practically neglected. Once again in terms of war economy this distribution may be, indeed probably is, justified. But the policy means that this war is seeing a great industrialisation of Canada and that this industrialisation is being concentrated in the provinces of Quebec and Ontario, with the consequence of greatly increasing their economic power and consequently their political influence within Confederation. It also means that Canada's external trade policy will be effected. The central provinces will not only wish to have protection against manufactured imports, they will be looking for markets for their exportable surpluses of manufactured goods and if, as one may expect, Canada becomes a creditor rather than a debtor nation the problems of marketing agricultural produce abroad and the problem of selecting the type of import in which we will permit our debtors to make payment will become exceedingly difficult and will breed conflict between the different economic regions. To some small extent these problems have been foreseen and provided against by the Dominion government. Whereas the total spending by way of capital assistance to industry has been highly concentrated in Quebec and Ontario, the spending per capita has been rather more equitable, though here the industrial provinces of Ontario and Quebec and to a lesser extent British Columbia have done better than the Prairies and Maritime provinces, and the spending per $1000 invested in manufacturing industry and per employee engaged in manufacturing industry, i.e. the increase in the degree of industrialisation, has been highest in the Prairies with Quebec running second, Ontario third, the Maritimes fourth and British Columbia fifth. Thus an effort has been made to spread the industrialisation and, particularly, to increase the degree of industrialisation in the Prairie provinces. This has been done, the figures suggest, at the expense of the already industrialised province of British Columbia rather than of Ontario and Quebec. But it does offer to the Prairies a slight improvement in the balance of their economy and some little safeguard against the possibility of restricted agricultural markets after the war. The degree of industrialisation in the Maritimes remains very small. Already less industrialised than British Columbia their industrialisation has been increased but little, and in actual fact what capital assistance to industry there has been, has been concentrated in a single community and in a single industry with little post war possibilities. This does rather suggest a further decline after the war in the relative economic position of the Maritimes, with respect to the rest of Canada, and consequently in their influence in the councils of the nation.

Economic Relations Between Canada and the United States

By J. Douglas Gibson

FEW developments in our economic relations with the United States can match in importance the so-called Hyde Park Agreement reached between President Roosevelt and Prime Minister King on April 20th last. It establishes the principle of co-ordination between the production efforts of the two countries: "Each country should provide the other with the defence articles which it is best able to produce, and above all, produce quickly, and production programs should be co-ordinated to this end." It also is designed to combat Canada's number one bottleneck—the foreign exchange pro-

EDITOR'S NOTE: J. D. Gibson is Editor of the *Monthly Review* of the Bank of Nova Scotia published at Toronto. The map on the cover of this issue was obtained through the courtesy of the American Association for Adult Education and was previously published in the Association's *Defence Papers No. 3*.

blem—and in this respect it makes a very substantial contribution indeed.

This economic agreement may be regarded as a logical development of the earlier defence pact (the Ogdensburg Agreement) and of the emergence of the United States' aid-to-Britain policy. Obviously, it will facilitate North American defence. Even more important, it will facilitate aid to Britain which, on both sides of the border, is now regarded as the first line of defence. While it may be doubted that it will weld the production programs of the two countries into a single gigantic whole, as some commentators have suggested, it will increase the effectiveness of the effort on both sides of the international border, and especially on the Canadian side. From a Canadian standpoint, it should add very substantially to our ability to increase our war effort, both because it will assist us to enlarge our purchases of essential materials and equipment and because it envisages a greater degree of specialization in our war production.

The Hyde Park Declaration has also longer-range implications. It is a further phase in that mixing-up of the affairs of the British Commonwealth and the United States which we may not want to unravel, or be able to unravel, when the war is over. It may be remembered that Premier King said of the Odgensburg Agreement, "it is part of the enduring foundation of a new world order, based on friendship and good will," and the present agreement is after all but an extension of the same basic principle. In the space of this article, however, it is not feasible to discuss such longer-range prospects, important as they are. Rather, it will be attempted to give a brief sketch of the development of economic relations between Canada and the United States which the war has brought about, presented from the Canadian angle, and with emphasis on the balance of payments and the exchange problem.

