AFTER RECESS

The house resumed at 8 p.m.

THE BUDGET

FINANCIAL STATEMENT OF THE MINISTER OF FINANCE

Hon. Donald S. Macdonald (Minister of Finance) moved:

That this House approves in general the budgetary policy of the government.

He said: Mr. Speaker, to commence, I would like to express my thanks to my colleagues, and to the officials in my own department and of the other departments and agencies, for their assistance to me in this my first budget. May I express my appreciation also to members of this House who directly, or by correspondence, have made requests or suggestions on behalf of constituents, and to the many hundreds of Canadians who, through the year, but particularly in the last several months, have made representations concerning a wide variety of changes in our fiscal system.

Though I am completing my fourteenth year as a member of parliament and have witnessed as many budgets, still there were some surprises for me in the task of budget making. One of these has been the extent and variety of changes large and small sought in our tariff and tax system. Each of these is assessed by my officials, they are grouped for discussion and then hundreds of items cross the Finance Minister's desk for final decision. In that pre-budget period, the Finance Minister acquires a nation-wide perspective into an apparently inexhaustible variety of personal situations, commercial circumstances or fiscal problems as they affect Canadians.

I am conscious that though some will be gratified by changes arising from this evening's announcements, many will be disappointed that their requests could not be met. I regret being the source of that disappointment but equity, administrative necessity, and a wider public interest have rendered it impossible to satisfy all requests.

Before proceeding with my budget statement, and with the permission of the House, I would like to table a number of supplementary budget papers which provide extensive background material relating to some of the more important measures. I would also like to table a number of Ways and Means Motions and ask that they be appended to Votes and Proceedings. I would ask that the supplementary tables on the government's accounts be appended to today's *Hansard*.

● (2010)

Mr. Speaker: Is the House agreed that the minister table certain documents? Is it so agreed and ordered by the House?

Some hon. Members: Agreed.

[*Editor's Note: For notices of ways and means motions, see today's Votes and Proceedings*].

[*For tables referred to above see Appendix A*]

Mr. Macdonald (Rosedale):

The International Economy

I would like first to set the stage for my remarks on the Canadian economy by reviewing some of the major eco-

nomic developments taking place on the international front. These have important implications for our own country as a major participant in world trade and capital markets.

The international economy is launched on recovery from the depths of the worst recession since the great depression of the 1930's. The output of the industrial nations making up the Organization for Economic Co-operation and Development stagnated during 1974 and declined sharply at an overall annual rate of 5 per cent during the first half of last year. This decline, fortunately, was arrested by mid-year, and with the United States in the lead, the prospect for strengthening recovery seems well-assured.

The severity of the recent recession was due in large part to the impact of soaring inflation around the globe earlier in the 1970's. From early 1973 spiralling price increases contributed to a substantial reduction in consumer spending, investment, output and employment in the world at large. This process was halted only slowly and eventually reversed as the run-down of inventories ran its course, as automatic economic stabilizers like social security came into play, and as governments injected strong stimulus into their economies. With the revival under way the OECD was able last December to forecast that real output among the industrial nations would rise by 4 per cent in 1976. Since the time of that forecast the world prospect has improved further.

While this strengthening recovery is welcome, the problem of deep-seated inflation persists. Although the rate of increase in consumer prices has slowed significantly, it still remains much too high. The world community continues to face the twin tasks of bringing the rate of inflation down to acceptable levels and maintaining a healthy growth of output, employment and real incomes.

One direct result of world-wide recession was a fall of 6 per cent in the volume of international trade last year. The imports of the industrial nations in particular dropped faster than their exports, and their current account deficits declined sharply from $33 billion the previous year to $6 billion. This reduction was mirrored in the decline of the surplus of the oil-producing nations. Unfortunately, the balance of payments position of the non oil-producing developing nations worsened.

The disruptions of the past few years have severely tested the strength of the institutions and practices of international co-operation built up over the past generation. Happily these did not fail us. On the whole the major countries have refrained from solving their problems at the expense of others. Essential joint action was taken on a number of different fronts—in the General Agreement on Tariffs and Trade, the International Monetary Fund, the World Bank, the OECD and other organizations.

Last January the Interim Committee of the International Monetary Fund, of which Canada is a member, reached agreement on significant reforms in the international monetary system. The government considers that these reforms will facilitate the expansion of world trade and investment. They will help to ensure orderly conditions in exchange markets and smoother balance of payments adjustments. The reforms will be embodied in important amendments to the IMF Articles of Agreement. Later this year the government will be presenting to parliament amendments to the Bretton Woods Agreements Act for the purpose of securing parliamentary approval for these changes.

