

DALHOUSIE UNIVERSITY BULLETINS  
ON PUBLIC AFFAIRS

XI

Canada's Economic  
War Policy

By

B. S. KEIRSTEAD



TORONTO

Thos. Nelson & Sons, Limited

1941

JF  
1321  
III4  
no. 11

1321  
.114  
no. 11

DALHOUSIE UNIVERSITY BULLETINS  
ON PUBLIC AFFAIRS

XI

# Canada's Economic War Policy

By B. S. KEIRSTEAD



TORONTO  
Thos. Nelson & Sons Limited  
1941

DALHOUSIE UNIVERSITY  
LIBRARY  
HALIFAX, N.S.

# Canada's Economic War Policy

## PREFATORY NOTE

This BULLETIN has been based on material prepared in the course of a study of the impact of the war on the Maritime economy, which is being conducted by the Institute of Public Affairs at Dalhousie University. Though it is not itself an integral part of the larger study which has been undertaken, it was thought that it contained sufficient interest in itself to warrant separate publication. The views expressed in this bulletin are those of the author and do not necessarily reflect the opinions held by the Research Committee of the Institute of Public Affairs.

The BULLETIN does not attempt to be an up-to-date chronicle of Canada's war effort; such is impossible except for the periodic journals or the newspaper press. It is rather intended as a review of a limited aspect of Canada's war effort, namely the economic policy of the Dominion as it emerged during the year 1940.

But the calendar or fiscal years are purely arbitrary time divisions. Policy is in a continuous state of development. As the war goes on the unfolding of policy throws more and more light on what has gone before. By the time this BULLETIN has appeared new facts may be divulged which would throw light on some of the questions of policy and require modifications in our interpretation. Because of this the author must be rigorously on guard lest he impose on his material any *a priori* schematism. But since it is impossible to set out "facts" without arrangement and selection, there must be always an element of personal or subjective judgment; and so the reader also must remember that new developments may shift the emphasis with which, or the focus through which, the facts are herein related.

## I. INTRODUCTORY CONSIDERATIONS

The object of military strategy is to concentrate against the foe the maximum striking power of which the state is capable, and this concentration must be at the point where and at the time when the enemy is most vulnerable. In modern warfare the concentration of this maximum striking power requires far-reaching changes in the economic organization of a belligerent state. To supply its armed forces with the machines and weapons of today the entire industrial structure must be "mobilized" for war. Every available man and woman, every available machine and factory, every available acre of land, every available source of steam or electric power must be engaged in the production of ships, aeroplanes, guns and munitions, and military supply. "Every available man or machine" means not only every man or machine that was lying idle in peace time, it means every man or machine that can be spared from peace time occupations up to the limit of maintaining the barest essentials of peace-time services and the necessities of life. Thus the limits to a country's war effort are set by the physical capacity of the economic system, the number of men and machines that it possesses, and by the willingness of its inhabitants to make sacrifices in their standard of living.

But economic mobilisation, like military, must proceed, if it is to be effective, according to a plan; it must be directed and organised. It might be a dramatic gesture to call to arms hundreds of thousands of men, but if equipment is not available to arm them it is useless; indeed worse than useless, because it takes them away from the factories where they might be employed in making weapons. It would likewise be mismanagement to adopt a policy which forces the public to go without the ordinary necessities and comforts of life while there are great unemployed resources of capital and labour. Such a policy would cause further unemployment in industry and put men to walking the streets while new factories for war goods were still in the building. Thus the transition to a war economy should begin by taking up the slack of employment and continue as rapidly as is consistent with the regular absorption of the labour and capital resources by the war industries. As these resources are employed in filling military supply, good organisation must guarantee, also, that labour and capital be directed to their most important uses and distributed among the various war employments so as to provide for a steady flow of component parts, as and when required, in an order of importance determined so as to maintain a constant stream of finished war goods emerging from the factories into the hands of the soldiers, sailors and airmen.

If the above argument has been correct there are two conclusions about the nature of economic organisation in war. The first is that the

"order of importance" which will determine the distribution of the productive resources of labour and capital will depend on the military needs and that in turn on the strategic situation or expected situation. This means that it will depend on the military plan or strategy.

The second is that the economic problem of war, considered apart from the larger problem of grand strategy consists in the methods to be used to allocate the productive resources so as to get the various needs satisfied according to the "order of importance" as designated by the military. The methods which may be used are of two general sorts. The government may acquire income from the public by taxation and borrowing and use it to bid up the prices of the productive agents (labour and capital) in the war goods industries, while at the same time the restriction in consumers' income forces down the prices of the agents in the peace-time industries. This method is a general reliance on the mechanism of the price system. The other method is for the government to enter the economic field and use its compulsory powers, saying that so much labour, so much capital, so many raw materials are to be allowed various industries, establishing what are called "priorities," namely, the right of essential war industries to satisfy their requirements before inessential industries are allowed to enter the labour or raw material markets, and even rationing the consumption by civilians of certain scarce goods. We shall have an opportunity to discuss and illustrate both these methods later as we come to examine the Canadian war economic policy.

The first consideration, then, dependent on military need, is the determination of "what has to be done;" the second, the purely economic problem, is "how to do it."

## II. THE FIRST PHASE TO MAY 1940

The general plan of Canada's war economic policy, that is the "order of importance" which was to be set her, naturally turned on strategical considerations. Thus, when she declared war on September 10, 1939, the economic direction of her war effort was determined by Anglo-French grand strategy. The Allies had an overwhelming preponderance of potential economic power, which, once developed, would be irresistible. They had also strong defences, the North Sea for Great Britain and the Maginot Line for France, on which they assumed they could safely rely while they built up their economic strength on a long-run plan which, though slow in maturing, would give the maximum strength when complete, and would cause the minimum of dislocation in their economies and be overwhelming after Germany had been weakened by two or more years of blockade. Sea power was on their side, so that they could rely on confining Germany

within the bounds of central Europe, depriving her of essential materials, at the same time obtaining supplies themselves from Canada and the United States.

When Canada declared war she did not have an economy in any way prepared for modern war. Her defence appropriations of thirty-two million dollars in 1938 and thirty-four millions in 1939<sup>1</sup> were rather less than 1 per cent of her total national income. This figure may be compared with the 50 per cent of her national income which Germany was devoting to military preparations during those years and the 25 per cent which Great Britain was devoting. As a consequence, Canada had a very small regular army, a small navy and a small air force, though all the services were regarded as highly competent. She had no large scale munitions and weapons industries, and for the most part lacked developed industries making machine tools, precision instruments and other necessary components of war industry. On the other hand she did have great natural resources and basic industries which were potentially of great value in modern war. She had an important steel industry; she produced 80 per cent of the world's supply of nickel, and supplies of copper and aluminium adequate to meet the war needs of the entire British Empire. She had a great export surplus of grains and feed and other agricultural products. Her forest and chemical industries could quickly be adapted to war purposes. With the development of the Turner Valley she was able to produce ten million barrels of oil annually and she had a developed refining industry. In addition, Canada possessed certain large scale manufactories, which had significant war possibilities and of which the most important was the automobile industry.