Pre-War Trading Relationships

Before turning to wartime developments, it may be well to outline the position which prevailed before the outbreak of hostilities. It is scarcely necessary to say that close economic ties existed between Canada and the United States. Indeed, the two countries did more business with each other than any other two countries, and well over 50% of Canada's international transactions were with her southern neighbour. This huge volume of business was about half in commodities and the remainder was in gold, tourist trade, interest and dividends, freight and minor items.

In commodity trade, Canada's principal exports to the United States were forest products (particularly pulp and paper), base metals and asbestos, certain farm products, fish and furs. The volume of these exports is closely related to the state of business conditions in the United States—and more specifically to such things as newspaper advertising and circulation, building activity and operations in heavy industry. Canada's commodity imports from the United States comprised a much wider variety of products. Some are basic raw materials and fuels, such as iron ore, raw cotton, petroleum and coal. Others are machinery, metal products, and parts for manufactured articles. And yet others are consumers' goods, some of which are of a luxury and semi-luxury character. The volume of these imports, of course, varies with the condition of Canadian business, but because of our great dependence on the United States for capital goods and equipment the volume becomes extraordinarily large in periods of capital expansion and, conversely, is much lower at other times. The commodity trade balance between the two countries is almost invariably against Canada. In 1938, the last full year before the war, the deficit on commodity account, including the related freight payments, was about $150 millions.

In addition to this net payment, Canada has also very large payments to make on the huge American investments within her borders. The U.S. investment in Canada is placed at not far from $4,000 millions, and though an appreciable part of this represents holdings of government securities, what is particularly notable is the large interest in manufacturing, mining and public utilities. This American investment required a remittance of interest and dividends of about $225 millions in 1938, of which only about $25 millions was offset by receipts from Canadian investments in the United States.

On the other hand, Canada made up for a good part of these payments with her receipts from gold production and from the tourist trade. The steady increase in gold output, which by 1938 was around $165 millions, has been a very important factor in meeting external payments and in enhancing our ability to purchase necessary imports. The tourist trade was also an important source of foreign exchange, though in the light of recent investigations it did not bulk so large as we used to think. On the basis of the new estimates it would appear that the net credit, i.e., the differences between receipts and payments for tourist services, was somewhere in the neighbourhood of $80 millions in the year prior to the war.

Taking all these transactions together and adding in the few smaller items, the current business between Canada and the United States resulted in a net debit for Canada of around $115 millions during 1938. But this was not an unhealthy state of affairs: it did not mean that Canada was going further into debt. Indeed, quite the reverse was true. So substantial was the credit balance with the British Empire and foreign countries that we were able to meet our deficit with the United States and in addition to redeem and buy back sizeable amounts of our previously-incurred debts in that country.

The Effect of the War

The war caused two fundamental changes which radically altered this picture. It greatly increased Canada's requirements of American goods and thus rapidly enlarged the deficiency in her accounts with the United States. And at the same time, it meant that her large and growing credit balance with the British Empire could no longer be freely converted into foreign exchange. These were the main factors which resulted in the "hard currency" problem.

Let us look first at the wartime development of Canada's trade with the United States. From 1938 to 1940, imports from the United States rose from $425 millions to $744 millions. About two-thirds of this increase was in imports of metals, metal products, machinery and aircraft and parts. A good deal of the remainder was in raw cotton, coal and petroleum. The reasons are not far to seek. Canada was in process of building up a large war industry and required machinery, equipment and steel in quantities and of a kind which were far beyond her capacity to produce. Furthermore, many of the new wartime products required parts and components which could not readily or effectively be made in Canada, and the rising volume of production necessitated a larger import of basic raw materials and fuels. At the same time there was a growing demand for consumers' goods, though this was checked as time went on by taxation and import barriers. And then, it should also be remembered that some sources of imports had been cut off by the blockade or made less accessible owing to the shipping problem.