The severe economic difficulties of many of the developing countries have led to intensified discussion concerning the evolution of a new international economic order. This discussion is taking place at present in the meetings of the Conference on International Economic Co-operation in Paris and in the United Nations Conference on Trade and Development in Nairobi. We are playing an active part in both world arenas, as well as participating fully in the preliminary stages of the multilateral trade negotiations now gathering momentum in Geneva. The year ahead promises to be one of exceptional challenge, as we are called increasingly to adjust to new trends and pressures in our relations with the interdependent world community.

The Canadian Economy

Against this brief review of the international setting, I turn now to the economic situation and prospect here at home.

As a country which depends heavily for its livelihood on exports, we were inevitably affected by the deep recession experienced by our major trading partners. During 1975, the volume of our merchandise sales abroad declined by nearly 7 per cent, with obvious effects across the whole economy. A substantial drop in total real expenditures on housing construction also occurred, even though the number of housing starts rose significantly during the course of the year.

Despite the adverse impact of these developments and the run-down of inventories, I want to stress that the performance of the Canadian economy in terms of output, employment and real incomes exceeded that of virtually every other industrial nation. This was mainly because of the sustained strength in outlays of consumers, business and governments.

Given the basic tendency of the Canadian and American economies to move in parallel, the contrast between our two countries over the recent period is particularly noteworthy. In the United States, the gross national product in real terms declined by 1.8 per cent in 1974 and by a further 2 per cent last year. Canada, in contrast, achieved a real growth of 2.8 per cent in 1974, and successfully staved off any decline last year. Employment south of the border fell by about 1.3 per cent in 1975; in Canada it rose by nearly 2 per cent. Over the same period, while unemployment rose to 6.9 per cent in Canada, in the United States it reached an average level of 8.5 per cent.

Real income received per person, after payment of direct taxes and after allowing for higher prices, advanced by 2.5 per cent in Canada in both 1974 and 1975; in the U.S. it declined in both years. Over the longer span from 1971 to 1975 real disposable income per capita has risen by almost 18 per cent in Canada, three times the increase in the U.S.

In real terms, Canadian business investment in plant and equipment grew by 4.7 per cent last year, to a level 40 per cent higher than that in 1970. In the United States it decreased by 12 per cent to a level that was only 2 per cent above that of five years ago.

[Mr. Macdonald (Rosedale).]

[*Translation*]

Our better record in weathering the economic storms of the past three years compared with almost any other country in the western world was not just accidental. One of the important factors was our relatively more favourable position in petroleum supply. That made it possible for the federal government to cushion the economy against the immediate harsh impact of the four-fold jump in world oil prices. But undoubtedly the major factor was the concerted and far-reaching action by both federal and provincial governments to sustain output, employment and real incomes in the face of severe inflation and recession abroad.

During the course of 1974, fiscal and monetary policies became more expansionary. Federal policies, including further major tax reductions, were strongly reinforced by provincial governments. Automatic stabilizers in the economy such as unemployment insurance also played their role, helping to soften the impact of unemployment and buoying up the economy as a whole.

Given these circumstances and deliberate policy decisions, the fiscal position at all levels of government swung heavily into deficit last year. I would re-emphasize the point that if these expansionary policies had not been adopted, the Canadian economy would have experienced a much more severe recession than in fact it did. Recovery, though slow, has been underway for almost a year now, and the pace has started to quicken.

Nevertheless, it is also true that the relatively better performance of the Canadian economy has in itself served to intensify some of our current problems.

● (2020)

[*English*]

In 1975, a domestically-fueled spiral of costs and prices increasingly became the major source of continuing strong inflationary pressures. Understandably, individual Canadians scrambled for substantially increased incomes to catch up with others, to keep up with inflation, or to protect themselves against the risk of even more rapid inflation in future. Canadian salaries and wages began to rise at much faster rates than in the United States, our major market and our major competitor. The advance of prices in Canada also began to outpace that south of the border. This cost-price spiral posed an increasingly serious threat to the competitiveness of the Canadian economy, particularly at the stage when recovery in the United States and other countries from lower bases would provide them with the opportunity to achieve much larger productivity gains. While we may have weathered the recession better than the United States we will be hard-pressed to keep up with U.S. economic performance in its present period of rapid recovery and slower inflation.

Moreover, during 1975 Canada encountered a current account deficit with other countries of nearly $5.1 billion, a sharp deterioration from the deficit of $1.6 billion the previous year. This swing was largely a reflection of the higher level of demand sustained in Canada than abroad, with the resulting faster growth in our imports as compared with exports. There is every reason to expect that our exports will pick up strongly as recovery proceeds abroad, but we must be aware that their recovery could be adversely affected by our reduced competitive edge.

