIGN INVESTMENT IN CANADA

($ million)

Year	United Kingdom	United States	Other	Total
1919	2645.2	1818.1	173.5	4636.8
1926	2636.3	3196.3	170.0	6002.6
1930	2766.3	4659.5	188.0	7613.8
1933	2682.8	4491.7	190.0	7364.5
1939	2465.9	4190.0	270.0	6925.9

Sources: 1919 - Knox op. cit., 1926-1939 - "Canadian Balance of International Payments, 1926-1944"

during the thirties almost 40% of Canadian capital (excluding farms and homes, but including funded government debt) was owned by foreigners[1]. However, during that

[1] "Canada Year Book"

decade an active trade balance enabled Canada to reduce this foreign-held debt slightly. Consequently the record of the thirties is one of increasing debits on capital account. In fact from 1930 to 1939 foreign investment in Canada was reduced by some $700 million. The latest estimate by the Dominion Bureau of Statistics in 1945[1] places total foreign investment in 1939 at $6,925.9 million. Earlier estimates had put the 1937 figure at $6,765.0 million[2], which, by inference, would place the 1939 figure lower than that. At any rate it seems to be generally agreed that by 1939 foreign investment in Canada amounted to $6.5-7.0 billion, no inconsiderable amount.

An important consideration so far as foreign trade and the balance of payments are concerned is not only the distribution of ownership noted in Table 17 on page 75 but the type of investment held. This we show in Table 18 which follows, using the latest estimates released by the Dominion Bureau of Statistics, which may slightly overstate the case. The three obvious things to note are the British holdings of Railways, the American holdings of Government Securities, and the American holdings of Manufacturing. The last is what interests us here. Of the $1,919.5 million of American investment in Canada that was in enterprises controlled in the United States $983.7 million was in manufacturing

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1. "Canadian Balance of International Payments, 1926-1944"
2. "Canadian Balance of International Payments, 1939"

Table 18

ESTIMATED FOREIGN CAPITAL INVESTED IN CANADA

CLASSIFIED ACCORDING TO TYPE, 1939

($ million)

Type	United Kingdom	United States	Other	Total
Government Securities	408.0	1241.0	23.0	1672.0
Railways	1250.3	588.3	67.0	1905.6
Other Public Utilities	89.3	470.7	28.0	588.0
Manufacturing	257.3	1159.9	28.0	1445.2
Other	461.0	730.1	124.0	1315.1
Total	2465.9	4190.0	270.0	6925.9

Source: "Canadian Balance of International Payments, 1926-1944"

enterprises[1]. The definition of American control is a hazy one, but the fact remains that an extremely large proportion of American capital was a direct investment in the form of branch plants. This certainly had an effect on foreign trade, particularly in respect to surmounting the Empire tariff preferences, but to what extent it decreased Canadian-American trade is impossible to estimate.

The fact that so much of the American investment during the twenties was of the direct variety helps explain why Capital account during that decade seemed to show no

[1]The "Canadian-American Industry" study by Marshall, Southard, and Taylor places the portion of manufacturing done in Canada by American controlled companies at 25%.

large credit balances. The total amounts in the Canadian balance of payments had grown to such an extent that other items could compensate for the large importation of American capital. Hence, although this importation was reflected in a heavy passive balance of merchandise trade vis-a-vis the United States, the even larger active balance of merchandise trade the country obtained vis-a-vis the rest of the world (due partly to the increased industrialization consequent on the opening of branch plants) allowed Canada on balance, especially during the thirties, to show a net export of capital. Consequently we should expect to see some considerable increase in Canadian investment abroad during the interwar period.

d) Canadian investment abroad to 1939

The latest estimate by the Dominion Bureau of Statistics ("The Canadian Balance of International Payments, 1926-1944") gives Canadian investments abroad for 1939 only, and places these at $1,340 million. In order to use continuous figures for the interwar period, then, we shall have to use the earlier estimates made in "The Canadian Balance of International Payments, 1939". These are somewhat higher than the more recent estimate as they place the 1937 figure at $1,757.9 million. However, it would seem we can safely say that, relatively speaking, Canadian investment abroad increased to a greater extent than foreign investment in Canada. Its

rate of growth was the larger (c.f. Table 19). But in absolute amounts the increase in foreign investment in Canada was the larger (c.f. Table 17, p.75). As can be seen from Table 19 the total sum of Canadian investment abroad was hardly comparable to foreign investment in Canada. However, we must admit that prior to the second World War that sum was not inconsiderable. Its size plus its tendency towards steady growth made its importance to future foreign trade easily recognizable.

Table 19

ESTIMATED CANADIAN INVESTMENT ABROAD

($ million)

Year	United Kingdom	United States	Other	Total
1919	--	--	--	941.7
1926	59.6	778.0	515.2	1352.8
1930	67.7	933.1	651.8	1652.6
1933	49.0	875.7	645.8	1570.2
1937	40.9	1097.6	619.4	1757.9

Sources: 1919 - Knox op.cit., 1926-1937 - "Canadian Balance of International Payments, 1939"

Here again we note rapid growth during the twenties. But in this case Canadian investment abroad resumed its course in 1934 after the setback of the World Depression. In decided contradistinction to British investment in Canada Canadian investment in the United Kingdom was negligible. On the other hand the

overwhelming importance of the United States in the Canadian picture was reflected here as elsewhere. The unexpectedly heavy investments of Canadians in other countries is most important. Figures here are unreliable, but it is known that there were considerable Canadian interests in South America.

Although most Canadian investment abroad was of the short-term variety there was considerable direct investment in other countries. In fact, relative to population there was more Canadian direct investment in the United States than American direct investment in Canada[1]. In 1937 of an estimated total of $510.7 million direct investment abroad $327.9 million was placed in the United States[2]. Canadian interests lay mainly in railways and other public utilities in the United States, and also in manufacturing establishments in that country, and in mining and petroleum operations in South America.

That, briefly, was the foreign investment picture at the outbreak of war in 1939. Foreign holdings of capital invested in Canada, though admittedly extremely large, presented no outstanding difficulties to the Canadian balance of payments. They had in fact passed their zenith, and showed a tendency (American direct investment included) to be replaced by domestic investment.

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1 "Canadian-American Industry" by Marshall, Southard, and Taylor

2 "British and Foreign Direct Investments in Canada and Canadian Direct Investments Abroad, 1937"

Against these huge sums Canadian investment abroad seemed very small indeed; but in fact it represented a considerable amount. And when considered in connection with the size of the Canadian economy it reflected a growing strength.

Chapter Six

THE CANADIAN ECONOMY GROWS UP

a) The miracle of production

Whether Canadians are aware of the fact or not Canada has emerged from the war as a near-great power. This responsible position has been won, not so much by the might of her sword, though this has been considerable, but by the unexpected strength of her economy that forged it. Canadians still appear to be not a little surprised that a mere 11½ million people could accomplish so much with an economy they had grown to believe was a bit hopeless. They rather believe that the statistics released by the various cabinet ministers portraying such a stupendous war effort are so much party propaganda. Until they themselves understand the import of the potential of their economy revealed by the war there is little sense in broadcasting their accomplishments to the uneducated foreigner. It is bad policy to put a little boy in a man's pair of shoes just because the shoes have been fashioned, as the world so ruefully learned from the United States during the interwar period.

Actually there is nothing mysterious about the

sudden maturity displayed by the Canadian economy. It has been a perfectly natural coming of age that was only accelerated by the war to the possible advantage of the country. The complete story of this sudden acceleration, of the prodigious quantities of goods that spilled from the Canadian productive machine, has yet to be written. But from the welter of statistics released thus far we can pick out a few which bear directly on our thesis and which will undoubtedly have much influence on the course of postwar foreign trade.

By 1939 the value of production had laboriously regained the position it had attained during the 1929-1930 boom. But by 1943, incited by the gods of war, the Net Value of Production had leapt from the 1939 figure of $3,224 million to the unprecented height of $6,325 million[1]. That, in the short space of four years! The Gross Value of Production in 1943 stood at $12,024 million[1]. Statistics available for 1944 reveal little change during that year; and it is probable 1945 was only slightly lower.

All branches of production, both primary and secondary, naturally showed very considerable gains; but the outstanding gain was shown in manufactures. In 1920 agriculture accounted for 40% and manufactures for less than 33% of the net value of production. In 1939

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[1] "Canada Year Book"

agriculture accounted for 26% and manufactures for 47%. And in 1943 agriculture accounted for 20% and manufactures for 60%. Those statistics[1] tell the story of the Canadian economy during the last quarter century. They reveal the story of a maturing, increasingly diverse economy. They reveal that this growth, swift as it was, was greatly accelerated by the war.

The increase in agricultural production during the war was actually accomplished with a considerable decrease in agricultural employment and little increase in acreage - a rather startling revelation. Certainly the contribution Canadian farms and farmers made to feeding the United Nations was important and most deserving of the publicity it received. But the most important factor in wartime growth from our point of view was the revolution that occurred in Canadian industry. And it <u>was</u> a revolution. In 1939 the Gross Value of Manufacturing amounted to $3,475 million (net value $1,531 million), in 1943 it amounted to $8,733 million (net value $3,816 million)[2]. That growth of $5,258 million was generated and directed by a revolutionary (for the Canadian economy) institution - the Department of Munitions and Supply, an autarchic institution which encouraged, supplemented, controlled, and, if need be, bullied private enterprise in order to achieve the ends it sought. The great proportion of increased production

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[1] Computed from "Canada Year Book"
[2] "Canada Year Book"

was, of course, war material (in 1943 64% of total productive capacity was used for war purposes[1]). But in so becoming an arsenal for democracy, in producing the tools of war, the Canadian economy underwent a swift industrial revolution which, if it can be consolidated, may change considerably the nature of its peacetime foreign trade.

Table 20 presents some of the changes in material production which will bear heavily on postwar trade. These are merely a few striking and basic examples. They do not adequately describe the plethora of new products manufactured in Canada for the first time, many of them entirely new products, others, formerly imported. They do not describe the vast extensions in existing industries, most notable in the aluminum, chemical, steel, and automobile industries. A few examples from the latter two industries will illustrate the point. The new iron ore development at Steep Rock, Ontario is most promising. It is estimated that it will produce at least 2 million tons of exceptionally high grade ore annually, giving Canada a new primary industry of considerable size. More important than the increase in the capacity of the Canadian steel industry are improvements in quality and extensions in types and forms of steel. The domestic market's requirements in rolled steel can now be largely satisfied

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[1] "Canada Year Book"

Table 20

CANADIAN PRODUCTION 1939, 1943, AND 1944

	1939	1943	1944
Iron ore (000 short tons)	124	641	553
Pig iron (000 short tons)	846	1,758	1,853
Ferro-alloys (000 short tons)	86	219	182
Steel ingots and castings (000 short tons)	1,551	2,997	3,024
Chromite (short tons)	--	29,595	27,054
Molybdenite (tons)	1	592	1,064
Aluminum (000,000 lbs.)	166	991	924
Magnesium (000 lbs.)	--	7,154	10,580
Tungsten concentrates (000 lbs.)	9	1,509	887
Petroleum (000 bbls.)	7,826	10,052	10,099
Rubber (000,000 lbs.)	--	9	87
Machinery ($000,000)	48	159	144
Machine tools ($000,000)	4	20	*
Aircraft ($000,000)	13	246	*
Ship-building ($000,000)	11	377	*
Automobiles ($000,000)	107	352	324

Sources: Dominion Bureau of Statistics publications
* not available

by Canadian production. So far as the automobile industry is concerned, its possibilities are realized when it is considered that $107 million of vehicles were turned out in 1939, and $352 million in 1943. They do not describe the several thousand vast modern plants which were built, equipped with the latest machinery. During the war the

government provided over $750 million and private enterprise another $500 million for new or expanded production facilities[1]. Many of these new plants were tooled by a new Canadian machine-tool industry, an industry that in four years has achieved major status. Nor do they describe the new techniques and production methods Canadian entrepreneurs learned. There is no doubt about it that the Canadian industrialist is now in a position to compete with his American counterpart in many fields in which the latter heretofore held unchallenged supremacy.

Canada verily has undergone an industrial revolution. The vast increase in industrial potential is seen in the increase in Capital Employed in Manufacturing Establishments from $3,647 million in 1939 to $6,317 million in 1943[2], the great part of which is not specific to the production of the tools of war only. A new fixed capital machine is there; all that is required is an effective demand that will encourage the procession of operating capital through it. This new machine is at the disposal of the country as it converts itself to a peacetime basis. Much of it could function in a mature, diverse economy. If the postwar aims of employment and income in a world of comparative economic freedom are attained a large portion of this machine will undoubtedly be used, and the effect on foreign trade will certainly be far-reaching.

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[1] Hon. C. D. Howe in "House of Commons Debates", Wednesday, March 20, 1946, p.118

[2] "Canada Year Book"

b) Changes in income, employment, and prices

This vast increase in the productivity of the Canadian economy was not generated "in vacuo". The economy remained primarily a capitalistic one, so that other similar measures changed in the same direction - national income, employment, and prices. If employment and income are a measure of a country's prosperity, then Canada was immensely prosperous during the war. The increase in Employment was staggering - something like 60% (c.f. Table 21). And between 1939 and 1944 National Income doubled! One has to repeat that to catch its full import. The real gains for the population can be measured in National Income per Capita, which increased from $404 in 1939 to $767 (estimated) in 1944[1]. In 1933 it had been a paltry $256. Gains of that order, though

Table 21

NATIONAL INCOME, EMPLOYMENT, AND WHOLESALE PRICES 1939-1944

Year	National Income ($ million)	Employment (1926=100)	Wholesale Prices (1926=100)
1939	4570	113.9	75.4
1940	5391	124.2	82.9
1941	6426	152.3	90.0
1942	8044	173.7	95.0
1943	8724 (est.)	184.1	100.0
1944	9186 (est.)	183.0	102.5

Source: "Canada Year Book"

[1] Computed from "Canada Year Book"

generated by the unnatural impetus of war, demonstrate the potentialities of the Canadian economy. However, we must remember to insert a certain amount of caution when accepting these statistics as a measure of prosperity for the country. Certainly the increase in employment cannot be disputed as a desirable measure of improvement; but a national income which includes the payment for war materials that are not only destructive but satisfy no want in the economic welfare sense can be easily disputed. Though we justifiably introduce this caveat, the evidence of the gains from full employment, full production, and a raising of the common standard of living is inescapable.

There is another caution we must insert when accepting value figures for war years; and that caution is prices. If prices increase, value figures exaggerate the real situation. In the Canadian case that exaggeration seems to be almost insignificant when compared to the amount of increase in national income. As Table 21 shows, Wholesale Prices increased by some 54% from 1939 to 1944. During the same period the Cost of Living rose less than 20%[1]. Surely that is no indication of a wartime inflation; and bespeaks the efficiency of the Wartime Prices and Trade Board. But it does indicate that the value figures overstate the case of 1943 and 1944 over 1939 by probably 1/3. Other evidence indicates that it may be slightly more than 1/3. However, the story of wartime price control

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[1] "The Labour Gazette", January, 1946

in Canada is not the subject of this thesis. Suffice it is to say that prices did not move sufficiently to seriously vitiate value comparisons with prewar years.

c) Public debt

This happy miracle of production and national income was also accompanied by a not so happy increase in the public debt. As a matter of fact the growth of the public debt (c.f. Table 22) was much greater than even the growth of production and national income; and, what is more alarming, showed a tendency to continue at a great rate in 1945 when national income had ceased to expand and had in fact contracted.