Consequently, on the basis of the strategical assumption that the Allies could develop their economic strength along the lines of comparative advantage, relying on their defensive strength in the meantime, Canada was asked to specialise along the lines which were indicated by her natural advantages. Instead of creating a large army for overseas service she was asked to undertake the Commonwealth Air Training Scheme, for which her geography and her flying traditions rendered her particularly suitable. In the industrial field, similarly, instead of attempting the development over a wide variety of products, of new war industries, she was asked to intensify production in the supply of raw materials, such as steel, nickel, copper, oil, cellulose and so forth, and to adapt her automobile industry to the mass production of military motor vehicles. Demands were also made on her chemical industry for explosives and on her infant aircraft industry for trainer aircraft.

1. This was of course the appropriation in the peace-time budget for the fiscal year 1939. When war broke out, a supplementary budget was immediately introduced.

In determining the economic methods to serve these general objectives the Canadian government seems to have had in mind two main considerations. The first was that Canada when she entered the war had a large mass of unemployed resources. There was idle plant and there was plant which was not being worked full time. There were thousands of unemployed workers and thousands more who were only in partial employment throughout the year. It was thought better to bring these unemployed resources into employment rather than to undertake an immediate policy of heavy taxation restricting consumers' demand. Such a restriction of consumers' demand would lead to reduced production of consumers' goods and would cause further unemployment at a time when the war industries had not begun to take up the slack in the already existing unemployment. The second consideration was that Canada's contribution was to be mainly along the lines of intensive development of already existing industries. This implied, to the government, that it was wisest to leave the expansion of these industries in the hands of the industrial executives who were familiar with the industries and consequently to have as little government interference as possible. These two considerations when taken together implied that fiscal policy should be directed towards the expansion of industry rather than the restriction of demand, and further that the price mechanism should be left relatively free to bring about the industrial expansion, and that there should be as little direct government control as possible.

#### THE FIRST WAR BUDGET

Parliament voted in September, 1939, one hundred million dollars for national defence.<sup>1</sup> The taxation which was levied to meet this appropriation was not restrictive. A 20 per cent surtax was imposed on all taxable income under the Income Tax Act.<sup>2</sup> There were also certain excise taxes, chiefly on luxury goods, but in the words of a later Minister of Finance, "these new or increased taxes were not designed to provide immediately for any large part of our heavily increased expenditures."<sup>3</sup> In response to popular pressure, a tax on excess profits was imposed, but it was the government's desire not to restrict too sharply the attractiveness of increased production, and the consequent Act could not be regarded as very severe. It provided for two schedules of rates at the option of the taxpayer, that is, the taxpayer could elect the schedule according to which he would be taxed. Schedule A imposed a graduated tax beginning at

1. An Act for granting to His Majesty aid for national defence and security. 11th Sept., 1939.

2. An Act to amend the Income War Tax Act, Sept. 12th 1939.

3. The Hon. J. L. Ralston, Hansard, unrevised edition, June 24, 1940.

10 per cent of profits in excess of 5 per cent and not exceeding 10 per cent of the capital employed and rising to 60 per cent of profits exceeding 25 per cent of the capital employed. Schedule B imposed a straight levy of 50 per cent on all "profits on excess of the average annual income of the taxpayer . . . for the four years 1936, 1937, 1938 and 1939 . . ."<sup>1</sup>

These taxes considered in sum were scarcely restrictive, particularly when set against the government's spending and its monetary policy. In November, 1939, a loan of two hundred million dollars was arranged with the banks on two-year notes at a rate of 2 per cent. Of this amount ninety-two millions was used to repatriate Canadian securities held in London; the balance was devoted to financing the war appropriation of one hundred million.

"This borrowing from the chartered banks was facilitated by appropriate monetary policy. Between August and November the Bank of Canada's assets increased by approximately one hundred and seven million dollars as a result of the purchase of securities and the increase in the value of its gold and foreign exchange reserves. This provided cash to meet the enlarged public demand for notes in circulation and to increase the cash reserves of the chartered banks by thirty-three million dollars.

"With this increase in cash reserves, the chartered banks were enabled to increase their total Canadian deposits by approximately three hundred and six million dollars. In the same period, they increased their current loans by approximately one hundred and forty-seven million dollars, mainly to finance the large wheat crop, and added to their net holdings of securities by one hundred and fifty-eight million dollars."<sup>2</sup>

Thus in the early stages of the war Canada's policy was to undertake an expansion of output, stimulated by borrowing, increase of credit and moderate government expenditure on supply. The object was clearly to direct certain industries and certain of the productive resources into war channels. The stimulus was reflected in the indices of production and volume of business. It was presumed that for the time being, at least, no serious sacrifices need be borne by the Canadian consumer. The increase in national income which was envisaged would take care, and more than take care, of the war needs.

The expansionist policy was continued by a public loan early in the new year (1940) of two hundred million dollars. The loan had the effect of taking money out of savings deposits held by the public and putting it into deposits which the government used for its supply programme with the

1. The Excess Profits Tax Act, 12th Sept., 1939.

2. Hon. J. L. Ralston, Hansard, unrevised edition, 24th June, 1940.



somewhat inflationary<sup>1</sup> consequence of putting into circulation money that had been idle. From this policy was derived the initial impulsion or stimulus which became rapidly apparent in Canadian business.<sup>2</sup> The total result was to give the government purchasing power without unduly restricting consumers' demand. This enabled the government to purchase the various war commodities it needed and so to put the idle productive resources to work in the war industries, without withdrawing resources already engaged in ordinary civilian production. The price system was left to reflect this increase in the demand for war commodities and very little direct control was attempted.