The relatively high interest rates prevailing in Canada also stem basically from the divergent course last year between domestic and international economic conditions. In particular, they reflect today a combination of factors—notably the continuing high rates of price increase, a strong demand for credit and the deliberate steps taken by the Bank of Canada to lean against inflation by moderating the growth of the money supply.

Over a period of many months, the crucial national need has been to gear down the rate of inflation without impeding economic recovery. To this end, over a year ago the government sought to develop a consensus, particularly with labour and business, in support of a program of voluntary restraint on prices and incomes. Unfortunately, as we all know, that effort was not successful. By last fall, in assessing both that experience and the dangers confronting our economy, we came to the conclusion that extraordinary steps would have to be taken to get us back on the course of full employment without inflation.

The anti-inflation program announced by the Prime Minister (Mr. Trudeau) on October 13 contained four closely-related elements—fiscal and monetary policy, government expenditure policy, structural policies and prices and incomes policy. I turn now to consider the evolution of policy on each of these strategic fronts.

[*Translation*]

Prices and Incomes Policy

The major new element in the Attack on Inflation was a set of guidelines for the setting of prices and incomes. All Canadians were asked to abide by them, and provision was made for mandatory control over the larger economic units within our economy. The essential purpose was to change expectations and to bring about a quicker response to the program as a whole, so that the fiscal, monetary and other general policies would in fact bring about real growth and declining inflation.

In the past seven months, the program has become fully operational and has begun to take effect.

The actual rate of inflation has slowed noticeably since the introduction of the program. In April of this year, the consumer price index was 8.9 per cent higher than a year previously, whereas in October last the year-over-year increase was 10.6 per cent. The seasonally adjusted CPI increased at an annual rate of 6.3 per cent from October to April of this year, whereas it had increased at an annual rate of 11.7 per cent in the preceding six months. This sharp reduction in the rate of price increase is very welcome.

A major factor has been an actual drop in the average price of food. Lower prices of some imported foods and the decline in livestock prices have resulted from market forces rather than the guidelines. The program has, however, ensured that these decreases in costs to the processing and distribution sectors were passed on to the consumer.

In the case of prices for goods and services other than food, there have been significant factors beyond the scope of the program tending to raise the rate of increase in recent months. These have included increases in retail sales taxes and other taxes, higher charges for public services and the rising costs of home ownership.

On the other hand, firms have been very cautious in raising prices in order to be certain that they are complying with the program. In a number of cases, firms have responded to requests by the Anti-Inflation Board to reduce proposed price increases. There has been a deceleration in those non-food prices that are subject to the controls.

With respect to wages and salaries under the program, I have tabled tonight a summary of preliminary data on compensation prepared by the Anti-Inflation Board. These figures show that compliance with the program is widespread. They demonstrate that even in the first six months of the program almost two-thirds of the wage proposals reported to the Board are within the arithmetic guidelines. Of the proposals only a small percentage are significantly above the guidelines and the Board is restraining them effectively. Thus, the record to date indicates that for all groups subject to the mandatory controls, average increases in compensation are only 1 per cent above the level provided for in the arithmetic guidelines. Given the significant improvement on the price side, these lower rates of compensation increase still represent sizeable real gains in income.

● (2030)

[*English*]

Mr. Speaker, the program is off to a reasonably good start. We feel a strong sense of responsibility to all those who have already contributed to the success of the program. They have every right to expect that others should be similarly restrained, and that the program should successfully bring the rate of inflation down to the target level.

Based on our experience to date, we have now come to the view that the regulations applying to prices and profits should be revised in order to achieve greater equity and effectiveness. Some firms are subject to insufficient restraint because in practice they have been able to choose which rules are favourable to them. Others are locked into very unfavourable starting positions and therefore have been subject to unreasonable restraints. The result is unfair treatment as between firms in competition with each other. Overall, this has created the danger that prices may be inadequately restrained in the future.

As a result of the detailed information supplied under the regulations, the Anti-Inflation Board has been able to complete an extensive analysis of the way in which the rules apply to the business community. The government has concluded that a number of important changes should be made. The details of the changes are described more fully in a supplementary paper, but I should like to summarize the highlights.

Let me begin by describing how the revised price and profit rules will apply to firms other than those in the distribution business. At present, not all firms are required to meet a profit margin test. Under the new rules, all firms will be required to do so. In justifying a price increase, they will be obliged to take into account not just increased costs, but the implication of the price increase on their profit position. Experience has now shown that a test based on profits has two advantages. First, it gives the Board a more effective regime to control prices. Second, it leaves everyone basically on the same set of rules and is therefore more equitable.