Table 22

GROSS AND FUNDED PUBLIC DEBT, FISCAL YEARS 1939-1945

($ million)

March 31	Gross Debt	Unmatured Funded Debt
1939	3,711	3,386
1940	4,029	3,696
1941	5,019	4,372
1942	6,649	5,865
1943	9,228	7,893
1944	12,359	10,937
1945	15,712	13,984

Source: "Public Accounts of the Dominion of Canada"

Although the gross debt of the Dominion increased between 1939 and 1945 from $3,711 million to $15,712 million the load was almost entirely born by the Canadian people. In fact the government was able actually to reduce the amount of its funded indebtedness payable abroad. That shows to what extent the colossal financial needs of the war were met at home. This was an outstanding achievement, and more than anything else portrays the maturity of the economy. Of course the amount of funded debt held abroad may not be exactly equal to the amount payable abroad. But in the absence of any precise information concerning the former, we may presume that it most probably closely approximates the latter.

On March 31, 1939 of the Unmatured Funded Debt of $3,386 million $2,510 million was payable in Canada and $875 million (26%) was payable abroad (almost equally divided between New York and London). But on March 31, 1945 of the $13,984 million of Unmatured Funded Debt $13,639 million was payable in Canada and only $345 million (2%) abroad (almost wholly in New York)[1]. The proportion payable abroad had not only fallen to a ridiculously small percentage of the total but in absolute amount it had more than halved. This fact, coupled with a substantial fall in the rate of interest, was responsible for the considerable reduction in the amount of interest on the debt payable in foreign

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1"Public Accounts of the Dominion of Canada"

currencies. In the fiscal year ending March 31, 1939 $30.5 million was payable whereas in the fiscal year ending March 31, 1945 only $12.5 million was so payable.[1]

This is a most striking illustration of a new condition manifest in the Canadian economy which will have a profound effect on the balance of payments and consequently on merchandise trade. It reflects the turning point from a mature debtor to an incipient creditor country. This element has already started to show itself in total Interest and Dividend payments made to foreigners. In 1939 these amounted to $306 million; by 1944, showing a steady fall, they amounted to $264 million[2]. Taken in conjunction with the increase in interest and dividend payments made by foreigners to Canadians it meant that the usual, large debit balance on that item was reduced in the five years from $249 million to $193 million[2], to a point where it would now seem to be less than the average pre-1939 credit balances of merchandise trade. This reduction is, of course, not outstanding in amount, but it means a great deal for the future.

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[1] "Public Accounts of the Dominion of Canada"
[2] "Canadian Balance of International Payments, 1926-1944"

Chapter Seven

WARTIME MERCHANDISE TRADE

a) Growth of trade

This amazing growth of the Canadian economy was an answer to the demand for Canadian products outside Canada for the prosecution of the war. It was actually foreign trade that cracked the whip over the straining economy. Mighty successful was its urging. Merchandise trade, excluding gold (c.f. Appendix III), leapt from $1,526 million in 1938 to an all time high of $5,242 million in 1944. Compare the latter figure with the average annual total of Merchandise trade (excluding gold) of the United States from 1936 to 1940, when American trade had well recovered from the World Depression. That average was U.S.$5,702 million.

Wartime trade is presented in Table 23. In the six years 1938-1944 it increased almost 3½ times! The increase in Imports was phenomenal (over $1 billion), but the increase in Exports was even more so (over $2½ billion). This left an active balance of merchandise trade of amazing proportions, to which problem we shall turn in the next chapter. In 1944 Canada exported alone

Table 23

MERCHANDISE TRADE, EXCLUDING GOLD, 1938-1945

($ million)

Year	Imports	Exports	Total Trade
1938	677	849	1526
1939	751	936	1687
1940	1082	1193	2275
1941	1449	1640	3089
1942	1644	2358	4030
1943	1735	3001	4736
1944	1759	3483	5242
1945	1586	3267	4853

Sources: 1938-1944 - "Trade of Canada, 1944"; 1945 - "Commercial Intelligence Journal", February 9, 1946.

$3,483 million worth of goods. In 1933 total Net Value of Production had been only $1,949 million; and even in 1929 it had reached just $3,658 million[1].

It will be recalled from Table 2 on page 10 that during the interwar period the average Merchandise Exports % of Net Value of Production was 35.1. In 1943 it stood at 49.7![2] It will also be recalled from the

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[1] "Canada Year Book"

[2] Merchandise exports during the interwar period included exports (physical movements only) of non-monetary gold. For that reason net (not total) exports of non-monetary gold (including earmarked gold) have been added to Merchandise Exports, Excluding Gold in 1943 and 1944 to gain a fairer comparison. The difference between exports (physical movements only) of non-monetary gold and net exports of non-monetary gold (including earmarked gold) does vitiate, however, any nice comparison of interwar and wartime figures.

same table that during the interwar period the average percentage of National Income accounted for directly by Exports was 25.1%. In 1943 it had risen to 36%, and in 1944 to 39.1%![1] Evidently the abnormal conditions of wartime trade do not invalidate the idea of the importance of foreign trade to the Canadian economy. In fact they strengthen considerably our early contention that the more prosperous is the economy the heavier will it be found that merchandise exports weigh in that economy.

Lest it be thought that this enormous growth of foreign trade was merely an artificial one of money values indexes for the Volume of Imports and Domestic Exports are given in Table 24. We know that during wartime prices, even in the best controlled economies, increase somewhat (c.f. Table 21, p.88). So that we should take this fact into consideration when studying changes measured in value terms.

Because the comparison of import and export prices is much more clear in graphical form we plot the price indexes given in Table 24 on Chart XI. It would appear that, although for the first part of the war (certainly in 1940 and 1941) Import Prices rose more quickly and to a greater extent than Export Prices, giving Canada slightly the worse of the barter terms of trade, by 1944 the prices Canada was paying for imports were certainly lower than the ones she was receiving for

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[1]See footnote 2 on page 94

Table 24

VALUE AND VOLUME OF MERCHANDISE TRADE,
EXCLUDING GOLD, 1938-1944
(1935-39=100)

	Imports			Domestic Exports		
Year	Value	Price	Volume	Value	Price	Volume
1938	99.0	98.3	100.7	94.7	102.2	92.7
1939	109.7	101.6	108.0	104.6	97.0	107.8
1940	158.1	109.9	143.8	133.3	109.1	122.2
1941	211.6	130.8	161.8	183.3	115.5	158.7
1942	240.2	151.8	158.2	267.2	134.3	198.9
1943	253.5	156.7	161.8	355.9	147.5	227.7
1944	256.9	149.6	171.7	388.9	156.8	248.0

Source: "Trade of Canada, 1944"

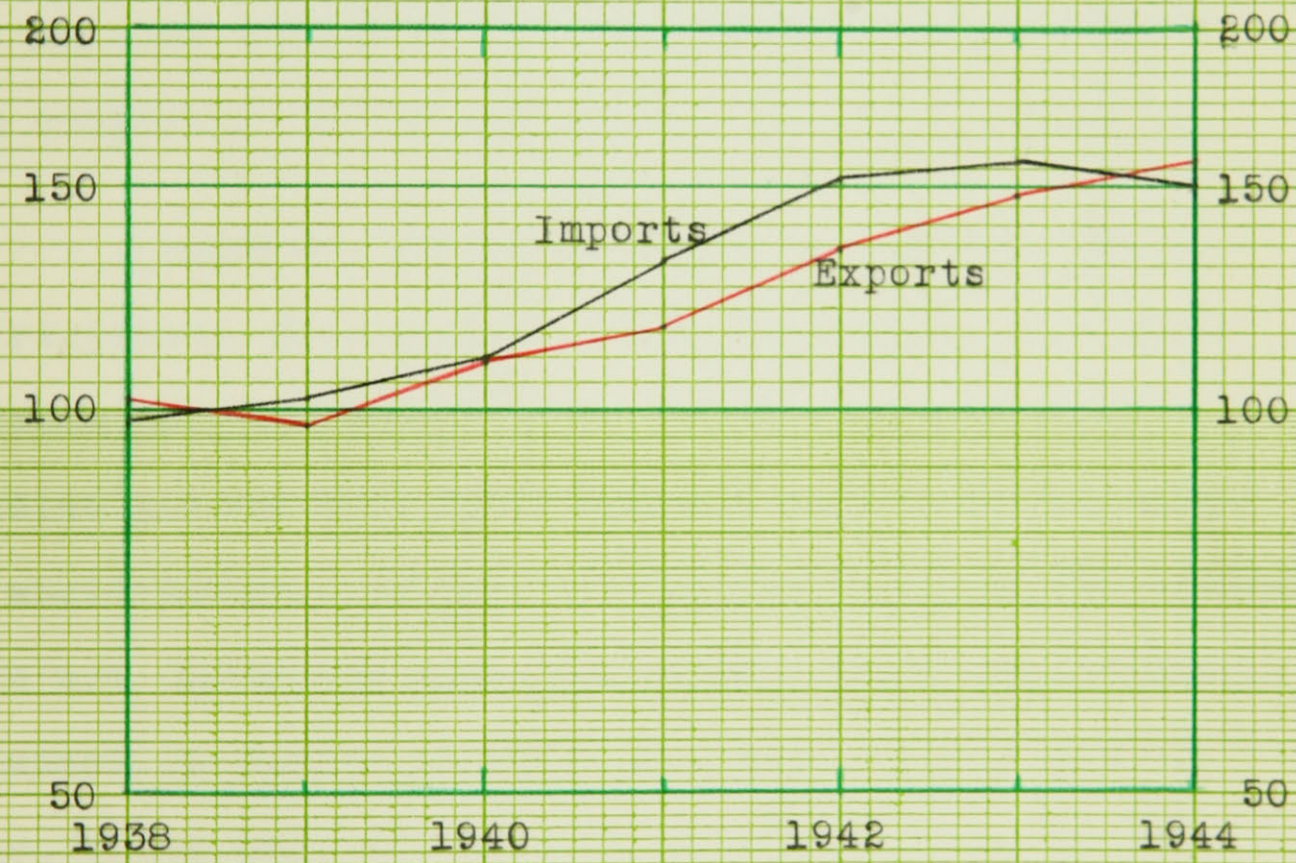
exports, which very probably gave her some advantage in the barter terms. However, beyond the fact that the abnormal nature of wartime trade makes any such comparison rather artificial, we must be careful of interpreting that comparison too closely.

To exactly what extent import and export prices changed is difficult to determine. In the first place, the difficulty we mentioned when considering the barter terms of trade in Chapter 4 of weighting in import and export price indexes is magnified manifold in wartime. In preparing the price indexes we have used in Table 24 and Chart XI the Dominion Bureau of Statistics has

Chart XI

INDEXES OF IMPORT AND EXPORT PRICES 1938-1944

(1935-39=100)



Source: "Trade of Canada, 1944"

weighted values with the average quantities imported and exported 1935-1939. But the make-up of trade obviously underwent radical changes during the war. Furthermore, the prices of most war materials were plainly artificial; they were set at a non-competitive cost. In the second place, the Commodity Prices Stabilization Corporation spent considerable sums of money subsidizing imports, particularly consumer goods, in order to keep such prices in line with controlled domestic prices[1]. So that we must accept with some caution any inference from comparing import and export prices in Chart XI.

However, as the eventually greater rise of export prices over import prices indicates, and other evidence corroborates, there is little doubt that Canadian prices from 1943 onwards were somewhat below the world level. If this condition continues to obtain there are certainly some advantages which will accrue to Canada in export markets and the barter terms of trade, which may, of course, be overbalanced by the cost of price control.

But to return to our inquiry into the comparison of value and volume of trade, these price indexes are useful in watering down inflated value figures, though we can scarcely call the price changes indicated inflation.

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[1]Import subsidies paid by this corporation from December 1, 1941 to December 31, 1944 amounted to $138.7 million ("Wartime Prices and Trade Board, Report to Parliament, January 1, 1945 to December 31, 1945").

If we apply these indexes we find that the Volume of Imports rose from 100.7 in 1938 to 171.7 in 1944, and that of Exports from 92.7 to 248.0. That is not as great a rise as the Value indexes showed. But, despite an admittedly considerable rise in prices, it dismisses any contention that the wartime growth of trade was an inflationary myth. In Volume as well as Value the growth was phenomenal.

As one would expect this growth was wholly accounted for by war material. In 1944 the Dominion Bureau of Statistics divided Domestic Exports of $3,440 million into War Exports of $1,555 million and Non-war Exports of $1,855 million[1]. In 1945 Domestic Exports of $3,218 million were similarly divided into War Exports of $1,161 million and Non-war Exports of $2,057 million[1]. (The change from guns back to butter was obvious as early as 1945.) However, the Bureau does not provide similar figures for previous years. And undoubtedly this division classifies only direct war materials such as ammunition, military vehicles, armaments, etc. as War Exports. If most of the food products and non-ferrous metals, and much of the forest products, were considered as War Exports - as they undoubtedly were in only a slightly more indirect way than tanks and guns - the proportion of War Exports could be considered to have been much higher. As a matter of fact the Bureau does estimate that 75-80% of wartime

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[1] "Canadian Intelligence Journal", February 2, 1946

exports belonged to an abnormal war category, and that only 20%, or approximately $600 million, could be considered as normal trade[1].

Normal or abnormal trade, the nature of that trade during the war is most important for the future. It will not only tell us what effect the war had on Canadian foreign trade directly but what effect wartime foreign trade had on the Canadian economy. It is our task in the following two sections of this chapter to analyse that trade.

b) Nature of wartime import trade

In studying the nature of merchandise imports and exports during the war we shall follow the identical plan we used in studying merchandise imports and exports during the interwar period. The reader can at any time compare more closely than our analysis attempts the two positions by referring to the relevant table in Chapter 3.

The changes in the proportionate composition of imports by classes of merchandise can be noted in Table 23. It should be emphasized that this table shows the classes by their percentage share in the total. In all cases the absolute value of each class increased during the war, though their share in the total changed. The urgent need for war materials is partly represented in this table,

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1 "Canada Year Book"

Table 25

IMPORTS* BY CLASSES OF MERCHANDISE

1939, 1941, 1942, AND 1944

(% by each class)

	1939	1941	1942	1944
Agr. & veg. products	17.0	11.9	9.0	12.0
Animals & products	4.4	2.4	2.2	2.0
Fibres & textiles	13.4	11.1	11.5	10.9
Wood & paper	4.5	2.5	2.4	2.5
Iron & its products	24.4	29.9	22.8	24.4
Non-ferrous metals & products	5.6	6.5	5.1	6.0
Non-metallic minerals & products	17.6	13.1	13.5	15.4
Chemicals & allied products	5.8	4.5	4.1	4.6
Miscellaneous	7.3	18.1	29.4	22.2

* Excluding gold

Source: Computed from "Canada Year Book"

and more fully in Table 26 on page 104. For the first two years of war these were of a kind to build the Canadian war production machine and to supply Canadian forces while that machine was being built; and after that they were largely of a kind to feed into that machine.