#### THE WARTIME PRICES AND TRADE BOARD

The exceptions to this general principle may briefly be noted. Memories of the last war had led some consumers to lay in stocks of sugar, flour, tea and other commodities which were rationed in 1917 and 1918, and exhaustion of retail inventories created local price rises. There were also certain wholesalers who seemed to be unduly increasing their stocks. Prior to the declaration of war the Wartime Prices and Trade Board had been set up and empowered to regulate and fix prices and to take other action necessary to maintain the supplies of certain commodities which were held to be necessities of life.<sup>3</sup> This Board intervened to check speculation in commodities and for the most part accomplished its ends by informal methods, issuing reassuring statements to the public and warning merchants against hoarding. But in November it did step in to buy up all sugar inventories and to become the sole agency for the importation of raw sugar, and as the sole supplier of sugar was able to stabilise sugar prices. Since then a similar control has been set up for wool, and in four commodities the Board has intervened to fix maximum prices. The stability of prices, which however must be attributed to general financial and monetary policy, even more than to work of the Board, because no Board could keep prices from going up in the face of a real inflationary movement, is reflected in the cost of living index which shows only a 6.2 per cent increase during the whole year of 1940.

#### THE FOREIGN EXCHANGE CONTROL BOARD

A second control was established by the Foreign Exchange Control Board. This Board was designed to conserve foreign exchange, to prevent

1. "Inflationary" is not used here in its popular sense of implying unregulated price rise. It merely signifies an increase in the circulation of the medium of exchange which in this case was accompanied by a corresponding increase in the volume of business. Compare footnote page 16.

2. Since the government carried over some two hundred million dollars to the fiscal year of 1940 some of this stimulus was delayed for some time.

3. Under the War Measures Act, 7th Sept., 1939.

exchange speculation and to check the flight of funds from Canada to New York. It must be remembered that, though Canada has a favourable balance of trade, her credits are all obtained in what are called sterling currencies, that is in the currencies of Great Britain, her Dominions and colonies and nations who have linked their currencies to the pound. Her balance with the United States is a debit one, and in wartime when she has all the more need for American imports her sterling balances will not avail for payments to the United States. Consequently it has been of the first importance to preserve for Canada every available American credit. The Board, armed with a large portion of the Bank of Canada's gold, immediately in September pegged the Canadian dollar at 90 cents in New York and became the only medium for the importation and exportation of funds. As the pressure for American exchange has increased, the Board has been given additional powers. How it used these belongs rather to the period of crisis than to the first phase of the war which we are now discussing, and will be considered at a later point in this BULLETIN.

#### SUMMARY

During the first phase of the war Canada accepted the general strategic plan of the Allied powers. The transition of her economy to a war footing was gradual and took the form of intensifying her production along the lines in which she enjoyed natural advantages, rather than any revolutionary change-over in her industrial techniques. She relied upon Great Britain for a great deal of the equipment for her own armed forces and for all sorts of specialised industrial production, such as precision instruments, aircraft components and so forth. Her economy was geared so as to mesh with that of her Allies and the success of the scheme depended on the interchange of materials and goods, as between Canada and Great Britain. For the proper development of her war industries along the lines which had been decided upon she depended upon a financial policy of stimulating new production rather than restricting consumers' demand, and the ordinary price system rather than a system of planned controls was the accepted mechanism for bringing the agents of production into their war employments.

### III. THE SECOND PHASE—MAY 1940 AND AFTER

The military collapse of France completely changed the whole strategic view of the war. The Allies were deprived of the French army and navy, the resources of French industry and French finance, in particular the gold reserves of the Bank of France, and the entire south flank of Great Britain was exposed to attack. There was imminent danger of invasion

and consequently there was a greater need for manpower in the British army at the very time that manpower was needed for increasing industrial production. Thus, while there was greater need for American supplies in the face of an increased submarine menace, there were reduced financial resources to purchase supplies and fewer escort vessels to convoy them.

Great Britain found herself without military equipment and almost without an army, and under the menace of invasion she had to provide both as rapidly as she could. She was consequently unable to provide Canada with aeroplanes, arms, machinery and components. On the contrary, she had to call on Canada for every item of equipment which Canada could possibly spare and to ask her to undertake to make good in part the loss of French industry, achieving a measure of self-sufficiency in war industries. Canada had not only to expand her production along the lines previously laid down, but she had to find either in the United States or within her own boundaries sources of supply for many of those things which she had previously been getting from Great Britain. This imposed on Canada the obligation to create vast new industries, to develop new techniques and new labour skills. In essence it was an industrial revolution. She had to supply her own armed forces with weapons and munitions, she had to undertake to find aircraft for the air-training scheme in addition to the operational craft she was sending the mother country; she had to build herself machine tools, precision instruments, various components for all types of weapons and armour steel. This industrial self-sufficiency imposed by the military needs was a complete reversal of the previous policy of following the lines of comparative advantage. What Canada had to do had been entirely changed.

#### THE SUPPLY PROGRAMME

The details of the new supply programme were not immediately made known, but we can gain some notion of what Canada was asked to do under the changed circumstances by examining her supply programme as it became known from time to time during the subsequent months.

There was, in the first place, the continuation of the Canadian supply of raw materials. Canadian agriculture had to supply foods for an England deprived of Scandinavian and Dutch sources. This meant that the wheat economy, with its European market depleted, had to yield place, at least in part, to the production of hogs, stock, and dairy produce. Hog production, for example, was increased by 50 per cent.

Canadian copper, nickel and aluminium production had to support, as they have adequately done, the war needs of the Empire. Her gold production was stepped up from one hundred sixty-five million dollars (1938) to nearly two hundred millions (1940) to increase her power to buy

United States supplies. Canadian steel had to make her war industries in this essential metal as independent as possible of American sources; 1940 figures of steel production show an increase of 45 per cent over 1939, and in ferro-alloys for armour steel the rate of production has been increased between twelve and fifteen times. In the industries in which there existed, prior to the war, plant, experienced management and skilled labour, fast schedules were set and exceeded. The British Army of the Nile was carried forward to crush Italian power in North Africa in Canadian-built motor vehicles; its supply was maintained by Canadian trucks. The Canadian Active Army of four divisions and their reinforcements and Corps troops and an even larger number of men in the Reserve Army were clothed and supplied by Canadian industry.

