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Notes for remarks by
Finance Minister Jean Chrétien
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CHECK AGAINST DELIVERY

I welcome this annual opportunity to come to Toronto and speak to the Canadian Club on the state of the Canadian economy. A year ago, as a new Minister of Finance, I spoke to you about how I expected the economy to perform in 1978. I also gave you my views on the question of national unity. Today, I will speak on the major economic issues confronting Canada. Last week I was very encouraged to hear Darcy McKeough say that "There's a big difference between being a brilliant economist and a good Minister of Finance." I agree with him on that and other comments he made in the same speech.

First, I am pleased to be able to report considerable progress in the economy in the last year. The achievements of 1978, I believe, have contributed to the underlying strength of the Canadian economy.

Employment grew much more rapidly than we had expected. More than 400,000 new jobs were created over the last 12 months. Despite the strong increase of almost 4 per cent in the labour force, there was a slight decline in the unemployment rate, contrary to what had been predicted by almost all forecasters.

Manufacturing output went up by 9 per cent over the past year, and employment in manufacturing rose by almost 7 per cent, or 125,000 jobs. At the same time, there was an absolute decline in employment in public administration. Capacity utilization in manufacturing grew from 83.6 per cent in 1977 to 87.4 per cent by the third quarter of 1978, and is now above the long-term average. Industries such as steel, textiles, shoes, pulp and paper and lumber are operating at close to full capacity.

The depreciation of the Canadian dollar has contributed to a much improved competitive position in international markets and thus to a record trade surplus of more than \$3.5 billion. In a report issued last week, the C.D. Howe Research Institute stated:

Industrial production is up 6.5 per cent over the past year. The Conference Board said recently that "Consumers have expressed more optimism in the last nine months of 1978 than at any time since 1973."

Despite all of these positive signs, there were some disappointments in 1978. Real growth in GNP of about 3 1/2 per cent was somewhat lower than I forecast. I did not foresee the extent of the increase in food prices or in import prices which were affected by the devaluation of the Canadian dollar. The increase in the Consumer Price Index was thus higher than I had hoped.

For 1979, we expect a better price performance. Yet, while the rate of increase in food prices will be less than in 1978, beef prices are still on the way up and food prices will again be pulling up the overall rate of inflation. In part because of a re-assessment of the food price situation, it now appears that the CPI for 1979 will average about 7 to 7 1/2 per cent above its 1978 level, compared with the 6 1/2 per cent forecast in my budget last November.

Economic growth is extremely difficult to forecast. The oil price increase by the OPEC nations, which was higher than had been expected, is a negative development. Our oil import subsidy program insulates Canadian consumers from the direct effect of this increase in the short-run. But the adverse impact of the OPEC action on world price trends and on the balance of payments positions of the oil-consuming nations obviously has some negative implications for Canada.

The higher increase in the CPI together with the rise in domestic interest rates following on the increase in U.S. rates also have negative implications for our economic growth.

An extremely important factor for Canada is what will happen in the United States. Many forecasters predict a downturn there because of the sharp increases in interest rates. Yet recent evidence demonstrates continuing strength in the American economy. The conflicting signals we

growth in order to free resources for use in the private sector. In my last budget, I provided enriched investment incentives through the tax system. As I have said earlier, business is responding with increased investment. Nevertheless, I think that there is room for further expansion.

These developments, on what economists call the 'real side' of the economy, are encouraging. Although preliminary evidence of supply constraints in a number of sectors does suggest a need for some caution, at the same time, it favours strength in investment.

Inflation - The Main Problem

In my view, inflation remains our major economic problem. I want to talk about some of the underlying developments on the price and wage side of the economy. Here, while there are some signs of progress in making the necessary adjustments to lower rates of inflation, we clearly have a long and difficult way still to go.

In order to continue to create jobs at the record pace we have been experiencing, and in order to reduce an unemployment rate which remains too high, we must not let our costs get out of line. All our efforts must be directed towards maintaining and improving our competitive position. Otherwise we will not be able to reach our primary goal which is a job for every Canadian who wants to work.

The recent numbers confirm that the cost of living is beginning to slow down from the rapid increases of last summer associated with the upsurge in food prices. Nonetheless the year-over-year increase is still a high 8.4 per cent. This is undoubtedly making the transition to the post-control era more difficult. While there has been no price or wage explosion, some upward drift in wage settlements is apparent. Some recent settlements have been disturbingly high and there have been some sharp price increases. If these were to become the norm, we would be in serious trouble again.

I want the business community to use its increased profits for investment and job creation. I do not want to see unwarranted increases in dividends or inflationary wage settlements which inevitably are passed on to the consumer in the form of higher prices.

Earlier, I stated that the lower Canadian dollar has improved the profit position of many industries. These industries will benefit in the longer term only if they re-invest these higher profits in modernization and expansion of plant and equipment so as to improve competitiveness and productivity. I intend to watch the situation very closely.

The objective of my economic policy in 1978 has been to prevent a new inflationary spiral. I introduced two budgets aimed at bringing down prices and increasing competitiveness.

We have cut sales taxes in order to slow down price increases. We have delayed increases in energy prices. We have taken a tough stance at the bargaining table with our own unions. The average wage increase granted by the federal government since controls were lifted is slightly more than 7 per cent. This includes the letter carriers' agreement, which was admittedly on the high side.

Over the past several years we have taken a series of tax measures consistent with the priority we attach to private investment as a leading factor in our medium-term growth prospects. Last November's budget included further measures of this type, including the indefinite extension of the investment tax credit at an increased rate, and higher rates of credit for the slower growth regions and for investment in research and development.

The government has been willing to run substantial deficits over the past few years in response to the rather slow growth that has prevailed over this period. In the November budget, I forecast that while cash requirements would remain high in the upcoming fiscal year - at \$10.75 billion -