In some respects, an analogy could be drawn between the present situation and that which prevailed in the late 'twenties. Now, as then, Canada is in a period of rapid capital expansion requiring extremely heavy imports from the United States, though the purpose and direction of the expansion is, of course, not the same. Canada, whose methods of manufacturing and production are North American, necessarily turns to the United States not only for capital equipment but also for technique and methods of industrial organization. But the analogy ends here. In the late 'twenties, much of the expansion was being financed by an inflow of capital from across the border. To-day, in contrast, the expansion is being financed at home, and largely by government rather than private capital. American investment has played little part: indeed, at the outbreak of war the risk of a withdrawal of previously-invested capital seemed a quite sufficient reason for the imposition of exchange control.

Of course, the expansion of trade has not been entirely in one direction. Canadian exports to the United States have risen appreciably, though to a much smaller degree than imports from that country. Rising business activity in the United States and the closing-off of certain European sources of supply (particularly for wood products) created a larger market for Canadian goods, especially for pulp and paper and base metals and to a lesser extent for lumber, asbestos, certain farm products, fish and furs.

The war also affected other types of business with the United States. It had an unfortunate influence on the tourist trade: expenditures of American tourists in Canada were about 20% lower in 1940 than in 1939. Through its effects on industrial activity, it also added somewhat to dividend payments on American investments in Canada, though higher taxation limited such increases. But the market for gold was not affected, and this source of U.S. dollars increased with the gradual growth of production.

To sum up, the effects of war have been to enlarge greatly our U.S. dollar deficit. Even after certain government measures were taken to check unnecessary demands for U.S. dollars, it would appear that our net deficiency in 1940 was somewhere around $300 millions as compared with somewhat over $100 millions in 1938.

As already indicated, we were no longer free to draw upon our credit balance with the British Empire. Although this balance has been growing rapidly, Britain had urgent need of her resources of gold and foreign exchange and the policy has been to help to finance her Canadian dollar requirements by repatriating Canadian securities formerly held in Britain, and by accumulating sterling balances. From the beginning of the war, until March 31st, last, i.e., in a period of about 18 months, our credit balance with Britain is officially estimated at $795 millions, and of this Canada financed $545 millions by these two methods. The remainder was received in gold, but it is clear that all such gold, and more, was required to meet Canada's deficit with the United States. In fact, we have drawn on our capital resources of monetary gold and foreign exchange to a material degree.

Exchange Control and Restrictions

Even at the outbreak of war, it was clear that there would be a dollar-payment problem, and exchange control was established almost immediately. Exchange control, however, was not set up to curtail imports or other forms of current trade. Its purpose was to guard against the risk of an outflow of capital which might have greatly accentuated our exchange problem, and also to provide a stable rate of exchange both in relation to the U.S. dollar and to the controlled rate of sterling. Partly because of our very close financial ties with the United States there were a number of ways in which such a capital outflow could have occurred. For one thing, there was a very large trade in securities between the two countries. Many Canadian securities have a well-developed market on both sides of the border and should the New York market for such securities have weakened, American holders would have had the alternative of selling in Canadian markets and withdrawing their funds. Furthermore, Canadians were substantial investors and traders in the New York market and, until exchange control was imposed, were at liberty to move funds into the United States without let or hindrance. In addition, Canadian corporations and governments had been buying back their securities held in the United States during the several years preceding the war. Also important in possible losses of capital were numerous and indirect methods by which American parent companies could reduce their investment in their Canadian subsidiaries. While a large outflow of capital might not have occurred, it was a risk which could not reasonably be taken in view of the great need for U.S. dollars to make current purchases.

