

OTHER ARTICLES

The Economic Outlook for Canada

By BENJAMIN HIGGINS

WHENEVER I am asked to indulge in economic forecasting, I am reminded of the Talmudic dispute regarding the relative importance of the sun and the moon. The controversy was resolved in favor of the moon because, it was pointed out, the moon shines in the dark.

Economics is a bit like the moon. It is a pale reflection of the pure, clear light of science; but it is all the more important and useful because of the black obscurity that surrounds questions of economic diagnosis, prognosis and prescription. The number of uncontrollable variables in the economic system is far too big for anyone to make economic forecasts with complete accuracy.

The situation of the economist is very much like that of the medical doctor. Both the doctor of medicine and the doctor of economics use a *scientific approach* to their problem, and base their recommendations on as complete and objective an analysis as possible. Both are handicapped by the small number of identical cases that are available for comparison, and by their inability to perform controlled experiments. Both are in the unfortunate position of dealing with human beings, who feel quite free to make their own prescriptions for minor ailments, but who are all too ready to blame the doctor when things go seriously wrong. And both the doctor of medicine

and the doctor of economics can give far better advice than the patients themselves.

One can scarcely blame the doctor for bad forecasting if he tells the patient he will be better soon but had better stay in bed and the patient, ignoring his advice, goes to a party and dies of pneumonia. Nor can one blame the economist if his forecasts go wrong, when the policy recommendations on which the forecasts are based are completely ignored. In short, one has a right to expect from the economist a prognosis no less and no more accurate than that of a physician dealing with an extremely complex disease, and whose patients sometimes find his prescriptions unpalatable.

The Pattern of Postwar Economic Fluctuations

In the past, postwar economic fluctuations seem to have followed a common pattern: (1) several months of hesitation and uncertainty, with desperate movements of prices, production, and employment in individual industries, adding up to mild recession in the economy as a whole; (2) primary postwar boom lasting one to three years, sometimes with inflation more violent than during the war itself; (3) primary postwar depression, usually short but sharp, dominated by deflation of prices; (4) secondary postwar prosperity of several years' duration; (5) secondary postwar depression, usually deep and prolonged. Since World War II the Canadian economy has

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followed this typical pattern, with somewhat less amplitude of fluctuations than took place in Canada after World War I, or in other countries after earlier wars. At the moment, we are still in the primary postwar prosperity phase, but an increasing number of people are beginning to wonder how much longer this phase will last. Must we continue to follow the pattern, and suffer a primary depression of the 1921-22 type in the very near future, and a secondary depression of the 1929-39 type later on?

A complete analysis of the determinants of income and employment cannot be given in short compass. Suffice it to say that the level of income and employment depends on the volume of total spending for goods and services; and that this volume of total spending can be broken down into a small number of strategic categories: private expenditures of consumers on home-produced goods and services (consumption); privately-financed expenditures of foreigners on home-produced goods and services (exports); and government purchases of goods and services (public spending).

The volume of public spending obviously depends on governmental policy. In the past, public spending has unhappily tended to vary in the same direction as income and employment as a whole thus aggravating economic fluctuations. It is to be hoped that in the future the stated policy of varying public spending counter-cyclically, so as to counteract fluctuations in private spending, will be carried out.

Consumption depends almost entirely on the level of income at the disposal of consumers. The variations in the ratio of consumption to income are small, and consumption does not stray or stay far from the "normal" relationship to disposable income. Just now, consumers are spending a slightly "super-normal" proportion of their incomes, because of the piled-up demand that developed during the war; but consumption can be expected to revert to a "normal" relationship to income in the future.

The volume of exports depends mainly on the level of foreign incomes, but also depends partly on governmental policy. The American Marshall Plan and our own Exports Credits Insurance Corporation are examples of government operations that tend to raise the level of exports.

Private investment is the most dynamic and volatile element in national income. In the past, fluctuations in income and employment have been associated mainly with variations in investment, and the repercussions of these variations on other kinds of spending. By the same token, private investment is the most unpredictable of the major components of national income. At the same time, it is not difficult to isolate analytically and statistically, the major factors that determine the level of private investment. They are: the level of profits in the most recent accounting period; expectations regarding future profits; and the stock of accumulated capital, including plant, equipment, housing and inventories.