Agricultural and vegetable products and Animal products imports, partly because of the inaccessibility of supply and partly because of the necessity of conserving foreign exchange for more necessary products, continued their interwar trend at an accelerated pace,

and dropped heavily. By 1944, though they had regained a small portion of lost ground in that year, they were considerably below their prewar position. Fibres, textiles, and textile products, lost a similar amount of ground, a great deal of which was taken up by domestic production of finished textiles.

The table shows the extent to which Iron and its products, in answer to the demands of armaments production, increased in the first two years of war over their interwar share. In 1941, by far the most important category, they accounted for 29.9% of total merchandise imports. However, in 1942 increased Canadian production plus heavier imports of products in the Miscellaneous class began to make itself felt, and this class dropped back to its usual place - still the most important class of import - where it accounted for almost ¼ of total merchandise imports.

Non-metallic minerals and their products exhibited little change during the period, although they were slightly lower than their interwar position, as were the other minor classes. Obviously then, the great change must have come in Miscellaneous commodities, which did in fact increase from 7.3% in 1939 to a high of 29.4% in 1942 to recede slightly to 22.9% in 1944. This sudden growth was due to the fact that the vast amount of ordinance, military stores, and airframes come under this heading. Preliminary figures for 1945 indicate that this class will

drop quickly in postwar years. In that year it had already declined to 14.4%

Our study of the composition of merchandise imports is completed in Table 26, which presents the ten leading commodity imports in 1939, 1941, 1942, and 1944. These ten accounted for 33-40% of total merchandise imports during the war years, indicating little change over the interwar period in the concentration of imports. Surprisingly enough even the exigencies of war neither greatly reshuffled the leading commodities Canada imported nor changed the weight they held in import trade. Throughout the six years 1939-1944 five commodities - Coal, Automobile parts, Machinery except farm, Crude petroleum, and Rolling-mill products - remained in the leading ten, and two others - Fruit, and Cotton goods - missed the charmed circle only once. The evidence still points to the fact that there are certain commodities that the Canadian economy either must or has grown accustomed to import, and, come hell or high water, seems likely to do so for some time.

Despite this exhibition of stability in the character of import trade the table shows some changes, all obviously due to the war, that will have important consequences. After the war plants had been built, imports of Machinery except farm dropped considerably. Whether industrial reconversion and expansion can use

Table 26

TEN LEADING COMMODITY IMPORTS 1939, 1941, 1942, AND 1944

($ million)

1939		1941	
Machinery exc farm	42.8	Machinery exc farm	130.4
Coal	41.6	Automobile parts	71.5
Petroleum crude	39.7	Coal	61.6
Rolling-mill products	32.3	Rolling-mill products	60.7
Automobile parts	25.3	Petroleum crude	56.5
Fruits	24.0	Rubber products	39.1
Sugar & products	23.4	Cotton goods	34.0
Farm implements	20.9	Engines & boilers	32.7
Cotton goods	17.2	Cotton raw	31.8
Cotton raw	16.4	Farm implements	31.0
Total Imports*	751.1	Total Imports*	1448.8

1942		1944	
Coal	81.9	Coal	113.1
Rolling-mill products	81.1	Automobile parts	80.3
Automobile parts	76.4	Machinery exc farm	78.6
Machinery exc farm	71.6	Petroleum crude	72.0
Petroleum crude	57.5	Aircraft excl engines	65.1
Cotton goods	48.4	Engines & boilers	63.2
Cotton raw	40.4	Fruits	61.9
Fruits	31.8	Electrical apparatus	57.9
Electrical apparatus	28.2	Rolling-mill products	51.4
Wool raw	24.5	Cotton goods	50.7
Total Imports*	1644.2	Total Imports*	1758.9

* Excluding gold

Sources: "Canada Year Book" and "Trade of Canada, 1944"

existing machinery or will require new equipment, and, if the latter, whether it can be supplied competitively by a new Canadian heavy industry is a problem that we can pose only. It certainly seems most probable that machinery imports will decline in relative if not in absolute importance. The war was also responsible for the decline

of imports of Rubber and its products in 1942 and Rolling-mill products in 1943. On the face of it the development of the production and processing of synthetic rubber in Canada has been eminently successful. If the government-released information is correct postwar importation of natural rubber and its products will be cut to a fraction of pre-1939 imports. The wartime extensions to Canadian rolling-mills will have a similar effect. These mills can now provide steel in most of the standard qualities and shapes that were imported in large quantities before the war. These two are only the more obvious cases of the probable replacement of imports by domestic production that are brought out by Tables 25 and 26. There are many others, particularly in the textile industry.

The war has, on the other hand, seen the increasing importance of the importation of certain other items - Automobile parts, Airframes, Engines and boilers, and Electrical apparatus. Any drop in the first will depend greatly on the international division of the Great Lakes automobile industry, which in turn will depend on tariff policy. At any rate, for some years at least, till the large backlog of demand for automotive vehicles is satisfied this item will most likely retain the important position it gained during the war. Airframes face somewhat the same situation; although undoubtedly this item will remain as a leading Canadian import from the United States. The size and diversity of the American

market will no doubt give the American aircraft manufacturer certain advantages in many lines in the Canadian market against which the new and sizable Canadian industry will be unable to compete unless protected by a tariff. Engines and boilers and Electrical apparatus will certainly decline, but may remain above their prewar levels if industrial activity continues high.

We now turn in Table 27 to the leading sources of merchandise imports. The emergence of the United States as almost the sole source of supply stands out. In 1944 Canada actually imported $1,447.2 million of merchandise from the United States. To put it mildly, that is being a pretty good customer. This has been a purely wartime phenomenon. Although the Canadian economy expanded tremendously in breadth, industrial expansion particularly depended heavily on imports of American industrial materials and machinery. Furthermore, there still remained certain products which the Dominion could not economically manufacture, at least completely (e.g. aircraft); these she imported in large quantities either for domestic consumption or for further manufacture and re-export.

This exceptional dependence on the United States meant that the leading six countries accounted for a larger share than ever of Canadian merchandise imports. By 1942 their share had risen to over 93%, to quite reverse any slight interwar trend of a slow broadening of the Canadian

Table 27

SIX LEADING SOURCES OF MERCHANDISE IMPORTS

1939, 1941, 1942, AND 1944

($ million)

1939		1941	
United States	496.9	United States	1004.5
United Kingdom	114.0	United Kingdom	219.4
Straits Settlements	13.1	Straits Settlements	38.7
Australia	11.3	Brazil	19.4
British India	9.8	Australia	19.2
Germany	8.9	British India	17.9
Total Imports*	751.1	Total Imports*	1448.8

1942		1944	
United States	1304.7	United States	1447.2
United Kingdom	161.1	United Kingdom	110.6
British India	21.3	British India	27.9
New Zealand	19.9	Colombia	13.8
Straits Settlements	14.7	Venezuela	13.8
Australia	12.9	Mexico	13.1
Total Imports*	1644.2	Total Imports*	1758.9

* Excluding gold

Sources: "Trade of Canada, 1942" and "Trade of Canada, 1944"

trade relationships. Despite these figures a closer examination of the table will reveal the seeds of some such broadening. During the war many of Canada's usual sources of supply were completely or partially cut off through transportation difficulties or an inability to supply the Canadian market. Consequently the country was forced to find alternative sources in the American continents. We noted the vast increase in imports from the United States. Just as significant is the more than

proportionate increase in imports from other American countries, notably Colombia, Venezuela, Mexico, Brazil, and Jamaica. This opening up of trade relationships presents Canada with the opportunity to maintain a higher level of trade with these countries, while regaining her other relationships which were cut off during the war.

Concurrent with the heavy swing to the United States there was a similar heavy swing from the United Kingdom. Although Britain undoubtedly attempted to maintain merchandise exports at as high a level as war conditions would permit, the conditions obtaining in this respect were most stringent, leaving British export trade in a crippled condition. This swing of Canadian import trade during the war to the United States from the United Kingdom, from other foreign countries, and also to some degree from the British Empire other than the United Kingdom is illustrated in Table 28. This table is carried back through representative years to 1933 in order to present a fair basis for the extent of changes since 1939 and to help complete the picture presented in Tables 10 (p.48) and 15 (p.59).

It is impossible to overestimate the importance of the fact that in 1944 82.3% of total merchandise imports came from the United States. The problem it poses is of no mean proportions and one of the major ones we shall discuss in the next chapter.

Table 28

MERCHANDISE IMPORTS* FROM BRITISH EMPIRE AND FOREIGN COUNTRIES, REPRESENTATIVE YEARS 1933-1944

(% from each source)

	British Empire		Foreign Countries	
Year	United Kingdom	Other Empire	United States	Other Foreign
1933	24.4	8.6	54.2	12.8
1936	19.4	10.4	58.1	12.1
1938	17.6	9.9	62.7	9.8
1939	15.2	9.9	66.2	8.7
1941	15.2	9.7	69.3	5.8
1942	9.8	6.9	79.7	4.0
1944	6.3	6.2	82.3	5.2

* Excluding gold

Source: "Trade of Canada, 1944"

c) Nature of wartime export trade

We follow the familiar pattern in analysing merchandise exports, noting first of all the changes in classes of merchandise in Table 29. In comparing the figures of this table with those of the interwar situation revealed in Table 11 (p.49) it should be remembered that the former exclude gold, by far the most important item in the Non-ferrous metals class, with a consequent increase in the other classes, most noticeable in Agricultural and vegetable products and Wood, wood products, and paper.

Table 29

DOMESTIC EXPORTS* BY CLASSES OF MERCHANDISE

1931, 1941, 1942, AND 1944

(% by each class)

Class	1939	1941	1942	1944
Agr. & veg. products	23.8	17.6	10.9	21.6
Animals & products	14.2	12.5	10.8	10.8
Fibres & textiles	1.6	1.9	1.2	1.7
Wood & paper	26.4	23.8	16.5	12.8
Iron & its products	6.8	14.7	19.7	22.5
Non-ferrous metals & products	19.6	15.2	13.0	9.9
Non-metallic minerals & products	3.2	2.8	2.4	1.7
Chemicals & allied products	2.6	3.6	3.3	2.9
Miscellaneous	1.8	7.9	22.2	16.1

* Excluding gold

Sources: Computed from "Trade of Canada, 1942" and "Trade of Canada, 1944"

It is interesting to note the unexpected, relative decline in the Agricultural and vegetable products class during the first half of the war. Although exports in this class amounted to $257.8 million in 1942, some $35 million greater than their amount in 1939, they had nevertheless dropped to a mere 10.9% of total Domestic Exports. However, in the two years to 1944 they trebled in value, thereby regaining their weighty position, second to Iron and its products. Animal products, though increasing tremendously in $ value, continued their interwar trend of slightly

decreasing relative importance. Wood, wood products, and paper dropped perforce from their leading position in 1939 to a bad fourth in 1944, accounting for only 12.8% of the total. At that, this class almost doubled in value in the five years.

The relative decreases in the above three classes are partly accounted for by the increase in Iron and its products from 6.8% in 1939 to 22.5% and the major position in 1944. If the three above-mentioned classes registered such a relative decline despite a doubling and trebling of value exported, the increase in the value of Iron and its products can be imagined. In 1939 it stood at £63.1 million, in 1944 at £772.9 million! That was the answer to "Give us the tools".

Non-ferrous metals and their products suffered a fate almost similar to the Wood group despite the vast increase in the production of these metals during the war (c.f. Table 20, p.86). Miscellaneous products, including such items as airframes, military stores, and ammunition expanded tremendously, reaching a high of 22.2% as early as 1942. By 1944, however, this class had started to shrink; and preliminary figures for 1945[1] indicate it accounted in that year for only 11.7% of total Domestic Exports.

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[1] "Commercial Intelligence Journal", February 2, 1946

We proceed to clarify the composition of export trade in Table 30, which lists the ten leading domestic exports in each of the four years. Despite the sudden and preponderant emergence of war material items such as Guns, rifles, and firearms, Military vehicles, and Ammunition which were exported in hundreds of millions of dollars,

Table 30

TEN LEADING COMMODITY EXPORTS 1939, 1941, 1942, AND 1944

($ million)

1939		1941	
Newsprint	115.7	Wheat	161.9
Wheat	109.1	Newsprint	154.4
Nickel	57.9	Automobiles	128.8
Planks and boards	48.8	Wood-pulp	85.9
Copper in forms	40.2	Meats	84.2
Meats	37.4	Aluminum	75.8
Wood-pulp	31.0	Planks and boards	74.2
Fish	28.0	Nickel	67.7
Aluminum	25.7	Wheat flour	44.8
Automobiles	22.6	Ammunition	41.9
Total Dom. Exports*	924.9	Total Dom. Exports*	1621.0

1942		1944	
Ammunition	300.4	Wheat	384.1
Automobiles	194.3	Ammunition	313.9
Newsprint	141.1	Automobiles	246.2
Wheat	121.8	Guns rifles & firearms	239.6
Aluminum	112.2	Meats	192.0
Meats	110.4	Newsprint	157.0
Ships and vessels	106.8	Automobile parts	139.3
Wood-pulp	95.3	Airframes	107.1
Planks and boards	80.1	Aluminum	105.3
Guns rifles & firearms	73.7	Wood-pulp	101.6
Total Dom. Exports*	2363.8	Total Dom. Exports*	3440.0

* Excluding gold

Sources: "Canada Year Book" and "Trade of Canada, 1944"

the Ten Leading Domestic Exports never accounted for more than 58% of the total. It is significant that the interwar trend of a slow broadening of Canadian export trade was not reversed to any extent. Rather it marked time. The Canadian productive economy increased in breadth as well as in depth. It produced for export in considerable quantity a sufficient number of other goods to balance the enormous quantities of the few major war items.

Surprisingly enough the composition of the top ten did not change a great deal during the war. Throughout the six years 1939-1944 Wheat, Newsprint, Meats, Wood-pulp, Automobiles, and Aluminum were all included - six of them. And these were all leading exports before the war. The first four were regularly in the leading ten throughout the interwar period, and the last two climbed to a leading position a few years previous to the outbreak of war. Planks and boards, Nickel, Ammunition, and Guns, rifles, and firearms were also leading wartime exports. The first two maintained their important prewar position until 1942; and even then, replaced by finished war armaments, they hovered on the heels of the leading ten.

Clearly, the vast increase in exports during the war depended on the already established nature of the Canadian productive economy. Canadian farms,

forests, and mines provide her with an advantage in international trade in certain proven directions. If her markets are not curtailed by trade restrictions there is no reason why she should not maintain exports along these established lines at high levels. Where the war has expanded those industries in which her comparative advantage is great they would seem to have the opportunity to survive, if not at expanded levels, at least above interwar levels.

The Aluminum industry in particular, together with other non-ferrous metals industries, would seem to face a bright future in the export market. The Automobile industry is rather more questionable. Very probably it could now compete more closely with its American counterpart, but it is difficult to see how it could maintain even its prewar level of exports without some measure of protection. A solution of the kind recommended by "The Midcontinent and the Peace"[1] is worth serious consideration. This study recommends a reduction of the Canadian tariff on automobiles with a rationalization of the Great Lakes automobile industry by which Canadian manufacturers would specialize in the production of certain parts only. Such a scheme would mean that Canada would export automobile parts and import finished automobiles. The inference is that Canadians would be able to buy

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[1] A report prepared under the auspices of the University of Manitoba and the University of Minnesota under the direction of W. J. Waines and A. R. Upgren.

cheaper, and hence more, automobiles; and that, insofar as the Great Lakes automobile would be a better buy on the world market due to a more efficient rationalization of the industry on an international scale, Canadian exports of automobile parts would be greater than Canadian exports of completed automobiles under the present tariff set-up. However, we must admit the likelihood of such a scheme ever being put into force is extremely slim.