Canada undertook to build weapons of the following categories:

- 40 mm. Bofors anti-aircraft guns
- 3.7-inch anti-craft guns
- 25-pounder guns and carriages
- Colt-Browning aircraft machine guns
- Colt-Browning tank machine guns
- 6-pounder guns for tanks
- 2-pounder anti-tank guns and carriages
- 4-inch guns and mountings
- 12-pounder guns and mountings
- 4-inch naval guns
- 6-inch naval guns
- Lee-Enfield rifles<sup>1</sup>

In November Mr. C. D. Howe was able to say that all of these were in production<sup>2</sup> and in February, 1941, that all were up to or ahead of delivery schedule.<sup>3</sup> Figures of deliveries cannot, of course, be given, but some indication of their magnitude can be gained from two sets of figures which Mr. Howe did release. The annual production rate of Bren guns (automatic light machine guns) has been "stepped up" from 5,000 (1938) to 97,500 (1941). Shell deliveries during 1940 had been increased to a monthly rate of 350,000, and some new plant is yet to come into production.<sup>4</sup>

The ship-building programme has included 70 corvettes for the Canadian and British navies, all of which are being delivered on schedule; the conversion of merchant ships and small vessels to armoured merchant

1. Hon. C. D. Howe, Minister of Munitions and Supply, Hansard, House of Commons debates, p. 292, Nov., 1940.

2. Hon. C. D. Howe, *ibid.*

3. Hon. C. D. Howe, Minister of Munitions and Supply, Hansard, House of Commons debates, Feb. 26, 1941, Vol. LXXIX, No. 29, P. 1145-1146.

4. Hon. C. D. Howe, *ibid.*

cruisers and patrol boats, and it has been intimated that Canada may undertake to build destroyers and even cruisers.<sup>1</sup> So far as is known, however, no keels for the larger war vessels were laid down in 1940. There is also some doubt as to what progress has been made on the programme of merchant shipbuilding which was announced in 1940.

Canada also undertook to build both infantry and cruiser tanks for the Canadian and British armies,<sup>2</sup> orders for 3000 of which were placed in 1940, and aircraft of various types for the Air Commonwealth Training Scheme and for the Royal Canadian and Royal Air Forces. Canada had no firms with experience in tank manufacture and but an infant aircraft industry. The problem of finding suitable Canadian industries, adapting them to these types of production and expanding them, was a difficult one, all the more difficult in that there was no previous experience or trained technical and managerial personnel. It is impossible for the layman to acquire any adequate comprehension of the difficulties involved. Though British models were used, innumerable changes had to be made because American or Canadian machinery had to be substituted for British, and American and Canadian component parts had to be used when British parts were unobtainable. Not only did these problems of design have to be overcome but technical productive problems presented difficulties. For example, the whole tank programme was held up for two months until a process had been developed for annealing armour plate.<sup>3</sup> Finally, there were the problems of mass assembly. Not only did the various parts have to be produced but arrangements had to be made so that they would be produced in the proper temporal order to permit mass assembly. It has been, for example, this last difficulty which has been at least partly responsible for the delay in the scheduled production of the Avro-Anson type of aeroplane.<sup>4</sup>

Naturally enough these difficulties have complicated and in some cases obstructed the rapid delivery of these products. The tank production which was supposed to have started in the fall of 1940 was just getting underway when Mr. Howe spoke to the House in February, 1941. Aeroplane production has been disappointing in certain types. The delivery of planes for the Royal Air Force has been up to schedule and the delivery of single-engined elementary and advanced trainers has also been good, though in connection with these it must be recalled that the Commonwealth Air Training Scheme has been stepped up to nearly twice its original rate and the pressure for training planes has consequently been great. It has been in the delivery of advanced two-engined trainers, the Avro-Anson,

1. Hon. A. L. Macdonald, House of Commons debates, unrevised edition, Nov. 19, 1940, Vol. LXXIX, No. 8, p. 231.

2. Hon. C. D. Howe, *op cit.* p. 1146.

3. Hon. C. D. Howe, *ibid.*

4. Cf. Hon. C. D. Howe's statement to the House, Feb. 26, 1941.

that failure to achieve schedule delivery has been most serious. The reasons for this are to be found in the difficulty of the problems that had to be overcome. The Avro-Anson was one of the planes which Britain was to supply for the training programme. When Britain could no longer supply this type it was decided to undertake its manufacture in Canada. For this completely new designs were necessary to suit Canadian manufacturing peculiarities and a Canadian prototype had to be made and tested. Substitute engines which in turn required new engine mountings had to be found in the United States. Sources for all sorts of components had to be discovered and the aircraft design modified to use such components as could be made available in Canada. To solve all these problems the Dominion government formed the government-owned company known as Federal Aircraft Limited, which was charged with the responsibility of producing the Avro-Anson aeroplane. It had to find the new parts, make the necessary modifications in design, assemble the designs, build and test prototypes and then let out by contract to aircraft and aircraft component manufacturers the actual job of manufacturing. It had to set its contracts so as to obtain synchronised production of the various parts which would permit of mass assembly. Apparently these problems did not permit of as speedy a resolution as had been anticipated. No delivery of the craft was made in 1940 and it appears that there will be some further delay before deliveries can be expected.<sup>1</sup>

In sum, what Canada was asked to do after the collapse of France was to maintain and increase her production of essential materials and at the same time to carry through what amounted to an industrial revolution in the development of new industries directed to the production of munitions and weapons and to become as far as possible a self-sufficient war economy. The difficulties were immense, and that there would be some failures was to be anticipated. But some notion of the general undertaking may be obtained by comparing the industrial advance of 1940 over 1939 with that of 1930 over 1925. In one year under the stimulus of war, and with government planning and direction, Canada achieved a technical revolution and expansion of output equal to or exceeding that which she achieved during the five years that had witnessed the greatest peace-time industrial development that modern capitalism had ever achieved under the stimulus of private profit.

#### FISCAL POLICY

The supply programme set the objectives, determined what the Canadian economy had to do. We come now to the question, how was it done; what were the economic techniques adopted to achieve the war purposes.

1. Hon. C. D. Howe, *op cit.*, p. 1155.

As we have seen, Canada had previously relied upon the price system to reflect the change in the demand for the productive agents. Her fiscal policy was devised so as to give to the government a large volume of purchasing power which it could use to attract production in the war industries, but to do so without restricting to any appreciable extent ordinary civilian demand. However, fiscal policy need not be conceived as a choice between taxing or borrowing. Wars have to be paid for out of current real income, in the sense that the guns, the ships, the tanks, the aeroplanes and all the various miscellany of war must be currently produced. To produce them in adequate quantities requires that every productive resource, labour and machinery, that can be made available, be employed in military supply. This imposes a two-fold process: (a) the employment of previously unemployed resources, and (b) the diversion of resources previously employed in satisfying civilian demand to the war industries. To obtain the maximum employment a fiscal programme of borrowing and monetary expansion is required. To obtain restriction of demand for civilian needs requires taxation. Thus the expansion and the restriction, borrowing and taxation, are not opposites or alternatives but complementaries. One must expand production and at the same time restrict civilian demand. This requires that a nice balance be maintained as between the volume of borrowing and the burden of taxation. The guiding principle for this careful balancing must be the volume of the national income and the estimated productive capacity of the economy.<sup>1</sup>