The new rules will be of particular assistance to many small firms which do not have sophisticated cost accounting systems.

Under the profits test, firms will not be able to set prices in a way which would increase their net pre-tax profits as a percentage of sales above an allowable level. That allowable level will be determined with reference to earnings in a base period. The base period margin is now the average margin in the five-year period ending prior to October 14, 1975. In order to provide a greater measure of fairness among firms, it is proposed that the base margin should be the greater of that calculated under the present rules and the margin earned by the firm in its fiscal year ending before May 1, 1976. For most firms this will be calendar 1975. At the same time, in order to ensure the over-all degree of restraint, it is necessary that the allowable margin be reduced from the present 95 per cent of the base margin to 85 per cent.

Firms will also be required to meet this margin test on each of their product lines as well as on their overall operations. Experience has shown that the product line test is the closest rule to actual business practice for most firms.

There will remain firms whose base margins are too low, whichever time period is chosen. In order to provide some relief for these firms, it is proposed that they be permitted to earn a minimum rate of return. The precise provision will be contained in draft regulations to be issued shortly. Similarly, at that time details will be provided relating to specific pricing and productivity rules.

Within this improved framework of rules, the Anti-Inflation Board will place greater emphasis on price justification. More firms will be required to notify the Board of proposed price increases and to justify them.

I have so far described the proposed revisions of the rules applying to non-distribution firms. The changes proposed for distribution firms are similar but less extensive. As now, they will be required to meet a net margin test on their whole business. In applying the net margin test, they will have the same choice of base period as other firms. However, because of this flexibility, they will be permitted to earn only 95 per cent of the base margin rather than 100 per cent as now. The gross margin test will be 100 per cent of their base year margins as now, but will be applied to product lines rather than on an over-all basis. Distribution firms with low base margins will also have access to the provision for a minimum rate of return.

Certain other changes in the regulations which affect the construction industry, trappers, fur farmers and the land development business are outlined in the supplementary information.

I also wish to announce certain changes in the rule referred to as the "restricted expenses" provision. This provision places a limit on the extent to which increases in certain expenses are allowed as costs. Political contributions will be added to the list of expenses subject to this restriction. On the other hand, charitable donations and approved expenditures for research and development will be removed from the list of restricted expenses.

It should be emphasized that the new rules represent a logical and evolutionary development of the present rules relating to prices and profits. They will ensure that the pricing behaviour of firms will be consistent with the general price targets which we have set for ourselves, without reliance on arbitrary powers of direction.

I have asked the Anti-Inflation Board to release as soon as possible a draft of the regulations incorporating all these changes. In order to ensure that the new rules will operate as smoothly and as effectively as possible, they will not become operative until July. Appropriate transitional provisions will be included in the new regulations.

There is one further aspect of the program which requires consideration. Out of a concern to ensure that all income increases were restrained, the rules have prohibited companies from increasing their dividends, except in special circumstances, for the first year of the program. Obviously, this freeze cannot be extended indefinitely. Hence, effective October 15, 1976 and thereafter until further notice, companies will be permitted to increase their annual dividends by 8 per cent.

Before I leave the subject of the prices and incomes policy, Mr. Speaker, let me pay tribute to all those in the private sector and in government who have worked so hard in this major national effort. We are particularly indebted to the Honourable Jean-Luc Pepin, Chairman of the Board, Mrs. Beryl Plumptre, Vice-Chairman, and other members of the Board and its staff, who have applied impressive skills and complete dedication to their tasks. Provincial ministers of all political parties and officials have given us both their support and valuable advice. I know that all involved feel sustained by the knowledge that the great majority of Canadians are solidly behind them.

Structural Policies

Beyond the introduction of a temporary program of controls, the White Paper of last October drew attention to the need for underlying structural adjustments in our economy. Such adjustments are essential if we are to win out against persistent inflation. In many ways, this is much the most difficult terrain of all. It raises fundamental problems of how to assure the most effective functioning of our mixed economy, and how to grapple with those social and institutional forces which make for continuous upward pressure on the general price level. These are the broad objectives which we must seek in looking forward to the removal of controls and in the post-controls period and beyond.

The government's work in this connection will be much advanced by the time of the opening of the next session of parliament, and we anticipate a wide-ranging public dialogue. In addition to the central focus of debate in parliament, the government is looking forward to meeting with all major groups in the community.

Mr. Clark: That will start next New Year's.

Mr. Macdonald (Rosedale): In that connection, preparations are already underway to meet the Canadian Labour Congress. The statement issued at the recent convention of the Congress makes clear its determination to press its views and interests in the formulation of social and economic policy in this country. The views and interests of all groups in our society must be heard. While government cannot abdicate its responsibilities, the growing complexity of our society requires that there should be every opportunity for consultation and the reconciliation of differing interests.