So much for the products Canada exported during the war. Just as these were produced in answer to the demands of war, Table 31 shows that they went to those areas most closely connected with the prosecution of war, a comparatively small circle. Consequently it is not surprising that the leading six markets took some 90% of Canadian domestic exports annually during the war, which actually was a degree of concentration very little larger than that of the interwar period.

The United States generally managed to maintain its position as Canada's best market, receiving a host of raw and partly manufactured materials to fashion into weapons of war, with the United Kingdom a close second. The conflict in the Mediterranean, starting with the Desert campaign in the summer of 1941, was responsible for the emergence of Egypt and later of Italy as important markets. The building of bases in Newfoundland in the winter and spring of 1942 was largely responsible

Table 31

SIX LEADING MARKETS FOR DOMESTIC EXPORTS

1939, 1941, 1942, AND 1944

($ million)

1939		1941	
United States	389.8	United Kingdom	661.2
United Kingdom	328.9	United States	609.7
Australia	32.1	Egypt	79.4
Japan	28.2	British India	38.3
British South Africa	18.0	Australia	37.6
New Zealand	11.0	British South Africa	36.4
Total Dom. Exports*	924.9	Total Dom. Exports*	1621.0

1942		1944	
United States	896.6	United States	1334.6
United Kingdom	747.9	United Kingdom	1238.1
Egypt	213.3	British India	175.1
British India	168.2	Italy	160.3
Australia	79.2	Egypt	108.4
Newfoundland	52.5	Russia	103.4
Total Dom. Exports*	2363.8	Total Dom. Exports*	3440.0

* Excluding gold

Sources: "Canada Year Book" and "Trade of Canada, 1944"

for the large increase in exports to that barren island. The allied organization for the waging of war in the East was as responsible for the rise of British India as a major market as it was for the comparative drop of Australia. Mutual Aid to Russia, commencing to flow in large quantities in the summer of 1943, made that country an important receiver of Canadian goods.

We conclude our study of export markets with Table 32, which shows the proportion of exports going to

British Empire and foreign countries. This table is a companion one to Table 28 on page 109, and completes the picture presented in Tables 14 (p.54) and 15 (p.59). It should be emphasized that this table does not include gold, which decreases the American share somewhat in latter years as a comparison with Tables 14 and 15 shows. As in Table 28 the table is carried back through representative years to 1933 in order to give a fair basis for comparison.

Table 32

DOMESTIC EXPORTS* GOING TO BRITISH EMPIRE AND FOREIGN COUNTRIES, REPRESENTATIVE YEARS 1933-1944

(% to each market)

	British Empire		Foreign Countries	
Year	United Kingdom	Other Empire	United States	Other Foreign
1933	39.8	8.4	31.8	20.0
1936	42.2	9.0	35.6	13.2
1938	40.6	12.3	32.3	14.8
1939	35.5	11.1	41.1	12.3
1941	40.6	13.6	37.0	8.8
1942	31.4	17.4	37.5	13.7
1944	35.9	11.2	37.8	15.1

* Excluding gold

Source: Computed from "Trade of Canada, 1944"

Since the outbreak of war neither the United Kingdom nor the rest of the British Empire changed its share to

any considerable extent; though the former market did drop fairly steeply in 1942 largely due to heavy exports to British India, Australia, and Newfoundland, which increased the share of the rest of the British Empire, and to Egypt, Iraq, and Russia, which increased the share of foreign countries other than the United States. But 1943 and 1944 witnessed a return to the almost identical situation of 1939.

The United States lost a small portion of its share during the war, which other foreign countries absorbed. Nevertheless, on the whole there were no startling developments, outside of the cessation of trading with enemy countries, in the broad outline of export markets.

Chapter Eight

WARTIME CHANGES IN CANADIAN INTERNATIONAL INDEBTEDNESS

a) Increase in active balance of merchandise trade

As we have emphasized in Chapters 2 and 5 changes in the extent of merchandise trade to the degree of those described in the last chapter could be expected to have had a marked effect on the balance of payments. If the Canadian balance of payments did undergo changes during the war as great as those experienced by Canadian merchandise trade the Canadian international debtor-creditor position at the end of the war must have been considerably different from the position at the beginning of the war described in Chapter 5. Remember any new international debtor-creditor position will react with considerable force on postwar trade. Consequently, before attempting any forecast of or recommendations for the future, we shall complete our description and analysis of wartime changes in foreign trade by a short analysis of the change in the Canadian position on international account.

At the beginning of the last chapter we drew attention to the tremendous increases in the active balances

of merchandise trade during the war. For convenience we list those active balances in Table 33. They represent a considerable alteration of the picture presented in Chapter 4, section e). The average Merchandise trade balance (excluding gold) for the interwar period was an active one of $134 million[1]. The active balance in 1936 of $315 million, and the passive balance in 1930 of $125 million were both near the extremes. Within those limits of merchandise trade balances the Canadian balance of payments managed to maintain a comparatively sound equilibrium.

Table 33

ACTIVE BALANCES OF MERCHANDISE TRADE* 1938-1945

($ million)

Year	Balance	Year	Balance
1938	171	1942	741
1939	185	1943	1266
1940	111	1944	1724
1941	192	1945	1682

* Excluding gold

Sources: 1938-1944 - "Trade of Canada, 1944"; 1945 - "Commercial Intelligence Journal", February 9, 1946.

Once the bottom of the World Depression had been passed the balance of payments, with an annual adjusted credit balance of merchandise trade approximating $200 million and an annual credit balance of gold of $100-200 million,

[1] Computed from "Trade of Canada, 1939"

jogged along with surprising stability. But the problem of keeping that balance in equilibrium when the credit balance of merchandise trade ran over $1,500 million was not nearly so easy of solution.

b) Problem of bilateral balancing

The solution was made vastly more difficult by the necessity of an almost complete bilateral clearing of accounts. Although Canadian industrial expansion created a heavy demand for American produced commodities, particularly producers' goods, the wartime conditions of currency inconvertibility did not allow the country to use the proceeds of the tremendous increase in sales of food, munitions, and raw materials to sterling area countries to pay for these American imports. We neither intend to analyse the successful solution by the financial authorities of the financing of Canadian international transactions despite the disintegration of the Canadian-British-American triangle, nor do we intend to discuss the incidence of foreign exchange control. The quantity of trade maintained with the minimum of dislocation bespeaks the efficiency of their solution. But we do intend to mention the directions that solution took in order to impress ourselves with some of the difficulties postwar trade must face.

The thorough system of foreign exchange control initiated at the very beginning of the war presented the

authorities with the opportunity to control the amount and direction of every legal international transaction, an opportunity they did not muff. Despite this channelling and control of transactions involving foreign exchange there still remained a serious deficit of U.S.$ required to purchase essential imports. The obverse of this situation, due to the lack of free convertibility of the £, was the surplus of £ for which Can.$ had to be found in order to keep the balance of payments in equilibrium.

The chief weapon in combatting the scarcity of U.S.$ was a rigid rationing of those U.S.$ available. The strain in the early part of the war was mitigated by the artifice of the Hyde Park Agreements of April, 1941[1] and by large exports of gold. By 1944 the substantial supply of U.S.$ provided by American government expenditures on military projects in Canada, such as the Alcan highway and the Canol project, and by the heavy increase in private American investment in Canada (probably

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[1]In principle, the object of the Hyde Park Agreements was the full utilization of the productive facilities of the United States and Canada by joint productive organization. "It was agreed as a general principle that in mobilizing the resources of this continent each country should provide the other with the defense articles which it is best able to produce, and, above all, produce quickly, and that production programs should be coordinated to this end" (United States "Department of State Bulletin", April 26, 1941). In fact, it was hoped that American purchases of defense articles in Canada would assist Canada in meeting the heavy costs of Canadian purchases in the United States. Since most of these latter were component parts of equipment Canada was producing for the United Kingdom, it was further agreed that such components should be provided to Canada under Lend-Lease to Britain.

encouraged by the 10% premium on American funds) eased the situation considerably. In fact, temporary developments even gave Canada an adjusted credit balance on merchandise trade with the United States of $331 million in that year[1]. By the end of the war there seems to be little question that the Canadian balance with the United States was in a fairly easy, if controlled, position.

The £ problem was more difficult. In the early years of the war a balance was achieved by the repatriation of Canadian securities (some $621 million from Empire countries in the first three years of war[1]), by the purchase of gold and U.S.$ from the United Kingdom, and by the accumulation of £ balances. However, there was a limit to these devices, the first two being exhaustible, and the last a temporary expedient only.

The outstanding solution of the British shortage of Can.$ was the billion dollar gift in 1942. This was quite a revolutionary, if logical, step in the balance of payments. If the goods were to go out, the Can.$ would have to come in to pay for them. And if the United Kingdom could not supply the Can.$, Canada would have to do so. She did. It was a revolutionary step because it was not a loan, payment for which would eventually be received. It meant that, although Canada exported $1 billion of goods, she received nothing (outside of

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[1] "Canadian Balance of International Payments, 1944"

goodwill) in return. Although she had an export credit of $1 billion, she neither received goods or services to that amount as a debit nor did she reduce her foreign-held indebtedness by exporting a like amount of capital as a debit. It was the Canadian taxpayer who paid for the $1 billion of goods. This principle could not, of course, be used in peacetime trade. Nevertheless, the point is that the billion dollar gift balanced the balance of payments. Peace or war that has to balance. Canadian goods just cannot be exported if Can.$ are not received in payment.

In the latter years of the war Mutual Aid, the repurchase by Canada of the British equity in Canadian war plants, and heavy current expenditures by the Canadian government for Canadian military forces overseas helped ease the £-Can.$ situation.

c) Effect of capital account balances on international debtor-creditor position

We have mentioned the problems the authorities faced and, briefly, the way in which these problems were solved in order to keep the Canadian balance of payments in equilibrium simply because we feel we cannot overemphasize the fact that the balance of payments must balance. If we have to, or want to, increase a credit item (e.g. merchandise exports), we must decrease other credit items, and/or increase debit items. During the

second World War by far the heaviest item in Current account - merchandise trade - increased tremendously. Not only that, the credit balance on that item increased tremendously (c.f. Table 33, p.120); so much so that the net credit balance on total Current account grew almost tenfold. From 1934 to 1939 the average credit balance on Current account was some $140 million. In 1940 it was $149 million. In 1941 it was $491 million! In 1942 it was $1,101 million!! In 1943 it was $1,206 million!! And in 1944 it was $997 million![1]

These massive credits were almost entirely made up with the United Kingdom, and unhappily, except for a small credit of $17 million in 1944, not at all with the United States. Of the total net credit balance on Current account from 1940 to 1944 inclusive amounting to $3,944 million $2,448 million was balanced by the debits of the billion dollar gift and of Mutual Aid, leaving some $1,500 million that was balanced by more ordinary capital account debits[1]. Undoubtedly a fair portion of that $1,500 million was of an extraordinary character and did not, in the final analysis, represent an export of Canadian capital. Just the same a debit balance of that size could not help but have meant that, on the whole, Canada reduced her international indebtedness considerably.

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[1] "Canadian Balance of International Payments, 1944"

To date figures of the amount of foreign investment in Canada and Canadian investment abroad at the end of the war are not available. However, we do know the trend of those figures during the war. In respect to the United States, the general trend manifest from 1933 to 1939 of a movement of Canadian capital to that country was reversed. Although Canadian securities held in the United States continued to be retired in large numbers, Americans were inclined to buy outstanding Canadian securities in even larger numbers. At the same time Canadian purchases of American securities dropped considerably. In Canadian securities transactions with the United States the net balance of sales to over purchases from Americans increased from $57.4 million in 1939 to $109.1 million in 1942, to $222.1 million in 1945[1]. The evidence certainly points to the fact that, despite complete government control of money movements, Americans were extremely willing to invest their money in Canada (probably with the blessing of the Foreign Exchange Control Board - a blessing that may now be acquiring several exclamation marks!). By the end of the war the Canadian indebtedness to the United States had no doubt increased over the estimated $4,190 million in 1939 (Table 17, p.75).

In respect to the rest of the world, and particularly to the United Kingdom, the evidence points

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[1] "Sales and Purchases of Securities Between Canada and Other Countries, December, 1945"

to a considerable reduction of Canadian indebtedness. Not only did the heavy repatriation of Canadian securities continue at an accelerated pace, but there seems to have been some private outflow of Canadian funds to the United Kingdom. From the outbreak of war to December, 1945 repatriation of Canadian securities from the United Kingdom aggregated $990 million with the result that the value of British investments in Canada at the end of 1945 was approximately $1,500 million[1] (in 1939 it had amounted to $2,466 million - c.f. Table 17, p.75). During the same period private Canadian investments in Britain increased by some $100 million to approximately $150 million[1]. Not only was the British-held Canadian indebtedness reduced to probably its desirable minimum, but Canadians even invested significant amounts in the United Kingdom.

Although it is impossible to estimate the exact amount of change that took place during the war in the Canadian international debtor-creditor position, it seems that Canada increased somewhat her indebtedness to the United States and decreased considerably her indebtedness to the United Kingdom. On balance, particularly in view of the large debit balance other than Mutual Aid and the billion dollar gift on capital account, it would seem that the country reduced its foreign-held indebtedness to some extent.

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[1]Hon. J. L. Ilsley in "House of Commons Debates", Monday, May 6, 1946, p.1276.

Just as important as any actual reduction is the prospect of Canadian capital exports in the future revealed by capital movements during the war. Undoubtedly there is much more capital available for investment abroad than there has been heretofore; and the tendency for Canadians to invest outside the North American continent has strengthened. If this tendency continues it will help give a very desirable flexibility to the Canadian balance of payments and to the whole financial set-up in Canada. This added flexibility would be a great aid in softening the various rigidities in the Canadian economy and in Canadian foreign trade which we have discussed.

It takes no stretch of the imagination to consider Canada as a net exporter of capital during the postwar period. The realization of that potentiality will depend largely on the conditions obtaining. If international economic relations resume something of their interwar nature, patterned after free enterprise, with a certain freedom and stability in the international investment sphere, Canada will no doubt move well along the path of an international creditor. If, however, international investment retains its circumscribed character or is hobbled by even tighter national restrictions, Canada may not move so far along that path. At any rate there are two policies to which she is already committed which will insure her creeping along that path at the very least.

Those policies are her extensive foreign loan policy and her relatively large contribution (U.S.$325 million) to the International Bank for Reconstruction and Development. If both of these develope fully they will mean, as much as a similar amount of private investment abroad, a considerable export of Canadian capital.

Chapter Nine

POSTWAR FOREIGN TRADE

a) Under a restricted trading system

Our study of the last twenty-five years of Canadian foreign trade leads us naturally to look to the future, to attempt some indication of the probable nature of postwar Canadian foreign trade and certain desirable trade policies to pursue.