The Canadian budget for the fiscal year of 1940 recognized the complementary unity of taxation and borrowing. It estimated expenditures of \$1,550 millions made up as follows—for the war at least \$700 millions, probably \$850 millions; for the repatriation of British securities \$200 millions; for government losses on the storage and marketing of wheat \$50 millions—that is, \$1,100 millions for direct and indirect war expenses—and \$448 millions for ordinary government expenditures. To meet these costs the government had in hand the \$200 millions in cash which it had

1. Inflation is frequently talked of as a method of war finance but people are often careless in the exact use of the word. In one sense the policies of the Dominion government during the first period of the war were inflationary. There was a definite expansion of credit and note circulation but there was no serious rise in prices because of the increase in production. If, however, there is a continued increase in credit after national production has reached its maximum or if there is an increased demand for purchasing power left in the hands of the public when the production of consumers' goods has been stabilized or even reduced, then there will really be an inflation of prices. This does have the effect of putting purchasing power in the hands of the government, restricting civilian demand because of the increase in prices, and enabling the government to attract industry into war channels. The great objection is that it does so in the clumsiest possible manner. It does not make for rapid adjustment and it distributes the burden of war sacrifices without any regard to the ability to bear them. It is consequently destructive of national morale. It has been well said that this type of war finance is characteristic of a nation facing defeat. It would be disastrous if advocates of this method should gain any following in Canada.

carried over from the previous fiscal year. It proposed to raise \$760 millions by taxation, \$50 millions on the sale of War Savings Certificates, and \$550 millions by borrowing operations.

Let us examine this programme to see the balance which was maintained between the restriction of demand and the expansion of output. The total national income in Canada was estimated in 1939 to amount to \$4,039 millions and in 1940 to \$4,594 millions.<sup>1</sup> Thus the increase was approximately \$550 millions. The increase in the amount spent on war goods and services was approximately \$720 millions. A certain amount of this was spent by the Canadian government in the United States but this would be more than offset by the increase in the amount spent by Great Britain in Canada. Including the British expenditures, the total increase in the volume of war goods and services produced in Canada would probably be in the vicinity of \$750 or \$800 millions. Thus the total production of all goods and services in Canada increased by a value of about \$550 millions, and the production of war goods and services increased by a value of \$750 or \$800 millions. This means that about three-quarters of the war production was accounted for by expansion. The balance of some \$200 to \$250 millions must have come by diverting peace-time production into war channels, and this would require a restriction of total civilian demand by that amount.

Civilian demand is of two sorts—the demand for the ordinary goods and services, including both the necessities and comforts of life which we consume and the demand for what are called producers' goods, that is to say, the durable goods or capital which are used in the further production of goods ultimately destined for civilian use. For purposes of brevity we shall refer to the first as consumers' demand and to the second as producers' demand, and to distinguish this type of producers' demand from the demand for plant and machinery for the production of war goods we shall use to designate the latter the phrase "war-producers' demand." Now, taxation restricts both consumers' demand and producers' demand. It restricts consumers' demand by withdrawing from the consumer a portion of the money which he would otherwise have to spend on consumers' goods. It restricts producers' demand in two ways. It restricts it directly because certain taxes reduce the volume of both private and corporate savings which would ordinarily be invested; that is, would be used to purchase plant and machinery and other capital; it restricts it indirectly because by reducing consumers' demand it limits the possibility of expanding output in consumers' goods industries and thus lessens their attractiveness for new investment. Certain types of borrowing may also restrict consumers'

1. J. J. Deutsch, Bank of Canada estimates for the Rowell Commission on Dominion-Provincial Relations.



demand. War Savings Certificates, for example, which are subscribed by lower income groups, and which are taken periodically out of income, reduce the available income which the subscriber has left for spending. Contributions to the unemployment insurance fund also form periodic limitations of spending power. Government bond issues on the other hand are generally subscribed from savings balances held in the banks. There may be some reduction of spending, because when the bank balance is reduced there is a tendency with many of us to try to re-establish it by economising in what we spend on certain comforts or luxuries, but such bond issues do not lead to a regular and continuous reduction in spending. On the other hand they do tap the savings balances which are ordinarily used for investment and thus reduce the volume of peace-time producers' demand.

### TAXATION

The new Canadian taxation of 1940 was both direct and indirect. The direct taxes, with the amount of increased income which they were estimated to yield over a full year, were as follows:

The increase in the personal income tax . . . . .	\$58 millions
National Defence Contribution Tax . . . . .	\$35 millions
Excess Profits Tax . . . . .	\$100 millions

The indirect taxes were a miscellaneous group, of which far and away the most important was the War Exchange Tax, a levy at a flat rate of 10 per cent on all goods imported for sale in Canada.<sup>1</sup> The total increased revenue estimated from all the indirect taxes amounted to about \$85 millions, making a total increase in all tax revenues of \$280 millions. Of this sum the better part of the indirect taxation, the National Defence Contribution Tax and some part of the increased Income Tax, would all restrict consumers' demand. If we add in the \$50 millions for War-Savings Certificates we have a total restriction of consumers' demand of something under \$200 millions. Presumably the remainder of the restriction came from peace-time producers' demand. We cannot of course set the total amount of taxation as exactly equal to the reduction in demand because we have not taken account of the increased incomes that consumers would be earning as a result of the war. Nevertheless this gives us an indication that the taxation

1. The following items are specifically excluded: 360,460,690,690(a), 696(a), 700,700(a), 701,702,603(a), 704,705,705(a) 706,707,708, and 709. *Customs Tariff and Amendments*. These items consist of such things as Canadian and British coin, fine paintings and works of art, philosophic and scientific apparatus, goods introduced temporarily by travellers or exhibitors at exhibitions, settlers' effects and articles for the use of diplomatic representatives, munitions of war and goods, the growth, produce or manufacture of Canada after having been exported therefrom.

policy was such as to reduce the increased volume of money income in the hands of the civilian public by approximately the same amount as the reduction in the volume of real income produced available for the civilian population. What we have next to ask is how evenly this burden of sacrifice was distributed over the population.