● (2040)

At this time, I propose to touch upon only those structural problems where immediate initiatives are being taken.

Energy Pricing

The first of these is in regard to energy prices—particularly oil and natural gas. The main message of the government's recent paper "Energy Strategy for Canada" is clear—energy is becoming more costly in the world and in Canada. The full impact of this trend on Canadians has been moderated thus far by our national policies for oil and gas. But Canada still has a long way to go in economizing in the use of energy and in developing new energy supplies.

The government has recognized the necessity of allowing prices of oil and gas to rise at a measured pace toward world levels. The need to encourage production and conservation and to ease the fiscal burden on the government points toward larger and faster increases of energy prices. But the need to slow down the rate of inflation, sustain output and employment and limit the immediate burdens on families of moderate means points toward smaller and slower increases. Regional considerations have to be balanced as well.

Having regard to all these considerations, my colleague, the Minister of Energy, Mines and Resources (Mr. Gillespie), has announced that the wellhead price of oil in Canada will increase by $1.05 per barrel on July 1, 1976 and by a further 70 cents on January 1, 1977. Natural gas prices will continue to be set on the basis of 85 per cent of the energy equivalent of oil. The price of natural gas delivered to Toronto will rise by 15.5 cents per mcf on July 1, 1976 and by a further 10 cents on January 1, 1977. There will be some delay before consumers feel the impact of each of these changes. I might note that the increase in revenues to the oil and gas producing provinces will result in higher equalization payments by the federal government to lower-income consuming provinces. Their increase over the 12 months beginning this July will be about $60 million.

I would like to emphasize the broad range of the policies followed by the government to encourage energy conservation and the development of new supplies. In order to discourage private use of gasoline and to help defray the cost of the import subsidy, a special federal excise tax was introduced last June. I will be announcing further new measures tonight to reinforce the energy conservation program developed by the energy minister. The government is strongly committed to active programs of oil and gas exploration and development through its participation in Panarctic, Syncrude, Petro-Canada and the Canada Development Corporation. The new northern oil and gas regulations are designed to speed up exploration and development. The income tax régime which we have evolved in recent years has provided major incentives for exploration. I would stress that for every dollar that the price of oil and gas goes up, the federal government will receive only three cents in income tax if producing firms make full use of the incentives for exploration. Further incentives are provided in this budget.

The Pricing of Government Services

A second important area for structural adjustment relates to the question of the pricing of government services.

The high rates of cost increase of recent years have led to rapidly growing deficits in the financing of many of these services. This has meant that only part of the costs have been covered by the users of the service, with the balance borne by the general taxpayer. In the absence of necessary adjustments in charges, the cost borne by the general taxpayer will continue to increase. This prospect of increasing deficits carries with it financial and economic implications which are particularly important over the longer term.

On the financial side, the growing cost to government can be met only through government borrowing or through increases in the level of general taxation. There are obvious limits to the extent to which the borrowing route can or should be followed. A further general tax increase may give rise to as much pressure on the general level of prices as an increase in specific charges. While careful attention has to be given to the objectives of the anti-inflation program, undue delay in needed price increases will simply enlarge the deficits and make it harder to pay our way in the future.

In economic terms, if prices charged do not adequately reflect real costs there will be a tendency towards inefficiency and waste in the use of the country's resources. Heavy subsidies erode the incentive for the development of more efficient ways of providing service. We must therefore encourage greater cost consciousness, not only in the provision of these services, but also in their use.

In recent months a number of provinces, confronted with large and growing deficits on particular services and in their over-all budgetary positions, have felt impelled to increase user charges. The federal government also faces rapidly growing deficits on a number of general and specialized services. Heavy transportation subsidies are being examined to ensure that they serve a social purpose without impeding the development of efficient systems.

In the case of the post office, my colleague the Postmaster General (Mr. Mackasey), last week announced necessary increases in postal rates. These increases have to be implemented in view of the rapidly accelerating deficit on Post Office operations, which has grown from less than $100 million in 1971 to an expected level of some $700 million this fiscal year in the absence of the rate adjustment. The proportion of costs borne by users of the Post Office has declined from 88 per cent in 1971 to less than 50 per cent this year. The effect of the rate changes will be to retard but not reverse the growth of the postal deficit. For the next fiscal year, the new postal rate structure will mean that the over-all deficit will be some $200 million less than it otherwise would be.

[*Translation*]

The Efficiency of the Economy

The productivity of the Canadian economy declined in both 1974 and 1975. While some decline is typical of a recession, this experience has raised concerns that the underlying growth of productivity—which is the basis for rising standards of living—may be slowing down.