In common with international economic organization Canadian foreign trade faces two main possibilities in the postwar world. The path it pursues depends almost solely on the general shape the international economic framework assumes. This does not mean that Canada will have no hand in the shaping of that framework. There is little doubt that before this last war the effect Canada had on the world economy was infinitesimal in comparison with the effect the world economy had on Canada. The war has improved this unhappy state of affairs. A snowbound country of 11⅛ million people cannot hope to wield the influence comparable to that of any of the three great powers; but the wartime exhibited maturity of the Canadian

economy plus the emergence of Canada as one of the world's leading small powers (if not the leading one) makes the voice of the Canadian people in any decision of the shape of postwar world economic organization an important one. The Canadian vote for a world of controlled economies or free enterprise now means something. That is admitted; but once the world economy as a whole is committed to one policy or the other Canada does not possess the strength to swim for any length of time against the stream.

If the world economic order continues to operate according to the pattern of national economic sovereignty conceived during the World Depression and perfected during the second World War Canada too will run with the pack. If the aim of the postwar world is the glorification of the sovereign nation state, with all the well-known economic policies that go with it, then we surely know that, without the artificial impetus of war, the circle of world trade will become narrower and narrower. The evidence that has been compiled by the numberless analyses of various aspects of interwar economic conditions points to the inevitable strangulation of international trade if the various insidious policies of economic control that go with the unbridled sovereignty of the nation state remain in effect. And Canadian foreign trade can do no other than shrivel with the rest.

To exactly what extent below its optimum Canadian

foreign trade will drop depends largely on the extent to which restrictive policies hold sway. However, in the postwar world there will be certain tendencies in the Canadian economy fostered during the war that will mitigate the too heavy effect of any restrictive international policies on Canadian foreign trade. It is more than likely that Canada will not be as near the end of the trade pendulum as she was during the interwar period (c.f. p.33).

The main reason why Canada will not feel the swings of world conditions to the same extent as she has heretofore is the greater maturity of her economy. With her eggs now spread among more baskets she will not lose so many if one basket breaks. Because the country no longer leans so heavily on the export of a few staples, if prices of basic raw materials, particularly agricultural, collapse on the world market, then the Canadian terms of trade will not suffer to their accustomed extent. With increased industrialization has come increased economic strength to face the hardships of any lowering of the extent of international trade.

The foreign trade aspects of this maturity are seen more directly in the greater degree of self-sufficiency evident in the economy. The change, as we pointed out in Chapter 7, section b, has not been startling; but some progress has been made. On the one hand, much wartime

expansion may not be able to hold its own in a freely competitive world market, but it could, in the event of a trade war, fill many gaps, and help lighten the quandary in which the country would find itself. On the other hand, some wartime expansion faces a promising future. Iron ore, machine tools, steel, heavy machinery, plastics, electrical equipment, synthetic rubber, textiles, aircraft, shipbuilding, and optical glass are a few of the more striking examples. In these and many others Canada seems likely to be able to fill at home a much larger proportion of her domestic needs.

This increasing self-sufficiency will have important repercussions in Canadian-American trade. Heretofore the vast proportion of industrial equipment, in fact, much of the producers' goods used in Canadian industry, has come from the United States. In the future, despite an even heavier dependence during the war on the United States as a source of supply, Canada will not find the necessity of many American imports so pressing. There is no doubt, as recent American strikes have proven, that the Canadian economy cannot yet operate fully without large imports of American industrial equipment and materials; but should protectionist policies ever place Canada in a position similar to the one she faced in 1930 she could decrease her imports with much less damage to her standard of living.

On the other side of the merchandise trade bargain Canada has strengthened her position as a supplier of many basic materials, and has opened up new opportunities in others. Her wartime exports of agricultural and animal produce have again proven her advantage in that direction. Her position as a source of non-ferrous metals is also enviable. Aluminum almost certainly will join nickel as a leading export. Copper and zinc too bid to place Canada as a leading exporter of those metals. She has further strengthened her export possibilities in non-ferrous metals by commencing the new production of such metals as magnesium and chromite.

The general improvement in export trade is most clearly seen in the trend of exports to be more manufactured. This is shown in Chart XII. In 1944 64% of Domestic Exports was Fully Manufactured! As late as 1937 only 36% was Fully Manufactured (c.f. Chart VIII, p.66). In this direction, as in many others, the war matured the Canadian economy very quickly, though it should be remembered from Chart VIII on page 66 that this tendency of doing more of the processing of Canadian exports in Canada was manifest during the thirties. Despite the fact that Raw Materials dropped as low as 13% of the total in 1942, the big gain was actually made in decreasing the proportion of Partly Manufactured goods from 33% in 1938 (fiscal year) to 14% in 1944 (calendar year). The breakdown of wartime imports is also included in this chart for comparison with the interwar situation, and for

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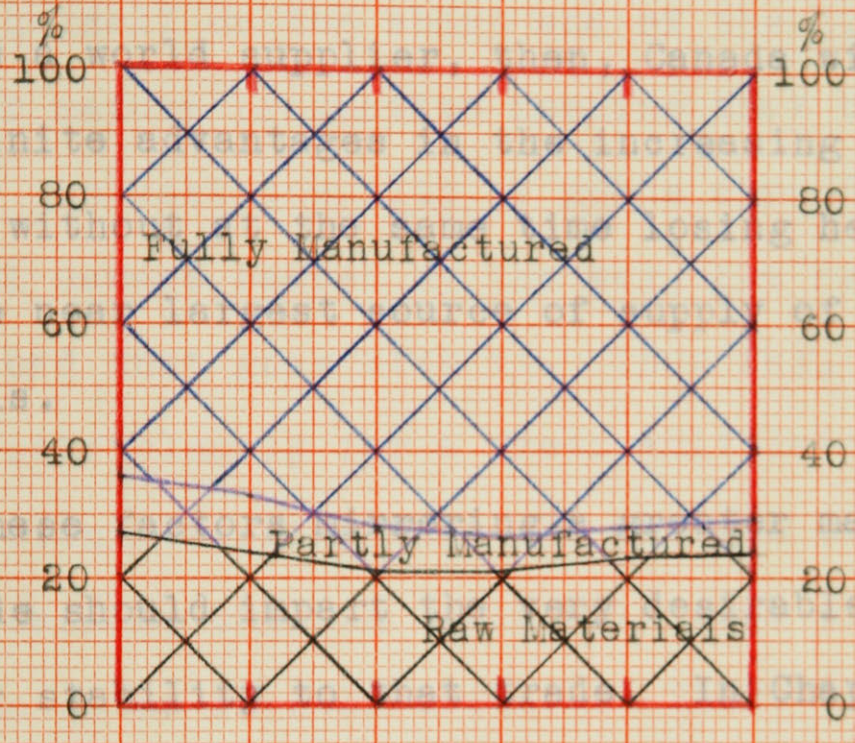
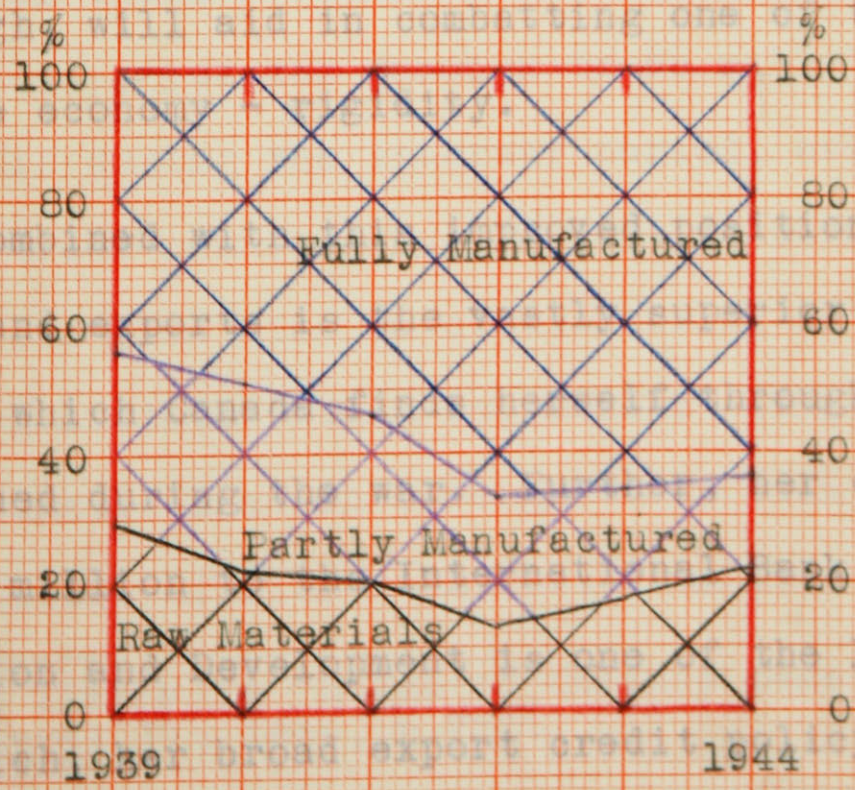
Chart XII

PROPORTIONS OF TRADE IN RAW AND MANUFACTURED PRODUCTS 1939-1944

Imports



Domestic Exports



Excluding gold

Source: Computed from "Trade of Canada, 1944"

comparison with wartime exports. There were no startling changes in Imports during the war; but a comparison of Imports and Domestic Exports reveals that at the end of the war the division between raw and manufactured products was almost the same in each case. Some 23% only of both Imports and Domestic Exports was Raw Materials.

As a world supplier, then, Canada will now possess definite advantages in the increasing diversity of her exports without at the same time losing her advantage of being the near largest source of supply of many basic raw materials.

These factors mirroring a greater maturity in foreign trade should impart the very desirable characteristic of a greater stability to that trade. In Chapter 4, section b) we drew attention to the hardships thrust on the Canadian economy by instability in the level of trade. Any improvement in that direction, particularly if the level of trade is high, will aid in combatting one of the greatest evils of the economy - rigidity.

Combined with this improved position in respect to imports and exports is the vastly superior bargaining position in which Canada finds herself through increased stature gained during the war. Further, her contribution of U.S.$325 million to the International Bank for Reconstruction and Development is one of the largest. Added to which, her broad export credit policy of the

Export Credits Insurance Corporation under which she has already committed herself to the extent of $644.5 million[1] will prove a very present help in combatting the early inception of any discriminatory trade policies. If the Dominion should be forced to negotiate bilateral clearing agreements there are very few directions in which she would find herself on the short end of the big stick. Added to her mature productive machine that can produce immediately the vast quantity of goods demanded to repair the physical damage caused by the war, she has the capital to loan abroad that goes with it. Thus far, she has pledged herself clearly for a freer multilateral trading world, not even demanding that the British Loan be spent wholely in Canada; but she could make such a condition if forced to do so in self-defence. There is no doubt that Canada will be able to support her professed postwar trade policy with a great deal of strength.

For these reasons it is extremely doubtful whether Canadian postwar foreign trade will drop to the depths it did during the interwar period, even under restricted trade conditions. In fact we would hazard a guess that for some time to come, barring nothing more serious than another "World Depression" (which was serious enough), Canadian foreign trade will not drop below the $1,500 million mark, or, roughly, the 1936

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[1]Hon. J. L. Ilsley in "House of Commons Debates", Thursday, April 11, 1946, p.787.

level of trade. And it is very probable that during the first two or three years of the transition period it will not drop very much below $3,500 million at roughly the present level of prices.

This section is not intended to be an argument for a Canadian protective trade policy. In our opinion Canada has much more to lose in retaliation than to gain by such a policy. Undoubtedly such a course would not present the degree of hardship it would have done in the interwar economy, but it is questionable whether increased industrialization has really altered to any great extent the basic Canadian position. Remember the developments which show the most promise are all in specialized lines. Furthermore, other countries too have stimulated and diversified their industrial capacities. We do intend to have shown, however, that restrictive trade policies will not damage Canadian foreign trade and the economy generally to the extent that they did during the interwar period.

b) Under a free trading system

The League of Nations study of "The Network of World Trade" comes to the conclusion that "the establishment of a workable system of multilateral trade - not necessarily in all detail on the pattern of the old system - appears, therefore, to be an important object for postwar reconstruction". The Canadian government

and most of the major powers have provisionally cast their votes for such a freer system of world trade. A significant start has already been made in the International Monetary Fund. But when the nations gather to form a world trade organization the result still hangs very much in the balance. In nations, as in individuals, there is a difference between liberty and licence. If the various nation states accept no curb, whether implicit or explicit, to their power of action, then a return to the conditions leading to the second World War is inevitable. More precisely, if a nation pursues an economic policy with a thorough disregard for the damage it may do another nation, then international economic relations will quickly assume the aspects of a conflict. Before open war eventually does arrive trade will have dried up to a trickle of paltry barter.

There is another factor which is bound to provide much (perhaps) unconscious opposition to a very free system of world trade. That factor is the demand for protection which may arise in the newly industrialized countries (the British Dominions) and in those which are in a position to embark on a policy of industrialization (mainly South America and possibly southeast Europe). New industry requires a certain amount of fostering; and it is a very difficult thing to decide, particularly when some of those industries have already been established under the duress of war, that they will not be worth the

cost of present protection. Now, industrialization may be pursued for either of two ends, but because it seems for the most part to be pursued for the second end the demand for protection generally receives strong support in newly industrial countries. The first end is one of improving real incomes. It involves increased specialization and the growth of international trade. The second end is one of stabilizing domestic employment and national income. It involves a less economic use of resources but wider diversification and a shrinkage of international trade. It is industrialization of the second kind that is the strongest proponent of protection.

In our opinion the price of the second course is too heavy a one for Canada to pay. In the first place, the policies required to insulate the economy from outside forces are much too drastic and complicated, and government spending much too heavy. And in the second place, even if we grant a complete program of industrialization possibly could stabilize employment and national income, as we have tried to emphasize throughout this thesis, it would do so at a rigorously low level. Given the Canadian climate, geography, and resources as they are, we just cannot replace by purely internal and domestic measures the stimulus given to national income and employment by foreign trade. Rather it is to the Canadian advantage to help revive world trade and to secure as large a portion thereof as possible by specializing in the

production of those goods in which the country has an advantage.

Specialization need not necessarily lead to wide fluctuations in income and employment. There is no reason whatever why international cooperation (of a different sort than the interwar variety) cannot impart comparative stability to a high level of international trade. At any rate centuries of economic history have proven that the wider and fuller has been the exchange of goods and services the wider and fuller has life become. Economic progress has improved man's standard of living, in tangibles as well as in intangibles. And economic progress has depended on specialization, a specialization that transgresses national boundaries.

It is not necessary to prove in this thesis the gains for all to be found in a world division of labour. Suffice it is to say that Canada, to a larger degree than most countries, depends on a freely functioning system of world trade. If that system is hobbled by the arbitrary and unpredictable control of governments implicit in such devices as clearing agreements, exchange control, import quotas, and so forth, then Canadian trade and the Canadian economy must suffer. Despite some improvement in the Canadian position Canada is still inexorably committed to a policy of free, multilateral trade. We cannot make this point too strongly. The country has increased its

productive capacity to an enormous extent, it has increased greatly the number of products it can produce, and those products it does produce are now predominantly in the fully manufactured form. But the products it produces, and is ever likely to produce to any great extent, are highly specific. Furthermore, until we reach the millennium of completely synthetic materials the country will never be able to produce certain basic needs. Even synthetic rubber still requires at least 15% of natural rubber to make it a satisfactory substitute. Self-sufficiency is just entirely out of the question. On the whole, then, the Canadian committment to a career of international trade is definite.