As Canada's war effort expanded and as imports from the United States increased rapidly, certain other measures were taken to conserve foreign exchange. In the second war budget of June, 1940, the 10% tax on non-Empire imports was imposed both with a view to revenue and to discouraging unnecessary imports requiring "hard currency" exchange. In addition, the heavily graduated tax on the sale of new automobiles had an exchange motive in that it bore most heavily on the more expensive imported vehicles. Later on, came the Exchange Conservation Act and the ban on pleasure travel outside the sterling area. The Exchange Conservation Act prohibited the import from "hard currency" countries of a variety of non-essential products, including most household appliances (refrigerators, stoves, washing machines, light fixtures, radios, etc.), many textiles and a variety of consumers' goods. It also subjected the imports of certain other goods to increasing restriction. At the same time, however, excise taxes of 25% were placed on the sale in Canada of most household appliances with the specific intention of discouraging any increase in their domestic production. Though the present budget features no major provisions for exchange conservation, there is an element of this in the federal gasoline tax, and the increase in the tax on the income of non-residents from 5% to 15% may result in an appreciable exchange saving.

The Present Position and the Hyde Park Agreement

That measures to conserve exchange were necessary is conclusively shown by the persistence of a very large U.S. dollar deficit. In the recent budget speech, the Minister of Finance stated that despite the measures which were adopted, Canada experienced a net deficit in all her transactions with the United States from September 15th, 1939, to March 31st, 1941, of $477 millions. Of this deficit, $250 millions was met by gold received from Great Britain, but the remainder of around $225 millions was met out of Canada's holdings of monetary gold and exchange, and by the liquidation of certain other U.S. assets. Moreover, the deficiency was growing: according to the Minister, in the present fiscal year (which began on April 1st) it would be around $478 millions—as much as in the preceding eighteen months.

This was the problem at the time of the Hyde Park Agreement. Towards its solution, that agreement made a very substantial contribution. In the first place, the United States agreed to relieve Canada's exchange problem insofar as her purchases from the United States are components for munitions and equipment which are being manufactured in Canada for Britain. In future, such purchases are to be included under Lease-Lend to Britain. This will mean a very substantial saving in exchange: no official estimates have appeared, but unofficial "guesses" go as high as $200 millions per annum. In the second place, the United States undertakes to purchase defence articles from Canada to an amount which it is hoped can be between $200 millions and $300 millions in the next twelve months.

While these steps go a long way to meet Canada's exchange problem, it would be unwise to assume that they offer a complete solution. The principles are agreed upon but the difficult technical details have still to be worked out. The export of $200 millions to $300 millions of defence articles from Canada to the United States is a "hope," not a contract, and even when this volume is reached there will not necessarily be a fully equivalent improvement in the exchange position. Indeed, the very fact that the Agreement relieves the exchange problem means that Canada may be able to increase her war effort and import even more from the United States. In the words of the Minister of Finance, the Agreement "does not remove all need for the conservation of foreign exchange. It is a magnificent contribution to the success of our common struggle, not to the ease and convenience of the Canadian people. It would be foolish, for instance, to assume that it will mean the restoration to par of the Canadian dollar in New York . . . or to assume that it will enable us to remove the present restriction upon the use of U.S. dollars for pleasure travel purposes in the United States."

Some Broader Implications of the Agreement

Because it will ease the vital exchange bottleneck and because it is designed to induce a greater degree of specialization in the output of defence articles, the Agreement should notably facilitate Canada's war production. "It means," said Premier King recently, "that in the case of corvettes and other weapons of war, Canadian plants will be able to go full-out and make to their capacity. One advantage in the case of planes is that makers of the chassis can go ahead as fast as they can knowing the engines will always be available from the United States."