Lest we jump to conclusions too quickly, we should recognize that there are particular problems of measuring productivity, especially in the service industries, which are becoming ever more important. But there can be no doubt of the importance of rising productivity and efficiency if we are to achieve our economic and social goals in the longer run. The government is giving urgent attention to the whole range of policies which can be brought to bear in fostering productivity.

Many measures have already been put in place to stimulate capital investment. I am thinking particularly of the manufacturing incentives, the investment tax credit introduced in the last budget and the various programs by which the government provides financing directly for energy development, transportation, small business, farming and fishing. These measures have helped to sustain high levels of business investment in Canada. However, the encouragement of business investment is only one part of a productivity policy which must be concerned with encouraging greater efficiency in the use of all factors of production.

A major objective in pressing ahead with the development of our competition policy is to promote efficiency. I will be announcing tonight a further extension of the tax concession to small Canadian businesses to enable them to grow and compete more effectively with large firms. Our negotiators at Geneva are pressing for the further liberalization of trade. This will provide more opportunities for Canadian industry and encourage it to improve its efficiency. The government will be ready to help.

[*English*]

One of the best ways to increase productivity is to encourage the development of high technology and innovative new processes. This is a high-risk business and it is difficult to attract venture capital into it. However, it is one which is of great potential for improving the growth rate of the economy.

The federal government already contributes to this process both through a variety of direct expenditure programs and through existing incentives in the tax system. Nevertheless, it has been proposed that more assistance is needed and that the best way to provide this encouragement is through additional tax incentives. It is argued that this catalyst is needed to bring together pools of venture capital and Canadians with new and innovative ideas.

● (2050)

I am sympathetic with these objectives and am willing to explore avenues to achieve them. However, I am not satisfied that we have yet found an efficient and workable solution to what is commonly referred to as the venture capital problem. Clearly, what is needed is a tax regime which will help do the job effectively but efficiently.

I have already instructed my officials to study this matter on a priority basis. I intend to consult with the provinces to gain the benefit of their thinking and work in this area. I am also anxious to hear from people who are interested in and knowledgeable about this issue and I invite Canadians to write in their proposals. If we can find the right answers, we will be quick to act.

Finally, to refer to another important part of the financial system, the government's proposals on the decennial revision of the Bank Act will be brought to the House later in the year. This will afford us an occasion for broad consideration of the task of financing the Canadian economy.

Employment and the Labour Force

We have of course a special interest in improving the functioning of the labour market in Canada. The Economic Council's recent study, entitled "People and Jobs", provides valuable insights into the structural problems of employment and unemployment in Canada. It analyzes the flows of people into and out of the labour force, from job to job and between unemployment and employment. This analysis documents the tremendous size and complexity of labour market change which takes place in Canada each year. Structural and frictional unemployment, which arises in this process of change, has increased substantially in Canada during the last decade. It reflects both institutional changes and the increased participation of youth and women in the work force. Better information on job opportunities, improved training and creation of the right kind of jobs are important means of reducing structural and frictional unemployment. The Council's study recognizes that manpower and direct employment policies and the unemployment insurance program have all made useful contributions toward dealing with these problems. It concludes, however, that all of them can and should be improved.

Unemployment arises not only from structural change but also from fluctuations in economic growth. The primary means of reducing unemployment due to periods of slow growth lies in the maintenance of adequate over-all demand. However, the experience of many countries in recent years underlines the danger of setting targets for unemployment too low or trying to reach them too quickly. If we are to sustain economic growth and job creation while simultaneously bringing down the rate of inflation, demand management policies and policies to improve the functioning of the labour market must go hand in hand.

Canada has been a leader in the recent development of direct employment programs. These programs have created jobs to alleviate the most severe problems of seasonal and regional unemployment. They have assisted those groups which are most likely to be without work for periods of time. We believe we have demonstrated that these jobs can have broad social value and are not simply "make-work". We continue to believe that there is a need for such selective programs of job creation if we are to be able to bring the rate of unemployment down without generating new inflationary pressure. They have to be adapted to the changing structure of the labour market, and to the need to obtain the maximum impact from the limited resources which can be made available within the framework of expenditure control.

Last year's budget speech noted that the continuing review of the unemployment insurance legislation had identified a need to strengthen certain aspects of this program. To meet these needs, a number of changes were incorporated in Bill C-69, which has now become law. During the debate on this bill, it was noted that further changes to the Unemployment Insurance Act would be brought forward as the review progressed. As a result of this review, my colleague, the Minister of Manpower and Immigration (Mr. Andras), will introduce legislation proposing a number of significant initiatives. These changes are designed to make the unemployment insurance system more equitable and dynamic, more responsive to regional unemployment conditions, and less costly. They are also designed to encourage those with jobs to stay with them and those who are unemployed to seek suitable jobs.