If plans for a progressive lifting of international economic restrictions eventuate the prospect of future Canadian prosperity is indeed bright. If the country can successfully pursue policies in harmony with such a lifting of the trade barriers, there is no reason why the government target of $1,750 million of exports (including non-monetary gold) annually[1], which means roughly a 60% increase in value and a 15% increase in volume over the immediately prewar level, should not be exceeded. In terms of current dollars and under favourable conditions we can foresee that postwar exports (including non-monetary gold) might easily maintain for some time an average of $2,000 million, with total merchandise trade

[1] Government white paper "Employment and Income", April 1945

probably close to $3,750 million. These optimistic estimates, though considerably above interwar levels, do not look entirely out of line if placed on Chart XIII (which excludes gold).

It might have been thought that, insofar as increased industrialization has made the country less dependent on foreign sources and less sensitive to fluctuations in trade, foreign trade would actually tend to decrease. On the contrary, the record has shown that under conditions of free, multilateral trade industrialization actually increases trade. Before the war by far the largest share of world trade was carried on between industrialized countries. Consequently we could expect the quantity of Canadian trade to increase, though its character might change. Canada might not import and export the same items as heretofore, but she would import and export more.

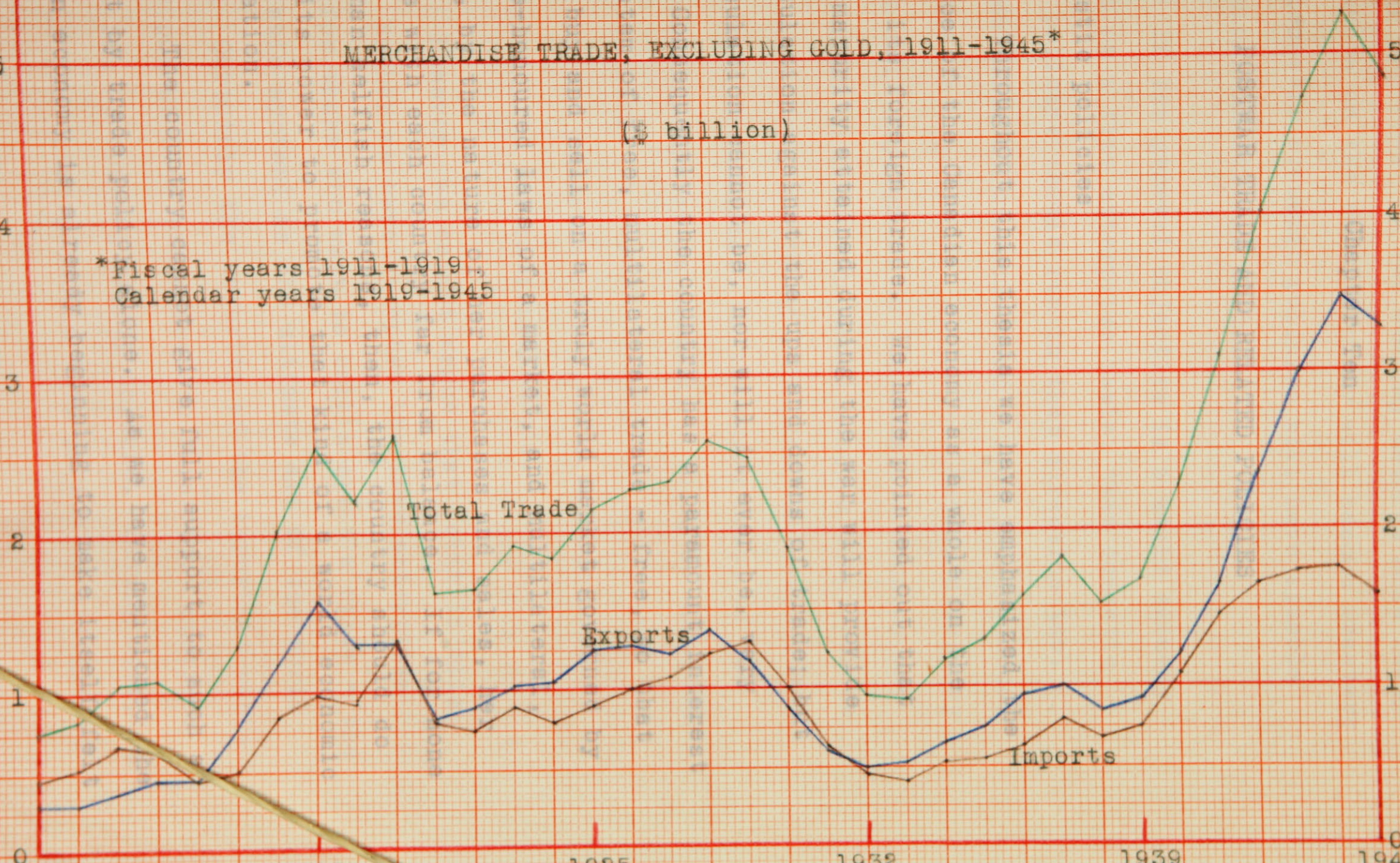
Another factor affecting foreign trade, particularly imports, is the level of national income. Just as foreign trade affects the standard of living, so the standard of living affects foreign trade. So that domestic policies will have a strong influence in determining the future level of Canadian foreign trade. We turn to a brief discussion of these policies in the final chapter.

Chart XIII

MERCHANDISE TRADE, EXCLUDING GOLD, 1911-1945*

($ billion)

*Fiscal years 1911-1919
Calendar years 1919-1945



Sources: "Canada Year Book", "Trade of Canada, 1944", Commercial Intelligence Journal"

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Chapter Ten

POSTWAR TRADE AND RELATED POLICIES

a) Domestic policies

Throughout this thesis we have emphasized the dependence of the Canadian economy as a whole on the state of its foreign trade. We have pointed out that greater maturity attained during the war will provide some insulation against the ups and downs of trade; but that insulation cannot be, nor will it ever be, very great. Consequently the country has a paramount interest in a system of free, multilateral trade - free, so that she can buy and sell on a truly world market governed by the time-honoured laws of a market, and multilateral, because, by the nature of her purchases and sales, her dealings with each country far from balance. If for none other than selfish reasons, then, the country should do all in its power to promote that kind of a world economic organization.

The country cannot give full support to such a movement by trade policy alone. As we have mentioned the Canadian economy is already beginning to make itself felt

outside its borders. The lines of influence no longer run solely inwards. As the economy matures more fully its influence on the world economy will become greater; so that domestic economic policies will have sizable repercussions in foreign trade.

If the general objective is a world economy patterned on a free enterprise basis, then domestic economic policies should run in that direction too. Regimented domestic economies and a free international economy are incompatible. If the mechanisms necessary to obtain full employment in the domestic economy are not compatible with international cooperation, then we must either accept something less than full employment or find other mechanisms. On the other hand, if the free enterprise system is actually a thing of the past and we now intend to depend on complete government planning in the domestic sphere, then we also must expect control in international trade.

However, we cannot argue that point in this thesis. Rather we have accepted the free enterprise system (for those who want to call a spade a spade - the capitalistic system) as the ultimate aim of the world economy. Certainly the majority of the important world economic powers have subscribed to this aim. Russia's position is, of course, highly obscure. Having accepted this point the country should then pursue an integrated

economic policy.

On the basis of our study a level of foreign trade of the kind foreseen on page 142 would involve a national income of some $6-7 billion. A national income of that size compared to interwar figures (Table 2, p.10) poses many domestic economic problems whose solution must be handled with care. The whole thing is interrelated; we cannot segregate commercial policy in an airtight compartment. It is not within the scope of this thesis to indicate the various measures the government's financial, monetary, labour, and taxation policies should pursue. We do point out, however, that they should pursue measures which are compatible with its trade policy.

Probably the most pressing question in this connection is price control policy. There is no doubt that a well and sanely controlled price system will give Canada certain advantages in the world market and in the barter terms of trade. It will certainly encourage exports. But the authorities must be wary of contradicting other policies too strongly. There is no sense in encouraging merchandise imports from certain countries if those countries are unable to sell in the Canadian market at existing prices. If Canada manages to hold internal prices below the general inflated world level, then we must accept the fact that the country will not be a good

market for many foreign suppliers. As a consequence Canadian loans abroad may well become the most important means whereby foreign countries are able to pay for Canadian exports, at least until world prices settle down. In other words, price control policy must be integrated with import and foreign loan policies.

There is also the related question of foreign exchange control. A foreign exchange control system which sets the Can.$ in a certain relationship to other currencies while a price control system is setting it in another relationship contains contradictory elements which, if they become too great, may have serious consequences. It is very difficult to determine by arbitrary measures what a proper exchange rate should be, particularly in view of the countless factors which have to be taken into consideration; but there is no doubt that the various relationships which were responsible for the original setting of the rate of the Can.$ on the official exchanges have changed considerably since the beginning of the war. At present the evidence seems to point to the fact that existing rates undervalue the Can.$ somewhat vis-a-vis the £ and possibly undervalue it slightly vis-a-vis the U.S.$. The undervaluation is probably not very great, and may be only temporary. Certainly it does not present the direct difficulties to the country that an overvaluation would. Nevertheless, rigid, distorted exchange rates do not allow a free play

and balanced solution of economic forces in the international sphere. There is the further obstacle that foreign exchange control presents to foreign trade in that it is the most efficient mechanism for government control of trade. These problems of exchange control must be squarely faced by the Canadian authorities in determining present trade policy, rather than left indefinitely to the International Monetary Fund; although that organization promises to provide a solution in this connection by its prohibition of national control of current transactions once the transition period (up to five years) is over except by special permission, and by its flexible yet stable system of exchange rates.

b) Investment policies

We have emphasized the influence international investment has had on Canadian foreign trade in the past; and postwar conditions are such that this condition will be multiplied. Canada cannot expect to have an active balance of trade all carried in a Canadian merchant marine, export the product of a large gold production, play host to millions of foreigners while Canadians stay at home themselves, retire foreign-held securities, and still invest only in Canada. That is not the balance of payments. The country must maintain an outward flow of Can.$ on capital account by new investment abroad. Canadian foreign investment will not only provide foreign

exchange for exports, but insofar as it increases productivity and purchasing power in the foreign country it will provide a larger market.

For a few years at least the demand for Canadian goods will be much larger than the ability to pay for the same. But the only countries to whom Canada will be able to sell her merchandise are those who will be able to procure Can.$ for payment, and as we have mentioned, one of the chief sources of Can.$ will be through the foreign investment sphere. The International Bank for Reconstruction and Development is designed to render some aid in this connection (when it commences operations!), but the country must be prepared to loan more than its quota of U.S.$325 million abroad if it intends to expand its export trade to the desired extent.

We noted in Chapter 8 a recent flow of private investment to the United Kingdom. This and other investment abroad through the International Bank should be encouraged - with the following qualification. Some provision should be made that the flow of Canadian capital abroad, including government loans and credits, be used for purposes which promise a genuine prospect of repayment. This would, of course, be ensured by loaning through the International Bank when it commences operations. Without advocating complete government control of international capital movements (which actually

the International Monetary Fund does allow) we believe some effort should be made to prevent the misdirection, of the type made by the United States during the interwar period, of any investment that may flow outside the International Bank.

Until a flow through private channels is able to cover the needs adequately some provision must be made to fill the gap. The credits extended under the Export Credits Insurance Corporation and the $1,250 million Loan to Britain do this admirably. Whether the Canadian citizen buys a government bond or pays taxes the proceeds of which the Canadian government in turn loans to the United Kingdom, or whether he buys, say, British Consols directly amounts to the same thing so far as the balance of payments and the supply of Can.$ to the United Kingdom are concerned.

There is little doubt that the Loan to Britain is in Canadian interests. As we have shown the British market has been, and can be again, an important one. The revival of that market will contribute much to Canadian prosperity. But we must be wary of helping to revive any market beyond its capacity to sustain itself. If the United Kingdom can show good promise of being able to repay this loan, then it is sound economic policy. But if the British economy has reached such a condition that it will require periodic large loans to sustain it

at the presently desired level, then the thing will inevitably collapse; and Canada would do better to regard the present loan as a gift and forget the British market as a major support of the Canadian economy. It is difficult to make any final judgment so early in the game; but, happily, the British economy has thus far shown a strong recovery. Certainly the already significant revival of British trade promises much.

This policy of encouraging Canadian investment abroad should be pursued only with a clear knowledge of the eventual results. As industry revives in Europe some war stimulated Canadian industries will face stiff foreign competition. This may be a good thing for the country as a whole, but it will certainly create some difficulties of adjustment in particular sections. These difficulties will be minimized to the extent that Canadian economic conditions and the level of international trade remain high. There is the further result, admittedly some way off in the Canadian case, that the country must be willing to face an eventual import surplus. Loans and investment, if well directed, will in time be repaid, which is a good thing. This repayment, as the United States has proven, must take the ultimate form of goods. However, due to the high absorptive capacity of the Canadian economy for imports, an import surplus should not prove any great problem for the Dominion.

As a final word in connection with Canadian investment abroad it should be mentioned that a wholesale repatriation of Canadian securities will not have the same effect as an equal amount of Canadian investment abroad, although Canada's final position, whether debit or credit, on international account would be about the same. In the first place international investment stimulates trade tremendously, whereas repatriation of such investment has the opposite effect. And in the second place international investment, by providing a constant flow of foreign exchange through interest and dividend payments, imparts flexibility to the balance of payments and helps keep the trade mechanism operating.

c) Trade policy

We have come to the conclusion that a general policy of freer, multilateral trade is a desirable one for Canada to pursue, and that the various policies related to foreign trade should be directed to that end. But, once a free international framework has been constructed, we cannot take it for granted that those products in which Canada enjoys an advantage in comparative costs will naturally flow into export channels. An effort has to be made. With proper trade promotion foreign markets can be developed and demand stimulated, though purchasing power cannot, of course, be created by promotion alone. It is not our task to

delineate step by step the various points of such a trade policy. However, there are certain points our thesis has consistently touched which we shall mention in conclusion.

More important than foreign investment as a source of supply of Can.$ for foreign countries is merchandise imports. Consequently, if the country maintains a high level of imports it will the more easily maintain a high level of exports; not to mention the fillip such a policy would give to freer trade. A separate division has actually been set up in the Department of Trade and Commerce to study import needs and encourage merchandise imports. Evidently the Canadian government has learned the lesson that if one wishes to export one must be willing to import, a lesson, the learning of which has presented insuperable difficulties to governments for a long time. Perhaps the nature of the economy, in which many imports are a downright necessity and extensive importation helps raise the standard of living, has made this lesson the easier to be learned.

Should any of Canada's markets experience balance of payments difficulties such a policy of import development would render considerable aid to Canadian foreign trade. By encouraging imports from any country Canada would lessen the necessity of

negotiating an outright clearing agreement with that country. Or if trade should eventually be forced into a series of bilateral agreements the encouragement of imports would be a very important means to sustain that trade at as high a level as possible. For a few years of the transition period there seems to be no doubt that certain countries will be forced to carry on their international transactions through some sort of a clearing arrangement, at least an implicit one. Heavy Canadian imports will mitigate this condition.