Indirect taxation bears generally on the whole population, irrespective of ability to pay. It usually results in an increased price so that the consumers of the taxed commodity have to pay the tax according to their rate of consumption. Some people argue that consumption is a measure of ability to pay, on the grounds that a wealthy man consumes commodities far in excess of a poor man. But this argument is misleading if not downright false. A bachelor does not buy the same quantity or type of goods that a married man with children will buy, even though the incomes of the two men are identical. Again a sales tax which falls on all the necessities of life does not bear evenly on poor and rich alike, for, while it is true that the rich man consumes necessities more freely than the poor man, his greater wealth is generally spent on a wide range of goods which the poor man does not buy, and certainly his rate of consumption is never in proportion to his greater income. Consequently a sales tax or a similar indirect tax does not weight as heavily on him as on a poorer man. Finally we might observe that ability to pay is not proportionate to the amount of income. If it were, a man with an income of \$5000 would be fairly taxed if his tax was ten times that paid by a man whose income was \$500. But an income of \$500 has to be spent entirely on the bare necessities of life. Any tax put on such an income forces abstinence from essential consumption. As you get into the higher incomes the tax merely forces abstinence from certain luxuries or prevents saving. The consequence is that ability to pay increases much more than proportionately with income. That is the reason for the steep graduation in the rate of income tax and for the exemption of a minimum income which is free of all direct taxation.

Now the Canadian indirect taxation imposed in 1940 falls on certain classes of goods. It falls on imported goods, on smokers' supplies, on motor cars of the more expensive sort and on certain classes of comforts such as radios, gramophones and so forth. The tax on imports is of value because it restricts importation and helps to conserve foreign exchange, but the tax itself is highly inequitable in its incidence. It does not perhaps touch very many of the actual essentials of life, but all import taxes bear much more heavily on the agricultural West than on the industrial central provinces. The other indirect taxes may be regarded as falling largely on comforts and luxuries. They certainly do not affect the necessities, but it could perhaps be argued that the tobacco tax falls rather on one of the minor vices of the poor than on a luxury of the rich.

The National Defence Contribution Tax is a direct tax levied at a rate of 2 per cent on all incomes in excess of \$1200 for a married person and 3 per cent on all incomes in excess of \$600 for an unmarried person. Considered by itself the tax is ungraduated and does not measure ability to pay, but this tax ought not to be considered by itself. It is supplementary to the income tax and it serves two important purposes. It brings into the economic war effort a large number of income earners who would not be affected by the income tax and it taps many of the new incomes being earned in war industries, thus putting some limit on the increase in consumption of new incomes. In the second place it serves to adjust the war burden as between industrial and agricultural workers. The industrial workers who have benefitted from increased employment and higher wages will come under the tax. Agricultural workers who have not benefitted and who have sometimes even suffered economic losses as a consequence of the war, will be exempt because their incomes are below the exemption limit.

The new income tax is very heavy, according to Canadian tradition. The exemptions have been reduced to \$1500 and the tax begins at 6 per cent on the first \$250 net income. It advances to 8 per cent on the next \$100 and thence by graduations of 4 per cent upon each additional \$100 up to \$5000, thence by graduations of 3 per cent on each \$1000 to \$7000, thence by graduations of 2 per cent on each \$1000 up to \$10,000. The graduations are then less great and advance only with each \$10,000 of additional income up to \$50,000. The tax upon net income exceeding \$50,000, but not exceeding \$75,000, is 50 per cent, and it rises to 78 per cent upon net income in excess of \$500,000. The tax is perhaps as severe as public opinion would consent to at this time. But if one looks upon the incomes which are left rather than the incomes which are taken away one sees that no serious element of sacrifice is being imposed on the classes whose net incomes exceed \$2000. After all, if 80 per cent of the Canadian population can live on incomes of less than \$2000, a married man with a net taxable income of \$2000 (which means at least a total income of \$3500) who pays \$195 in taxes is not undergoing privation when he has \$3300 left after paying his income tax. At the top of the scale the five hundred individuals with incomes of \$50,000 or more in Canada cannot be said to be suffering undue privation as a consequence of the war. Income tax revenues could probably be doubled as over 1940 by sharper graduation without inflicting any serious privation. The only difficulty is that really heavy taxation of the higher incomes would not yield enough to make it worth the government's while to risk the opposition which it might arouse. The total assessed income in excess of \$25,000 does not total more than \$50 millions and if the government took every penny of it, it would only increase its revenues by an amount of about \$16 millions, since it now obtains about

two-thirds of it. If the graduations, however, were stepped up from the very start and were designed to reach high figures at a net income of say \$10,000, the tax yield could probably be doubled.<sup>1</sup>

The excess profits tax which was originally imposed in 1939 aroused a great deal of criticism and it was indeed a very badly framed tax. As amended, the tax imposes a levy of 75 per cent upon all profits in excess of an average taken over the years 1936-39. In cases where the tax yield so calculated would be less than 30 per cent of the net profits then the net profits will be so taxed. This tax is considered as an important revenue raiser and it is also defended as meeting the public request that no profits should be made out of the war.

However, this tax is not entirely equitable in its effect on corporations. Finance companies, and some of the big corporations which held a monopolistic position on the market and which were earning high profits prior to the war, some of them running as high as 20 per cent on share capital, and some even higher, are permitted to increase an already enormous profit by 25 per cent. On the other hand corporations which were barely breaking even during the four pre-war years, find the tax excessive. Thus the tax falls with particular severity on companies in highly competitive industries or on companies in exposed industries which suffer most seriously from depression and recession, and which feel that they ought to be treated with leniency in the good years when they have to put aside a reserve to carry them over the bad. It is possible that some allowance may be made for this latter case when allowances for depreciation and reserve are adjudicated. The government has named a referee whose duties it will be to make fair and equitable depreciation allowances which will be deducted from taxable profits.

Thus in sum Canadian taxation has in general been directed by the principle of ability to pay. There are of necessity certain inequalities, and it may be that in future years certain anomalies in the tax system will be removed. But in war time the essential thing is to restrict consumers' demand by the requisite amount and to do so without reducing the health, morale, and efficiency of the population. The Canadian taxation policy of 1940 seems to exemplify this general principle.

#### BORROWING IN RELATION TO SAVING

We have already shown that the government proposed to raise \$600 millions of its total requirements by borrowing. This sum includes the War Savings Certificates. To these \$600 millions should be added the

1. We are here neglecting provincial and municipal income taxes, which in some cities and provinces are of consequential magnitude. Some redistribution of taxing powers and consolidation of income and corporation taxes is urgently needed. Adequate war finance requires that the federal authority be unhampered in its ability to level equitable income taxes over the whole nation. At present this cannot be done. Had the recommendations of the Rowell-Sirois Commission been considered and implemented, this obstacle to the war effort could have been removed.