Three main changes will be introduced relating to unemployment insurance benefits:

First, the present requirement for eight weeks of insured employment to qualify for benefits will be increased to 12 weeks. This amendment is intended to reflect the changes which have taken place in the Canadian labour market in recent years. These include the increase in the number of people who have only a marginal attachment to the labour force and who thus have less of a claim for the protection of unemployment insurance.

Second, the number of weeks during which benefits may be drawn will be more directly related to the number of weeks worked. In addition, regional extended benefits will be related in a more sensitive manner to the level of regional unemployment.

Third, severance pay will be treated as savings and as such will not affect a person's eligibility for unemployment insurance benefits.

The act will also be amended to permit the payment of unemployment insurance to beneficiaries on a discretionary basis where they take part in such activities as selective employment, training or short-time work programs. My colleague will elaborate on this new concept of adding an important thrust to the over-all insurance system.

The Minister will also elaborate proposals to integrate the administration of the unemployment insurance system with the programs and services of the Department of Manpower and Immigration. We believe the time is ripe to have a common organizational setting in order to promote even greater effectiveness in administration and to enhance the quality of employment services to Canadian workers.

[*Translation*]

Federal-Provincial Fiscal Relations

Finally, Mr. Speaker, a basic structural element in this country is the financial relationship between the federal and provincial governments. We are engaged at present with the provinces in discussion of the Federal-Provincial Fiscal Arrangements Act and shared-cost programs.

My views on the fiscal arrangements that should apply in the post-1977 period are on record. They were discussed with my provincial counterparts at the April 1 meeting, and tabled in the House on the same day. Thus I can simply note the way in which our position fits in with our overall policy.

I want to preserve the principle that the federal and provincial governments should be free, in their taxing and spending activities, to discharge their respective constitutional responsibilities. On the revenue side this means access to sufficient fiscal resources. There is, of course, a need for a great co-operative effort if we are to maintain a uniform national tax system. But fiscal freedom and responsibility are also essential for the control of expenditures and the efficient provision of public services.

Equalization payments must be retained as a continuing and central feature of the ongoing system of fiscal arrangements. We are committed to this. Our objective is to help the less affluent provinces provide reasonable levels of service. But equalization and other transfers to provinces impose a heavy burden on Canadian taxpayers generally. Costs must be kept within acceptable bounds and the ability of the federal government to finance the program through its own revenue sources must be protected.

Over the past 10 to 15 years, shared-cost programs have been a major instrument in the development of a high level of public services across the entire country. In such fields as health care, social welfare and post-secondary education, Canadian citizens have benefitted greatly from these programs. However, as some of these programs have matured, the financing and administrative arrangements built into them have not left enough room for improvements and efficiencies. As a result, costs threaten to outrun the financial capacities of both the federal and provincial governments. For the federal government, these open-ended cost-sharing arrangements have raised many problems in the allocation of limited funds for national needs and priorities. A better method of providing these essential services to the Canadian people needs to be found and, to this end, discussions have been held between the federal government and the provinces. They will continue as a matter of high priority.

● (2100)

[*English*]

Government Expenditure Policy

I come now to the third principal element of the anti-inflation program—the limitation of the growth of government expenditure and of public service employment.

In recognition of the widespread feeling among Canadians that present circumstances demand restraint in government spending, the government has stated that the "trend in total spending by all governments in Canada should not rise more quickly than the trend in gross national product." Two aspects of this objective should be stressed.

First, it is not put forward as a short-term goal: a brief slowdown in the rate of expenditure growth to be followed by a resumption of excessive growth. Rather, it is put forward as a basic change in the trend of expenditure increase. This guideline is stated in terms of trends in view of the stabilizing role which actual government expenditure should play as the GNP grows more quickly or more slowly than its trend in any particular year. In a period of slow growth, it may be appropriate for government expenditure to rise more rapidly than GNP. In a period of strong economic expansion government expenditures should grow more slowly than GNP.

The Budget—Hon. Donald S. Macdonald

Second, the objective does not imply an indiscriminate slashing of programs. Such an approach would have disruptive effects on the economy, bear harshly on many people and impair the efficiency of government in providing essential services to the public.