To this end it seems that any equalization of Canadian imports from and exports to each country would be of some help as a long-run policy in lessening the stress on the balance of payments. Naturally this should be in the direction of a levelling up rather than a levelling down of trade. The very nature of the Canadian economy and the history of Canadian foreign trade makes it extremely unlikely that Canada could ever balance her merchandise trade transactions with each country, but any improvement in this connection, particularly with the United States and the United Kingdom, would ease balance of payment problems. Certainly we do not recommend discriminatory trade practices to bring it about. Rather it should be a general aim of <u>long-run</u> trade policy and should be held in view in tariff negotiation.

This leads us to another question to which we have paid considerable attention throughout this thesis - the broadening of the Canadian trade relationships. We have already mentioned that more important as a factor in postwar Canadian-American trade than the increasingly heavy wartime dependence of Canada on the United States as a source of supply is the increased self-sufficiency of the Canadian economy, particularly in industrial machinery and materials. This will no doubt mean that the proportion of Canadian imports coming from the United States will drop from the 1944 high of 82.3%. But even the prewar proportion of over 60% seems to be also somewhat high. Inevitably Canada must lean economically to a large extent on the United States. A close integration of the two economies is probably a good thing. But the extent to which Canada has depended on the United States in the past is not a good thing - for Canada. Far be it from us to hinder the flow of goods and services across the Canadian-American border, but we would place the greatest emphasis on the development of profitable trading relationships <u>outside</u> the United States. The country has made a fine start in some areas during the war, and has received unexpected assistance from present industrial unrest in the United States. This advantage should not be allowed to slip.

One country from whom Canada must of necessity increase her imports is the United Kingdom. This will be

doubly important as long as the Labour government in Britain continues to follow an indefinite policy so far as the socialization of industry is concerned. Such a policy does not attract foreign investment to the country, with the result that government loans and British merchandise exports are her only means of paying for imports.

Two other particular areas are worth mentioning. One is India. A country of some four hundred million, with rich resources complementary to those of Canada and just commencing serious industrialization, should offer Canada much opportunity for the development of mutually beneficial trade.

The other area is South America. During the war Canada turned to South America as an important source of raw materials. In 1939 she imported $21.0 million worth of goods and exported $16.2 million worth to that area. In 1944 imports had increased to $54.8 million and exports to $26.1 million.[1] The present is an excellent time to extend these relationships and so broaden Canadian foreign trade. Extensive Canadian imports from this area give the country a useful lever in trade negotiations.

The South American Republics have the further very desirable attribute as a trading partner of a

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[1] "Trade of Canada, 1944"

plentiful supply of gold and U.S.$ acquired during the war. They have cash of the kind Canada can use with which to pay for imports from Canada. This would be a very important consideration should the reserves of the Bank of Canada be low. An active balance of merchandise trade can, of course, be reflected in a building up of monetary reserves rather than in investment abroad. This would be more easily and directly accomplished if gold and valuable currencies were received directly in merchandise trade operations. Naturally it is impossible for us to determine what has happened to the $225.7 million of gold and $27.7 million of foreign exchange the Bank of Canada sold to the Foreign Exchange Control Board in May, 1940 under the Foreign Exchange Acquisition Order and the Exchange Fund Order, which temporarily suspended its minimum reserve requirements. Since that time the £ and U.S.$ the Bank has kept under 'reserve' for its short-term requirements and necessary working balances have fluctuated violently from a month end balance of as low as $.2 million to as high as $377 million[1]. It is possible that, due to its large increase in liabilities, the Bank's reserves will be rather low when the above-mentioned orders are rescinded and certain Foreign Exchange Control Board assets are returned to it. If such is the case, and the authorities who have access to the inner workings of the Foreign Exchange Control Board are aware

[1]Bank of Canada "Statistical Summary"

of the position, then merchandise trade policy could play a very important part in this connection.

The general problem of trade policy in the postwar world, as of all economic policies, will be one of economic isolationism and government control. Throughout this thesis we have avoided a direct analysis of the tariff question. (Consequently our observations must be taken with some reservation.) However, it must be remembered that tariffs, provided they are relatively stable, are not foreign to a free economy. Just the same the tariff question is something that the makers of trade policy must study very closely. But it is the more direct government control of trade commonly known under the general term of quantitative trade restrictions that must receive the greatest attention. Since we have accepted free enterprise as the ultimate aim of the world economy it is the problems engendered by this last kind of restriction that must be first resolved.

During the war bulk purchasing and selling under direct government control replaced private competitive enterprise in international trade. Once the central international boards in Washington had handed down their decisions the Canadian importer or exporter was still not free to carry on business within the prescribed boundaries. He had to do business with a whole host of Canadian boards, committees, controllers, and government corporations.

Rarely did he deal directly with his foreign private buyer or seller. He bought from or sold to Canadian or foreign government agencies; or at the very least transacted his business on government licensed forms which had to be approved at every step of the transaction. He usually acted merely as an agent for the government corporation concerned.

If it is now intended to return to a relatively free system of individual initiative in international trade this enormous hierarchy of government buying, selling, and merchandise and market allocating agencies will have to be dissolved. That is an international problem which can be solved only by international cooperation. Canada can do her bit, for her system of economic control is second to none in completeness. There is general agreement that it would be very foolish to abolish all economic controls immediately. However, that is no excuse for the government to hang on to them merely through habit or inertia. Only those controls which are conducive to the restoration of the Canadian productive machine to a point where it can join freely and without disadvantage in a free international trading system need be retained.

A relaxation of controls entails, of course, the idea that the state must accept limitations to its sovereignty, which idea is really the crux of the whole

problem. Until this basic political problem is resolved little can be accomplished in solving the principal economic problems, as intertwined as the two are.

It is yet too early to determine whether the world trading system will take the path of free enterprise or continue its way of nationalistic control. During the interwar period there was certainly a divergence between actual national commercial policies and the recommendations of international conferences and committees. However, this time there seems to be a general awareness of the consequences of selfish national restrictions. The question is whether that awareness can be translated into effective action, whether a common international cooperation can be attained which will aim to make economic conditions generally endurable and peace thereby durable.

One is almost tempted to say, in the shadow of an awful atomic catastrophe, "if we don't do it this time we shall never have another chance". However, centuries of history indicate that, rather than go completely one way or the other, world economic organization will undoubtedly resolve the struggle somewhat and take a course somewhere between a nationalistic control and a free enterprise world economy. We hope that it will be rather less of the former and more of the latter.

On the basis of our study it seems that the Canadian economy in the postwar world would find such a compromise course most accommodating. Certainly to the extent that the world turns from complete economic isolationism Canada will gain. But, although we have strongly supported a free international economic framework as being to the Canadian advantage, there is no doubt that some sort of control is necessary to provide a workable framework. Unfettered "laissez-faire" does not work. That we have learned by experience. A logical solution seems to be presented through such organizations as the International Monetary Fund and the International Bank for Reconstruction and Development in which national economic liberty is to be rationalized where it becomes licence in the international sphere. If this type of solution fully developes Canadian foreign trade can look to the future with considerable optimism.

Appendix I

INTERWAR STATISTICS

Appendix I presents the various statistical series from which the tables and charts dealing with the interwar period in this thesis have been drawn up. The selection of statistics is fairly complete, so that the reader can draw his own conclusions therefrom, quite independent of the writer's, if he so desires.

The authorities for each series, all Dominion Bureau of Statistics publications, are given below in columnar order. All indexes are based 1926=100, and all values are in $ million. Refer to Appendix III for an explanation of the place of gold in trade statistics.

1) Index of Gross Value of Manufactures: Computed from Gross Value of Manufacturing in "Canada Year Book".

2) Index of Wholesale Prices: "Prices and Price Indexes 1913-1939".

3) Index of Employment: 1919 and 1920 not available, 1921-1939 from "Annual Review of the Employment Situation in Canada, 1940".

4) Index of Industrial Production: 1919-1933 from "Review of Economic Tendencies 1919-1934", 1934-1936 from "Economic

Fluctuations in Canada during the Postwar Period, 1938", 1937-1939 from "Business Conditions in Canada, 1939".

5) Index of Gross Value of Agriculture: Computed from Gross Value of Agricultural Production in "Canada Year Book".

6) Value of National Income: National Income produced minus the international balance on Interest and Dividends, from "Canada Year Book, 1943-44".

7) Index of National Income: Computed from (6).

8) Total Merchandise Trade: Including non-monetary gold, sum of Imports (9) and Exports (15)

9) Value of Merchandise Imports: Including non-monetary gold, from "Trade of Canada, 1939". Although this source officially "excludes gold", the import figures it contains actually include very small amounts of genuine imports of commercial gold (i.e. non-monetary gold) in the form of jewellers' sweepings, etc. Except for 1938, there have been no Canadian imports of bullion during the period; and we have excluded that movement in 1938, as is explained in Appendix III.

10) Index of Value of Merchandise Imports: Computed from (9).

11) Index of Import Prices: Wholesale prices of merchandise imports, from "Prices and Price Indexes 1913-1939".

12) Volume of Merchandise Imports: Obtained by dividing Index of Value of Merchandise Imports (10) by Index of

Import Prices (11)

13) Domestic Exports: Merchandise Exports of domestic origin, including non-monetary gold; 1919-1938 from "Review of Canada's Foreign Trade Calendar Year, 1938"; 1939 obtained by adding to Domestic Exports excluding gold for 1939 from "Trade of Canada, 1939" an estimate of domestic exports of non-monetary gold for that year. The estimate was made by projecting to December, 1939 the Dominion Bureau of Statistics released figures for domestic gold exports January-August of that year. If compared to figures of Canadian gold production and of net exports of non-monetary gold for 1939 the estimate appears to be very accurate.

14) Foreign Exports: Merchandise Exports of foreign origin originally imported for consumption, including non-monetary gold; 1919-1938 from "Review of Canada's Foreign Trade Calendar Year, 1938"; 1939 obtained by adding to Foreign Exports excluding gold for 1939 from "Trade of Canada, 1939" an estimate of foreign exports of non-monetary gold for that year. The estimate was made by projecting to December, 1939 the Dominion Bureau of Statistics released figures for foreign gold exports January-August of that year. Obviously, it is taken for granted that there were no outstanding non-monetary gold movements during the last four months of 1939. Published figures of net exports of non-monetary gold for 1939 would seem to bear this out.

15) Total Merchandise Exports: Including non-monetary gold, Domestic (13) plus Foreign (14) Exports.

16) Balance of Merchandise Trade: Including non-monetary gold, active balance in black, passive balance in red; Total Merchandise Exports (15) minus Merchandise Imports (9).

17) Total Merchandise Exports Excluding Gold: Excluding non-monetary gold, from "Trade of Canada, 1939".

18) Index of Value of Merchandise Exports: Computed from (15).

19) Index of Export Prices: Wholesale prices of merchandise exports, from "Prices and Price Indexes 1913-1939".

20) Volume of Merchandise Exports: Obtained by dividing Index of Value of Merchandise Exports (18) by Index of Export Prices (19).

Interwar Statistics

Year	(1) Index of Gross Value Manufactures	(2) Index of Wholesale Prices	(3) Index of Employment	(4) Index of Industrial Production
1919	103.9	134.0	-	65.5
1920	119.7	155.9	-	69.9
1921	80.2	110.0	88.8	60.4
1922	76.5	97.3	89.0	76.9
1923	85.9	98.0	95.8	83.8
1924	82.8	99.4	93.4	82.4
1925	90.7	102.6	93.6	89.7
1926	100.0	100.0	99.6	100.0
1927	104.8	97.7	104.6	105.6
1928	115.5	96.4	111.6	117.8
1929	125.4	95.6	119.0	127.4
1930	105.7	86.6	113.4	108.0
1931	82.3	72.1	102.5	90.4
1932	63.9	66.7	87.5	74.0
1933	63.0	67.1	83.4	76.8
1934	77.2	71.6	96.0	93.6
1935	85.5	72.1	99.4	103.6
1936	96.8	74.6	103.7	114.4
1937	117.0	84.6	114.1	126.8
1938	107.7	78.6	111.8	114.7
1939	112.2	75.4	113.9	125.6

Interwar Statistics (continued)

Year	(5) Index of Gross Value Agriculture	(6) Value of National Income	(7) Index of National Income	(8) Total Merchandise Trade
1919	125.3	3816	84.7	2236
1920	119.5	4598	102.0	2640
1921	82.4	3507	77.8	1616
1922	82.5	3671	81.4	1661
1923	83.0	3847	85.4	1932
1924	88.8	3865	85.8	1879
1925	98.9	4239	94.1	2173
1926	100.0	4507	100.0	2297
1927	105.8	4738	105.1	2329
1928	107.3	5269	116.9	2603
1929	96.9	5273	117.0	2510
1930	73.4	4452	98.8	1914
1931	49.9	3580	79.4	1257
1932	45.6	2813	62.4	1007
1933	47.7	2723	60.4	1004
1934	55.3	3147	69.8	1279
1935	55.8	3371	74.8	1389
1936	63.3	3827	84.9	1663
1937	61.7	4368	96.9	1934
1938	63.2	4291	95.2	1684
1939	72.8	4554	101.1	1850

Interwar Statistics (continued)

Year	(9) Value of Mdse. Imports	(10) Index of Mdse. Imports	(11) Index of Import Prices	(12) Volume of Mdse. Imports
1919	941	93.4	139.6	66.9
1920	1337	132.6	158.8	83.5
1921	799	79.3	105.8	75.0
1922	762	75.6	100.4	75.3
1923	903	89.6	110.0	81.5
1924	808	80.2	105.0	76.4
1925	890	88.3	105.6	83.6
1926	1008	100.0	100.0	100.0
1927	1087	107.8	97.7	110.3
1928	1222	121.2	96.1	126.1
1929	1299	128.8	94.2	136.7
1930	1008	100.0	83.7	119.5
1931	628	62.3	72.4	86.1
1932	453	44.9	70.5	63.7
1933	401	39.8	73.0	54.5
1934	513	50.9	76.5	66.5
1935	550	54.6	77.9	70.1
1936	635	63.0	79.4	79.3
1937	809	80.3	89.8	89.4
1938	677	67.2	83.1	80.9
1939	751	74.5	84.4	88.3

Interwar Statistics (continued)

Year	(13) Domestic Exports	(14) Foreign Exports	(15) Total Mdse. Exports	(16) Balance Mdse. Trade	(17) Total Mdse. Exports Exc. gold
1919	1241	54	1295	354	1290
1920	1273	30	1303	34	1298
1921	803	14	817	17	814
1922	884	14	898	136	898
1923	1015	14	1029	125	1016
1924	1058	13	1070	262	1042
1925	1271	12	1283	393	1252
1926	1273	15	1289	281	1277
1927	1222	20	1242	155	1231
1928	1357	24	1381	159	1364
1929	1185	26	1211	88	1178
1930	886	19	905	103	883
1931	617	12	629	1	600
1932	546	8	554	102	498
1933	597	6	603	201	535
1934	759	7	766	252	656
1935	825	13	838	288	738
1936	1015	13	1028	393	951
1937	1110	15	1125	316	1012
1938	913	43	957	279	849
1939	1087	12	1099	348	936

Interwar Statistics (continued)

Year	(18) Index of Mdse. Exports	(19) Index of Export Prices	(20) Volume of Mdse. Exports
1919	100.5	134.8	74.6
1920	101.1	158.1	63.9
1921	63.4	116.5	54.4
1922	69.7	94.7	73.6
1923	79.8	93.5	85.3
1924	83.0	95.7	86.7
1925	99.5	104.5	95.2
1926	100.0	100.0	100.0
1927	96.4	97.8	98.6
1928	107.1	94.2	113.7
1929	93.9	92.2	101.8
1930	70.2	77.4	90.7
1931	48.8	60.5	80.7
1932	43.0	54.9	78.3
1933	46.8	55.2	84.8
1934	59.4	60.6	98.0
1935	65.0	62.2	104.5
1936	79.8	66.8	119.5
1937	87.3	81.8	107.6
1938	74.2	70.9	104.7
1939	85.3	83.5	104.5

Appendix II

EXPORTS AND NATIONAL INCOME

In order to study the relationship between exports and national income during the interwar period it is considered desirable to first eliminate the long term trend of each for the period; assuming, of course, that there is one, and that it can be fairly represented by a straight line of the type $y = a + bx$. The method used is that of the least squares as given by Mills in his "Statistical Methods".