It seems safe to say that so far as internal forces are concerned, there is little reason for early recession in Canada. Profits are still at extremely high levels. Indeed, profits net of taxes are at an all-time high. Profit *expectations*, of course, cannot be measured directly; one must rely on questionnaires, and expectations of business men can change faster than questionnaires can be distributed and analyzed. However, profit expectations, as indicated by questionnaires, are still favorable and there is no obvious reason why they should change. The stock of capital is accumulating rapidly and this in itself is an unfavorable factor; but the stock of plant and equipment is still subnormal in many industries and inventories as a whole are not excessive as to sales. The situation in housing is more complex. There are in Canada about one-quarter of a million families who could afford houses at the prices at which they are being offered, and some 200 thousand houses have already been completed since the war; obviously, an

early decline in the volume of private housing must be anticipated unless some means is found of tapping the huge housing market represented by middle and lower income groups. However, the housing boom may well last through 1948.

As for exports, devastated Europe and the underdeveloped areas of the East and Latin America are still eager to buy Canadian exports in large quantities, so long as they can find dollars; and it is likely that policy in the United States and Canada will be such as to provide dollars in substantial quantities.

Finally, some piled-up demand for durable consumer goods such as automobiles, refrigerators and radios still exists, and the federal, provincial and municipal governments combined have a fairly substantial backlog of public investment projects, execution of which is being postponed for a recession period. Consequently, the volume of total spending in Canada should remain high for some time, unless the Canadian economy is subjected to deflationary pressure from outside.

Forces for Prosperity and depression in the United States

The major outside influences on Canadian economic conditions come from the United States and the United Kingdom. Any forecast of economic developments in Canada must take account of the prospects in these two countries.

Despite recent declines in certain commodity prices, there is no reason why the United States should have a serious depression in 1948, *unless* the business and financial community succumbs to panic. A group of economists canvassed by the National Industrial Conference Board expressed opinions ranging from continued prosperity to mild recession in 1948. The most pessimistic anticipated unemployment of from 7 to 8 million, equivalent to some 12 per cent of the working force. Such a figure would mean a recession comparable to that of 1939. Similarly, 75 out of 100 economists polled by the Dodge Corporation

expect some recession in 1948 but do not expect a serious depression.

The President in his Economic Report is still more optimistic. He expects "another year of splendid achievement" and insists that "inflation is the dominant problem." He points out that inventories are not high relative to sales, and that the ratio of spending to liquid assets, while higher than in 1945, is still much lower than in 1940. He does point out, however, that "when an inflation is in progress, there is no way of predicting when it will break of its own accord. One can only be certain that if permitted to run its own course, it will break with destructive force."

On the other hand, the United Nations Department of Economic Affairs is some what more pessimistic. They too consider a minor recession the most likely development in 1948; but they warn that "a recession may, however, have a serious depressing effect on business investment and fixed capital, which in 1948 will be much less conditioned by urgent needs of postwar re-adjustment. Although the unsaturated demand for automobiles and houses will have a mitigating influence, large portions even of that demand may cease to be effective once the recession sets in. In that case a serious depression instead of a mild recession may well be the result." They add that in the absence of additional American financial aid, net exports will fall, and they anticipate that voluntary inventory accumulation will come to an end during the year. Automobile sales are likely to increase with improved supply conditions, but residential construction will be hampered by high cost. Finally, it is their opinion that the piled-up demand for plant and equipment was largely met in 1947, and that henceforth investment plans will depend on the current economic situation.

On the whole, the most likely situation in the United States would seem to be a mild recession. If this recession takes the form mainly of price reductions, it need not injure and might even help the

Canadian situation, through the fall in cost of materials and equipment imported from the United States.

Forces for Prosperity and Depression in the United Kingdom

The sterling area constitutes our chief export market. The Canadian economic situation would obviously be improved if free convertibility of the pound sterling into American dollars were restored in the near future. However, there seems little likelihood of such an event, unless the Marshall Plan develops on a very large scale.

It is important to understand that the current British crisis has been developing at least since 1913, and probably since the Great Depression of 1873-93 began. As Dr. Kahn says in his recent book on *Great Britain and the World Economy* "by 1875 she (Britain) was seriously challenged; by 1913, she was no longer even the second industrial nation." Her export industries were very narrowly based on steel and textiles, fields in which Britain faced increasingly effective competition in the late 19th and early 20th centuries. As early as 1825 Britain faced an unfavorable balance of trade in commodities, and by 1875 she had an unfavorable balance of trade in goods and services combined. She had become a "rentier" nation, paying for her unfavorable balance of trade with the returns on her foreign investment.