\$200 millions which were borrowed just prior to the fiscal year of 1940 and were carried over into that year. This sum represents monetary savings of the previous fiscal year and its use by the government in the current fiscal year on non-civilian spending imposed a real saving (that is an abstinence from the consumption of civilian goods) to the value of \$200 millions. Thus there was a total real saving of \$800 millions. This amount came from three sources: (1) War-Savings Certificates which came out of current income; (2) long-term loans subscribed by the public, which may come partly from current income but partly from accumulated savings; (3) short-term loans on Treasury notes from the banks. The first item is comparatively small, so that we can say that a large portion of the \$800 millions came out of savings and represented a diversion of savings to the government. The general effect of this policy, as we have already noted, was to stimulate business and to increase the national income.<sup>1</sup> It also served to increase savings and to divert to the hands of the government a large sum for investment in the war industries, incidentally imposing restriction on peace-time producers' demand.

In a bulletin of this sort we cannot hope to enter into any further detailed analysis of this subject. We might however note the relationship between this volume of savings directed into war channels and the total volume of savings ordinarily made available to industry by the Canadian public. The total peace-time savings of the Canadian people have been estimated to amount to about \$1,000,000,000 a year.<sup>2</sup> Of this amount about one-half is required to maintain the existing capital equipment of the nation, and the remainder, plus or minus foreign borrowing or lending, is what is available for net investment, i.e., for improvements in and accretions to the national capital. At this rate of peace-time savings, if absolutely no improvements or additions were made to the peace-time capital equipment of the economy and only ordinary maintenance provided for out of savings, there would be available only something over \$500 millions for war savings. Consequently the government's policy amounts to asking the people to increase their savings by at least another \$250 millions or \$300 millions and, since the assumption that there would be no new additions to capital is unwarranted, probably more. This increased saving is not so formidable

1. The almost exact correspondence between the increase in the national income (\$550 millions) and public borrowing, excluding war savings certificates of \$550 millions, is of course accidental.

2. See D. C. MacGregor: "Gross and Net Investment in Canada," *The Canadian Journal of Economics and Political Science*, Vol. VII No. 1. Professor MacGregor estimates gross investment in Canada in 1937 at \$1,137 millions of which \$547 millions was required for maintenance of capital. To the remaining \$566 millions must be added \$199 millions which came from abroad for investment in Canada, making a total net investment in Canada of \$765 millions. But in 1940, far from importing capital, Canada was exporting it to Great Britain, thus reducing the total of Canadian savings available for investment in Canada. The amount exported to Great Britain is included in our figure of \$800 millions as shown in the main text.

as it may appear. A society can save a far larger proportion of an increase in income than it can of the original income before the increase was available. This has its counterpart in the individual's saving; indeed, it derives from the totality of individuals' behaviour. A man who is just earning \$1000 a year will find it difficult to save very much. He may just be able to put aside enough to keep up a small insurance policy, but that is about all. We might find that his total savings amounted to \$50 a year, that is 5 per cent of his income. If his income is increased to \$1500 a year he will undoubtedly feel that he can increase his standard of living and buy certain things that previously he just could not afford. But he is likely to feel that he has now a margin and that some of it he should save. Different individuals will behave differently, of course, but the majority will put aside from \$100 to \$200 of the additional income, that is from 20 percent to 40 percent, as compared with the 5 percent saved from the original income. When a nation at war increases its total income, which is made up of the sum of all incomes earned by its individual members, there will be every pressure exerted to get people to save, and consequently a large proportion of the increased income can be set aside without undue hardship. As a qualification to this proposition we must remember that in Canada there were, at the outset of war, thousands of unemployed, living in destitution and below the level of healthy subsistence. Those people were bound first to restore their standard of living and increase their consumption. This throws the burden of saving, as is quite proper, on those whose standards of living were already adequate.

#### SUMMARY—FISCAL POLICY

Canadian fiscal policy was thus nicely calculated both to stimulate production and so increase the national income by putting unemployed resources to work and to restrict the demand for consumers' goods and for peace-time producers' goods. The taxation programme in general was conceived so as to throw the burden on those most able to bear it and so to impose no sacrifices on the civilian population in excess of those which were necessary to make up the difference between the amount by which the national income could be increased and the total required for the efficient prosecution of the war. The borrowing programme was not inflationary in the worst sense of that word and it was in no way out of proportion to the capacity of the Canadian public to save. In total sum, \$1,550 millions were made available for the public treasury of which all but \$448 millions were for the conduct of the war.

#### CONTROLS AND REGULATION

In the earlier phase of the war Canadian policy had been to permit the regular development of industry according to the guidance of the free price

system with only limited government interference. That was then possible because the emphasis in war production was on the expansion of already well-established Canadian industries. But with changes both in the tempo and the nature of the industrial needs the question of government planning and control assumed a different complexion. With the government the chief or only purchaser of many types of goods, including capital goods, the price system could no longer be relied upon as the guide to the most needed production. It is only competition among buyers that makes the price mechanism a reliable indicator of consumers' needs. If the government tried to simulate competition by permitting different purchasing departments to bid against one another, the result would be chaos. Prices would be driven up and the general cost of the war increased, and production in certain lines might get hung up because of the lack of some small but essential component. In any case the government could hardly rely on free competition and the price system to guide the establishment of new industry. To illustrate one of the many difficulties, the investment of new capital in a war industry that would only be profitable for the duration of the war would not be undertaken if investment were permitted to follow freely the most attractive channels. It is essential for government either to build and operate—or lease—new plant, or to instruct private firms to construct new plant under a government guarantee of amortisation during the period of the war.

Canadian governmental controls during 1940 were not set out according to any "blueprint," but grew as the result of administrative experience and realisation of their needs. In the earlier phase some controllers of "key" materials had been appointed and this system grew and underwent modification. There were controllers under the Ministry of Supply for coal, oil, timber, steel and certain other essential minerals. Their duties were to ensure, at a fair price, the supply of these materials and to provide for the maintenance of a regular flow to the war industries according to their requirements. For the most part the controllers were able to achieve their objects by informal methods because industry was glad to cooperate or was willing to cooperate rather than see the controllers forced to use the powers which remained always in the background. As the various individual controllers gained experience of the techniques of control and as the various *ad hoc* problems of single industries were solved as far as they were capable of solution within the limits of single industry, it became desirable to extend the direction by coordinating the work of the various controllers. The establishment under the Minister of Supply of the Wartime Industries Control Board on which all the individual controllers sat was the first step in bringing about this coordination of

supply. But this Board did not have powers to deal with all questions of supply; its work was not integrated with that of the Labour Supply Council; it was indeed limited to problems of planning the supply only of such materials as were under the control of its individual members. Many observers felt that further measures would need to be taken as scarcities became more stringent and that some authority midway between the Wartime Industries Control Board with its powers limited to specific industries and the Advisory Committee on Economic Policy with its responsibility for broad economic planning would have to be established. Such an authority came into existence with the establishment of the Wartime Requirements Board with its extensive powers over the planning and direction of industrial supply both of materials and other productive resources. This Board has been supplemented finally by the Priorities Board, which will have the responsibility of establishing priorities in capital, materials and labour, a process which is tantamount to rationing industry in its employment of the productive resources.