We insert the proper values in the two equations:

$$\Sigma y = na + b\Sigma x$$

$$\Sigma xy = ax + b\Sigma x^2$$

where

Σy = the sum of the values of y

Σx = the sum of the values of x

Σxy = the sum of the products of the paired x's and y's

Σx^2 = the sum of the squares of the values of x

n = the number of pairs of values

In the case of our time series of Exports and National Income calculation is simplified by placing the

origin at the median value, 1929. As a result x is 0, and the two equations become:

$$\Sigma y = na \ldots\ldots (1)$$

$$\Sigma xy = b\Sigma x^2 \ldots. (2)$$

Using the Exports data on page 174, where x is the time factor and y the index for Exports, we substitute in equations (1) and (2):

(1) $\Sigma y = na$

$$a = \frac{\Sigma y}{n}$$

$$= \frac{1654.2}{21}$$

$$= 78.8$$

(2) $\Sigma xy = b\Sigma x^2$

$$b = \frac{\Sigma xy}{\Sigma x^2}$$

$$= \frac{-852.9}{770}$$

$$= -1.1$$

which gives us a value of 78.8 at 1929 with annual decrements thereafter of 1.1. We project this line back to 1919, at which point we can say our trend line begins at 89.8, and, with annual decrements of 1.1, runs to 67.8 in 1939.

Having determined the secular trend line, z, we secure the fluctuations from it by applying to it the original data, y (p.175); and thence the standard deviation, which is, of course, the square root of the arithmetic mean of the sum of the squares of the deviations of the original data from the trend, that is:

$$\sigma = \frac{\Sigma(y-z)^2}{n}$$

$$= \frac{6541.96}{21}$$

$$= 17.7$$

We then express the differences between the

Merchandise Exports* 1919-1939

Year	Time Factor x	Export Index y	xy	x^2	Trend Line z
1919	-10	100.5	-1005.0	100	89.8
1920	-9	101.1	-909.9	81	88.7
1921	-8	63.4	-507.2	64	87.6
1922	-7	69.7	-487.9	49	86.5
1923	-6	79.8	-478.8	36	85.4
1924	-5	83.0	-415.0	25	84.3
1925	-4	99.5	-398.0	16	83.2
1926	-3	100.0	-300.0	9	82.1
1927	-2	96.4	-192.8	4	81.0
1928	-1	107.1	-107.1	1	79.9
1929	0	93.9	0.0	0	78.8
1930	+1	70.2	+70.2	1	77.7
1931	+2	48.8	+97.6	4	76.6
1932	+3	43.0	+129.0	9	75.5
1933	+4	46.8	+187.2	16	74.4
1934	+5	59.4	+297.0	25	73.3
1935	+6	65.0	+390.0	36	72.2
1936	+7	79.8	+558.6	49	71.1
1937	+8	87.3	+698.4	64	70.0
1938	+9	74.2	+667.8	81	68.9
1939	+10	85.3	+853.0	100	67.8
		1654.2	-852.9	770	

* Including non-monetary gold

Source: Appendix I

Merchandise Exports* 1919-1939 (continued)

Year	Export Index y	Trend Line z	y-z	$(y-z)^2$	(y-z) in terms of σ
1919	100.5	89.8	∔10.7	114.49	∔.60
1920	101.1	88.7	∔12.4	153.76	∔.70
1921	63.4	87.6	-24.2	585.64	-1.37
1922	69.7	86.5	-16.2	262.44	-.92
1923	79.8	85.4	-5.6	31.36	-.32
1924	83.0	84.3	-1.3	1.69	-.07
1925	99.5	83.2	∔16.3	265.69	∔.92
1926	100.0	82.1	∔17.9	320.41	∔1.01
1927	96.4	81.0	∔15.4	237.16	∔.87
1928	107.1	79.9	∔27.2	739.84	∔1.54
1929	93.9	78.8	∔15.1	228.01	∔.86
1930	70.2	77.7	-7.5	56.25	-.42
1931	48.8	76.6	-27.8	772.84	-1.57
1932	43.0	75.5	-32.5	1056.25	-1.84
1933	46.8	74.4	-27.6	761.76	-1.51
1934	59.4	73.3	-13.9	193.21	-.79
1935	65.0	72.2	-7.2	51.84	-.41
1936	79.8	71.1	∔8.7	75.69	∔.49
1937	87.3	70.0	∔17.3	299.29	∔.98
1938	74.2	68.9	∔5.3	28.09	∔.30
1939	85.3	67.8	∔17.5	306.25	∔.99
	1654.2			6541.96	

* Including non-monetary gold

Source: Appendix I

original data and the trend, y - z, in terms of σ (p.175) for comparison with that of National Income (c.f. Chart IV, p.16).

The trend line for National Income is secured in the same way. Substituting the values shown on page 177 in the two equations:

(1) $\Sigma y = na$

$$a = \frac{\Sigma y}{n}$$

$$= \frac{1873.8}{21}$$

$$= 89.2$$

(2) $\Sigma xy = b\Sigma x^2$

$$b = \frac{\Sigma xy}{\Sigma x^2}$$

$$= \frac{-181.6}{770}$$

$$= -.23$$

we find the trend line runs from 91.5 in 1919, with annual decrements of .23, to 86.9 in 1939.

Similarly we find the standard deviation:

$$\sigma = \frac{\Sigma(y-z)^2}{n}$$

$$= \frac{4862.75}{21}$$

$$= 15.2$$

and express the fluctuations from trend in terms of it (p.178) for comparison with the Exports series (c.f. Chart IV, p.16).

The coefficient of correlation, r, between Exports and National Income is the measure of proportion of variation between the two. Perfect direct relationship would give r a value of ± 1, though actually anything over $\pm .5$ shows some significance. The coefficient is determined from the following formula:

$$r = \frac{\Sigma(y-z)_1(y-z)_2}{n\sigma_1\sigma_2}$$

National Income 1919-1939

Year	Time Factor x	Index Nat. Inc. y	xy	x^2	Trend Line z
1919	-10	84.7	-847.0	100	91.5
1920	-9	102.0	-918.0	81	91.3
1921	-8	77.8	-622.4	64	91.0
1922	-7	81.4	-569.8	49	90.8
1923	-6	85.4	-512.4	36	90.6
1924	-5	85.8	-429.0	25	90.4
1925	-4	94.1	-376.4	16	90.1
1926	-3	100.0	-300.0	9	89.9
1927	-2	105.1	-210.2	4	89.7
1928	-1	116.9	-116.9	1	89.4
1929	0	117.0	0.0	0	89.2
1930	+1	98.8	+98.8	1	89.0
1931	+2	79.4	+158.8	4	88.7
1932	+3	62.4	+187.2	9	88.5
1933	+4	60.4	+241.6	16	88.3
1934	+5	69.8	+349.0	25	88.1
1935	+6	74.8	+448.8	36	87.8
1936	+7	84.9	+594.3	49	87.6
1937	+8	96.9	+775.2	64	87.4
1938	+9	95.2	+856.8	81	87.1
1939	+10	101.0	+1010.0	100	86.9
		1875.8	-181.6	770	

Source: Appendix I

National Income 1919-1939 (continued)

Year	Index Nat. Inc. y	Trend Line z	y-z	$(y-z)^2$	(y-z) in terms of σ
1919	84.7	91.5	-6.8	46.24	-.45
1920	102.0	91.3	+10.7	114.49	+.70
1921	77.8	91.0	-13.2	174.24	-.87
1922	81.4	90.8	-9.4	88.36	-.62
1923	85.4	90.6	-5.2	27.04	-.34
1924	85.8	90.4	-4.6	21.16	-.30
1925	94.1	90.1	+4.0	16.00	+.26
1926	100.0	89.9	+10.1	102.01	+.66
1927	105.1	89.7	+15.4	237.16	+1.01
1928	116.9	89.4	+27.5	756.25	+1.81
1929	117.0	89.2	+27.8	772.84	+1.82
1930	98.8	89.0	+9.8	96.04	+.64
1931	79.4	88.7	-9.3	86.49	-.61
1932	62.4	88.5	-26.1	681.21	-1.72
1933	60.4	88.3	-27.9	778.41	-1.84
1934	69.8	88.1	-18.3	334.89	-1.21
1935	74.8	87.8	-13.0	169.00	-.86
1936	84.9	87.6	-2.5	6.25	-.16
1937	96.9	87.4	+9.5	90.25	+.62
1938	95.2	87.1	+8.1	65.61	+.53
1939	101.0	86.9	+14.1	198.81	+.93
	1873.8			4802.75	

Source: Appendix I

Coefficient of Correlation: Exports and National Income

Year	Differences in Exports $(y-z)_1$	Differences in Nat. Inc. $(y-z)_2$	$(y-z)_1(y-z)_2$
1919	ƒ10.7	-6.8	-72.76
1920	ƒ12.4	ƒ10.7	ƒ132.68
1921	-24.2	-13.2	ƒ319.44
1922	-16.2	-9.4	ƒ152.28
1923	-5.6	-5.2	ƒ29.12
1924	-1.3	-4.6	ƒ5.98
1925	ƒ16.3	ƒ4.0	ƒ65.20
1926	ƒ17.9	ƒ10.1	ƒ180.79
1927	ƒ15.4	ƒ15.4	ƒ237.16
1928	ƒ27.2	ƒ27.5	ƒ748.00
1929	ƒ15.1	ƒ27.8	ƒ419.78
1930	-7.5	ƒ9.8	-73.50
1931	-27.8	-9.3	ƒ258.54
1932	-32.5	-26.1	ƒ848.25
1933	-27.6	-27.9	ƒ770.04
1934	-13.9	-18.3	ƒ254.37
1935	-7.2	-13.0	ƒ93.60
1936	ƒ8.7	-2.5	-21.75
1937	ƒ17.3	ƒ9.5	ƒ164.35
1938	ƒ5.3	ƒ8.1	ƒ42.93
1939	ƒ17.5	ƒ14.1	ƒ246.75
			ƒ4801.25

where

$(y-z)_1$ = differences between data and trend line in Exports

$(y-z)_2$ = differences between data and trend line in National Income

σ_1 = σ Exports

σ_2 = σ National Income

Substituting the values determined on page 179 we find:

$$r = \frac{\pm 4801.25}{21 \times 17.7 \times 15.2}$$

$$= \pm .85$$

a very high coefficient indeed.

Appendix III

PLACE OF GOLD IN MERCHANDISE TRADE STATISTICS

This appendix is intended only as a brief explanation of the position of gold in merchandise trade and the balance of payments in this thesis.

First, let it be said that an exact interpretation of gold statistics is in no way aided by the almost complete lack of uniformity of treatment of such statistics by the Bank of Canada, the Dominion Bureau of Statistics, External Trade Branch, and Mining, Metallurgical, and Chemical Branch. This has been due, of course, not solely to official vacillation, but largely to the anomalous position gold has acquired.

On the one hand, gold would seem to be one of Canada's export staples, a product of her resources and industry, exported with little relation to the state of the domestic monetary system, and hence to be considered an important merchandise export. It is felt that this is the interpretation to be put on non-monetary gold movements (those which do not increase or decrease Canadian monetary gold stocks) when considering merchandise trade in relation

to the other factors in the Canadian economy. The difficulty is the interpretation of 'non-monetary gold movements'. Since we are using Dominion Bureau of Statistics trade figures we have followed the Bureau in taking 'non-monetary gold movements' to mean actual physical movements of "non-monetary" gold.

The case has been comparatively simple in respect to merchandise imports for the reason that non-monetary gold imports have been almost nil except for 1938, when the Bank of Canada shows an import of $58 million under this category. However, in common with many Dominion Bureau of Statistics publications, we have decided to disregard this outstanding movement when considering merchandise trade, and to treat it as a monetary movement, as it obviously was. (The annual domestic consumption of gold in the jewellery industry, including old gold for refining, has been under $2 million[1].)

So far as non-monetary gold exports go, these have been negligible until the thirties, when they grew to over $100 million annually from 1934, making a considerable difference in export trade figures and raising the gold producing industry to one of major importance. This was due largely to the initiation of the famous American gold buying policy in 1933. Since

[1]"Summary Review of the Gold Mining Industry in Canada"

that time the United States Treasury has been a fairy godmother to the Canadian gold mining industry. The position is, then, that non-monetary gold movements up to 1939, as interpreted by the Dominion Bureau of Statistics (i.e. excluding "earmarked" gold), have been included in merchandise trade unless otherwise specified.

On the other hand, even when divided into monetary and non-monetary categories, gold cannot escape the peculiar characteristics it has inherited from centuries of use as a money metal. The market for gold is determined to an infinitesimally small extent by ordinary commercial forces. Rather it is determined by monetary factors as dependent on the whims of governmental monetary policies. If the United States suddenly were to decide to bury only silver instead of gold in Fort Knox Canadian gold exports would suddenly drop to almost zero. For that reason, when considering the specific character and make-up of Canadian merchandise trade during the interwar years, where statistics permit, non-monetary gold is treated as an item rather distinct from other commodity items. Furthermore, gold does not have to cross a boundary to enter into international transactions. A change in earmarking can do the trick very nicely, in which case, although there has been no physical movement and hence no inclusion in merchandise trade, the gold enters the balance of international payments just the same. Annual changes in the amount of earmarked gold

held by the Bank of Canada for the account of foreigners in 1936, 1937, and 1938, were $47.0, $20.3, and $77.7 million respectively, which amounts we have not included in merchandise exports. Consequently it is felt that, under certain circumstances, gold movements should be segregated from ordinary trade transactions. Such is the case in the balance of payments, where all gold transactions, whether monetary or non-monetary, whether earmarked or physical movements, are drawn together under one heading.

Since 1939 earmarking and the importance of gold in the balance of payments have placed the metal in such a singular position that we have excluded all gold from merchandise trade commencing with the war years. If this decision were not one of choice it would be one of necessity for the simple reason that the only official gold trade figures available after August, 1939 are net gold exports. These have been: $185 million for 1939, $203 million for 1940, $204 million for 1941, $184 million for 1942, $142 million for 1943, $110 million for 1944, and $96 million for 1945[1].

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[1]Bank of Canada "Statistical Summary"

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