The two world wars accelerated and aggravated the tendencies towards stagnation already observable in 1913. Both wars brought liquidation of overseas investment and accumulation of overseas obligations. Both accelerated the industrialization of other countries and the development of foreign shipping. Both contributed to the growth of financial centers in other countries. Both led to more rapid improvement of techniques in other countries than in Britain. By 1946, U. K. industry as a whole was not more than half as efficient in terms of productivity per man-hour as U.S. industry. In 1937 world trade was 143

per cent of the 1913 volume, and world industrial production 152 per cent of 1913 but U. K. exports were only 72 per cent of the 1913 level.

Until enough savings and investment have been undertaken to get the British economy "over the hump," Britain will face severe difficulties. Despite wartime deterioration of plant and equipment, gross capital formation in Britain was less in 1946 than in 1938. Even in so crucial a field as coal, production was lower in 1946 than in 1938, while consumption was greater, exports and stocks very much less. It will be a long haul before Britain restores her capital equipment and her ability to compete in world markets. Meanwhile, we can go on exporting to Britain in large quantities, if we do not insist on payment in dollars, or if the dollars are made available by the Americans and ourselves.

General Conclusions

There seems a good chance that Canada may escape a primary postwar depression altogether this time. The Canadian economy can survive, and may even profit by, mild recession in the United States. The economic difficulties in Britain are likely to continue for some time, but if an adequate supply of dollars is forthcoming, we should have no difficulty in disposing of our major exports in one market or another. Moreover, the government's plans for maintaining full employment would probably prove adequate to meet a mild recession. Thus any decline in 1948 is unlikely to be serious, unless business men themselves become panicky, and there is good reason to suppose that 1948 will be the most prosperous year in Canadian history.

Professional economists are in general agreement that the real danger lies farther ahead. Some time in the early 1950's, when piled-up demand for capital and consumers' goods has been exhausted, when competition in export markets will be more keen, and when large stocks of

inventories, housing, and plant and equipment have been accumulated, the stage will be set for deep and prolonged post-war depression. The depression of the 1950's could be as much greater than that of the 1930's, as world War II was greater than World War I. How soon this threat will appear depends to a large extent on how successful we are in fighting inflation now. Inflation brings more rapid exhaustion of the financial reserves of households. It shifts incomes from wages to profits, and thus increases savings at the expense of consumer spending. It raises costs, and so leads to postponement of investment.

Of course, the threat of secondary postwar depression could be staved off by appropriate government policies. In

Canada the present government is committed to such policies, but lacks the cooperation from provincial governments necessary to execute them. Great Britain has both the commitment and the powers for an effective fight against unemployment. The United States, on the other hand, lacks even a clear-cut commitment by its government to pursue the policies needed to avoid another great depression. One need be no Marxist to recognize the danger that another great depression in the United States might foment so much unrest as to lead to the development of a species of fascism in that country. In such an event, the chances of avoiding World War III would be very remote.

Some Thoughts on Steel Production

By STUART ARMOUR

SINCE considerable interest in the subject of Canadian steel production has of late been evident, and since a good deal of misinformation seems to be going the rounds, it may not be out of place to recite a few facts at this time. As usual, the facts may prove somewhat less interesting than the fancies. The principal question in the minds of certain persons seems to be: "Is there sufficient steel-making capacity in both Canada and the United States to meet post-war demand?" It is an involved subject which can only be profitably discussed if it is dispassionately examined in all its aspects.

Production Figures

While official figures show Canada to have an annual ingot producing capacity of some 3,300,000 tons, the present-day usable capacity is thought by steelmen of long experience to be considerably below that figure. Hence, when the over-all Canadian ingot production

figure for 1947 is officially estimated at some 2,900,000 tons, this, they say, should be related to a productive capacity of not more than 3,000,000 tons. Production in 1947 was nearly twice as large as in 1937, the peak pre-war year. It was about two-and-one-half times larger than the average of production for the years 1935-39 inclusive.

It is said, in fact, that percentage-wise the production of steel in Canada has increased far more during the past seven or eight years than that of any other country in the world.

In 1918 the Canadian steel industry produced 1,800,000 tons of ingots. Eleven years later, in 1929, a year of very high prosperity, production was only 1,467,000 tons. This represented utilization of only 78.7% of then rated capacity. Another decade later, in 1939, when all Canadian industry was operating under the shadow of World War II, production reached 1,490,000 tons; only 69.2% of then rated capacity. Not until 1940, when production totalled 2,178,000 tons did Canadian ingot production exceed