Our objective, then, is to achieve a major shift in the pace of growth of the government sector, in a deliberate, sustained fashion. This lay behind the cuts in planned expenditures for the 1975-76 fiscal year announced in the last budget, and the cuts in planned expenditures for this fiscal year announced by my colleague, the President of the Treasury Board (Mr. Chrétien), on December 18. It was made clear on both occasions that unavoidable cost escalation in a number of programs had made such action necessary. We have recognized the need for action not just in the government's own manpower and operating expenses but also in major program areas. Some grant programs have been eliminated completely and strict ceilings have been imposed on many others. Measures have been taken to reduce the cost of unemployment insurance to the taxpayer. Ceilings have been placed on the growth in the federal contribution under certain federal-provincial shared-cost programs. Government financing of Crown corporations has been curtailed and in this regard, we have decided upon a further deferral of the proposed Federal Mortgage Exchange Corporation.

To achieve our expenditure control objectives, the introduction of new programs must be kept within careful limits and the resources required for the continued operation of existing programs must be minimized. A number of recent developments should help us achieve this goal and help parliament and the public monitor progress. One of the few areas in which provision has recently been made for a significant increase in staff is in the Office of the Auditor General. I trust the expanded capacity of this office will encourage the efficient use of resources by departments. In a report tabled last year, the Auditor General expressed concern over the adequacy of certain aspects of the government's system of financial management. The government is responding to these recommendations by establishing a separate branch of the Treasury Board secretariat responsible for all aspects of financial management. Additional changes have been made which will strengthen the effectiveness of the Treasury Board through centralizing responsibility for control of outlays in its hands. The Treasury Board itself is reviewing all proposals for increased expenditure before they are approved by cabinet.

In our expenditure planning, we have focused on total outlays, including both budgetary expenditures and loans, investments and advances. Total outlays increased by 28 per cent in 1974-75 and 18 per cent in 1975-76. I should note that the preliminary estimates of total outlays for 1975-76 are somewhat higher than the President of the Treasury Board and I expected earlier this year. A major contributing factor was a decision to permit our enterprises engaged in energy and export development to obtain financing from us somewhat earlier than had been anticipated. While this has increased the growth rate of expenditures in 1975-76, it has helped to reduce it in 1976-77. Based upon planned total outlays of $42,150 million, our target rate of increase for this fiscal year works out at about 14 per cent. Our forward planning for 1977-78 is based on a growth rate of the order of 11 per cent. For both 1976-77 and 1977-78, these increases are less than the expected growth of the GNP.

[Mr. Macdonald (Rosedale).]

I wish to remind the House that my colleague, the President of the Treasury Board, is holding the increase in the public service to 1.5 per cent this fiscal year. This is substantially below the growth rates of earlier years. Given the need to add significant numbers of policemen, prison guards and postmen to the payroll and the need to maintain other essential protective and regulatory services in a growing economy, the strict manpower ceiling is requiring most departments to freeze or actually reduce the number of employees in less essential services.

It is a fact of life that the scope for expenditure control increases as one looks further into the future. It proved very difficult to cut back on our expenditures in 1975-76 once the year was already underway. We have been able to get on track for 1976-77. We hope to consolidate our gains in 1977-78. We believe we have put in place the planning and control systems which will ensure that these targets are met.

Fiscal and Monetary Policy

Finally, the anti-inflation program requires that fiscal and monetary policy be aimed at increasing total demand and production only at a rate consistent with declining inflation. In the White Paper of October 14 I stated that "the success of the government's whole program for achieving a progressive lowering of the rate of inflation, together with a sustained recovery of the growth output and employment, will depend crucially on its success in keeping the over-all level of demand in the economy growing at a pace consistent with successively lower rates of price increase."

The monetary policy of the Bank of Canada has been set out by the governor in his 1975 Annual Report and in recent speeches. It carries my full support. Last autumn the Bank announced an initial target for the growth of the narrowly-defined money supply in the range from 10 to less than 15 per cent and the rate of increase since the second quarter of 1975 is now at the lower end of the range. The Bank has indicated that its target range, which allows for the continued real growth of the economy, will have to be lowered over time so that the rate of monetary expansion will be consistent with the price-level objectives of the prices and incomes policy.

This monetary policy, in its refusal to underwrite continuing high rates of inflation, is helping to destroy expectations that they will continue. It requires that we should expect variations in interest rates and the exchange rate. While we would all like to see lower interest rates, the way to bring them about is to reduce inflation. In the most recent years, the level of interest rates has not been high enough to maintain the real value of the money which Canadians have deposited in banks or invested in Canada Savings Bonds or other financial assets. The strengthening of the exchange value of the Canadian dollar, due in no small measure to high domestic interest rates, has increased the challenge faced by Canadian firms competing in world markets. At the same time, it has lowered the cost of the goods and services we buy from other countries and has thereby contributed directly to the success of the anti-inflation program.