But what about these proposed exports of defence articles to the United States? What are they to be, and shall we have enough of them to ship to the United States after meeting our own and British requirements? While the answers to these questions are not yet known, some rather vague indications have been given. In the text of the statement following the meeting between President Roosevelt and Premier King, it was suggested that the defence articles concerned might be "certain kinds of munitions, strategic materials, aluminum, and ships." In regard to all these items, the requirements of Great Britain are heavy and undoubtedly have first call. The situation probably boils down to something like this. In the first place, we can ship to the United States such defence articles as we can produce in sufficient volume after meeting our own and Britain's needs. It would appear that the immediate possibilities in this direction are fairly limited. Secondly, and of greater importance, we can ship products that Britain needs to the United States, provided that the United States can proportionately or more than proportionately increase her aid to Britain. For example, it is conceivable that shipments of aluminum to the United States might be made at the expense of British and Canadian requirements if it were clear that such aluminum could be used more effectively by that part of the American aircraft industry which is working for Britain. Similarly, we could ship corvettes to the United States Navy for patrol work on the North Atlantic shipping lanes; and if, by receiving corvettes, the United States felt able to turn over some more destroyers to Britain the advantages would be obvious. In other words, it is a three-cornered proposition and the criterion is the largest possible joint effort, with emphasis on the first line of defence.

The principle of co-ordination between the productive efforts of the two countries was strongly stressed at the Hyde Park meeting, though no specific indications were given of the form which co-ordination was to take. Judging from recent developments, it appears that Canada is to concentrate her effort even more on shipbuilding, both of merchant vessels and of smaller naval craft, on munitions and explosives, on certain kinds of armaments and on such vital materials as aluminum. It would also appear that we have dropped the idea of making high-powered aircraft engines. But this is about all that can be said at the moment.

The announcement at the time of the Agreement concludes: "the technical and financial details will be worked out as soon as possible in accordance with the general principles . . ." It is quite clear that these details are very important. In addition to the financial aspects, they include all the practical problems of co-ordination—the degree of concentration on certain kinds of output, the assurance of an adequate supply of machinery and materials, questions arising out of the difference in type between British and United States military equipment, and out of the difference in specifications between North American and British industry, and so on.

Such problems require almost continuous consultation and study. Some machinery for this purpose is already in existence. There is the Joint Defence Board which is concerned with the military aspects of Canadian-American defence. There is also the recently-established Material Co-ordinating Committee which includes representatives from the Canadian Department of Munitions and Supply and from the U.S. Office of Production Management and whose purpose it is to collect and exchange information on raw material supplies in the two countries. Now, it is unofficially reported from Washington that Canada and the United States may set up closely collaborating economic defence boards in the near future. Such co-operation and consultation must play a major part in translating the broad principles of the Agreement into effective co-ordination of defence production between the two countries.

Regional Aspects of Government in the United States

By John M. Gaus

THE Report of the Royal Commission on Dominion-Provincial Relations is evidence to its readers in the United States of the important similarities in our problems. Such a measure as the Prairie Farm Rehabilitation Act reminds us also that there are parallels between us not only in our physical regions but the resultant problems of adjustment of man to his environment and the institutional devices which may be employed in that adjustment. We on the south of the border may usefully study Canadian policies and proposals. They will not only have much that bears directly on our own problems, but in looking at these problems through the eyes of others we can reappraise them freshly and more objectively. By pooling our practices and ideas we may find mutual advantages. A brief summary, therefore, of developments in the governmental reflection of regional factors in the United States and a reference to some of the centers of work in this field may have some interest for Canadian students.

What do we mean by a "regional" aspect of government in the United States? The problem of adjusting areal boundaries to the nature and scope of the functions and powers of government has been present throughout our history. Our system of government is federal, our area is continent wide, our economy is affected by international and national factors within the sensitive interdependent price system. Through our constitution, the powers with which the people of the United States may attack public problems are allocated to the national government and to the states, and in that same instrument prohibitions are placed on both—prohibitions that are substantive and procedural. The original arrangements have been amended by formal change in the document and modified by judicial interpretation and legislative and executive practice as changes in technology, in institutions, in the distribution of population and in attitudes of mind have dictated or permitted. Nevertheless there cannot, apparently, ever be achieved a perfect fitting of gov-

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