The problem of artificial restriction of supply by monopolistic firms dominating an entire industry has not been acute in the defence industries. The increase in demand, the government's generous policy on depreciation and the weight of the excess profits tax have been such that, even had the patriotic motive not sufficed, the tendency has been to extend output to the physical maximum. On the other hand there was in peace time a good deal of such monopolistic restriction in Canada, and though it has disappeared in the defence industries where the government is the chief buyer, there is no reason to believe that it does not still exist to the detriment of the public in the ordinary supply of peace-time goods and the necessities of the civilian population.

Besides the establishment of industrial controls, and their extension into supply boards, the government has, under legislation which gave it ample powers,<sup>1</sup> the right to expropriate property, to direct an industry, or, if the industry fails to accept direction, to take over the management for the duration of the war, to set and fix prices, and to enter directly the field of production on its own account. Taxation and borrowing made available to the Dominion government a large share of the annual Canadian savings and made the government the largest investor in the country. The demand for capital for war industries comes, consequently, either

1. An Act respecting a Department of Munitions and Supply, 12th September, 1939; an Act to Confer Certain Powers upon the Governor-in-Council for the Mobilization of National Resources in the present war, 18th June, 1940; an Act to amend the Department of Munitions and Supply Act, June 14, 1940; an Act to amend the Department of National Defense Act, July 8, 1940; an Act respecting a Department of National War Services, 12th July, 1940; an Act respecting the payment of compensation for the taking of certain property for war purposes, 1st August, 1940.



directly or indirectly from the government. But in many cases producers hesitate to embark on large construction to meet a demand, which, though immediately immense, is temporary and, in the future, uncertain and might well leave them at the war's end with an over-expanded plant and capital costs so heavy as to be ruinous. To meet this difficulty and to provide for an abundant supply of new fixed capital when and where needed, the government has arranged in some cases for the amortisation of new plant by permitting contractors on war account to charge in their price an amortisation write-off based on a war-period depreciation.<sup>1</sup> The government, in effect, pays for the new plant over the course of two or four years, and in the end the plant remains in the hands of the industry. Another method, which the government is increasingly adopting, is for it to construct the new plant at public expense and lease it to the industry, retaining ownership.<sup>2</sup> During 1940 the government spent \$146 millions on such construction and plant extension, and the policy is to be continued in 1941. This gives the government a direct interest in and control over war industry which promises interesting developments both now and in the post-war period.

A third sort of direct control has been extended over foreign exchange and foreign investment, a control which had its origins in the Foreign Exchange Control Board. It is difficult to increase Canadian exports to the United States, though there is some hope that there will be an improvement in receipts from American tourists, and there has been an expansion of Canadian gold output. Yet Canadian purchases from her great industrial neighbour have increased, are increasing and will continue to increase to supply urgent war essentials. The only way these war imports could be financed was to reduce other imports to the minimum and to obtain from every available source such American credits as were held by Canadians. Many Canadians, business men and others, held dollar balances in the United States as well as American securities of long term. The Foreign Exchange Control Board has taken over the cash balances and has registered the securities, which it may eventually have to acquire by forced purchase. It has had its powers increased under the Foreign Exchange Conservation Act of December, 1940, and certain items can no longer be imported. Pleasure travel in the United States has been prohibited in the sense that the Board will not sell Canadian citizens American funds for such travel. The Board's monopoly of the sale of American funds gives it, in effect, the power of licensing all private imports from the United States.

1. Hon. C. D. Howe, House of Commons debates, Vol. 79, No. 26, p. 1001 - Feb. 21, 1941.

2. *ibid.*

## LABOUR POLICY

The war industries were calculated in 1940 to require 200,000 additional skilled workers over and above those who were being recruited into the armed forces. Unemployment at the outbreak of the war greatly exceeded this amount in total, but of the unemployed many were unskilled or had lost their skills. Thus we have been treated to the spectacle of labour scarcity in certain trades with a continuing mass of unemployment. Such a situation requires a solution based on the training of the unskilled and the transfer of the unemployed to the areas and industries where the labour shortages exist. To accomplish such a programme, which will require both the cooperation of workers who are to be moved out of their accustomed homes and of those in employment in the industries where they are to be introduced, the government's general labour policy must have the enthusiastic support not only of management but of all ranks of labour. The government's labour policy has been increasingly, of late, based on a recognition of the gravity of the problem of labour supply, though it seemed rather slow in developing a policy which took cognizance of all the difficulties and dangers. At first it seemed inclined to rest on the laurels it had earned by the Unemployment Insurance Act, an excellent piece of legislation, but not one particularly relevant to a situation in which there was a scarcity of workers rather than of jobs. To the task of meeting the need for workers in the war industries the government enlisted the assistance of the provincial Youth-Training Programmes which were then jointly conducted and, for the better part of 1940, were operated at a rate calculated to produce 24,000 skilled or semi-skilled workers a year. There were some training schemes in private industry but no national organisation of such schemes. To the problem of supplementing this admittedly inadequate programme by the rehabilitation of older workers and the training of women the government's attitude as late as November, 1940, can best be given in the words of the Minister of Labour: "I would not want to say that definite representations had been made to industry to employ older men. I think that is something which industry will have to take upon itself. As demand increases and supply diminishes industry will almost automatically be required to take on older men and women."<sup>1</sup> It was not until December that a more realistic attitude was adopted. Then the announcement was made that the rate of training in the Youth-Training Programme was to be doubled at least and that the figure of 50,000 "trainees" might well be increased during 1941. A national system of "upgrading" in industry was adopted, with the purpose of training or rehabilitating men so that they could take

1. Hon. N. A. McLarty, Minister of Labour, House of Commons debates, Nov. 28, 1940, Vol. 79, No. 15, p. 532.

over from skilled workers not their entire task but certain functions so as to leave the fully skilled man with only the most difficult and essential part of his task to perform. This has been credited with trebling the output of some key craftsmen in certain trades. Finally employment transfer bureaux were set up across the Dominion to shift the unemployed into the areas and industries where they were needed.

The enthusiastic support of labour for the earlier policies of the government was qualified by certain misgivings as to where policy was tending. Trades Unions were being asked to agree to the sacrifice of hard-won standards, a sacrifice they expressed themselves as perfectly willing to make, but in return they were anxious to obtain a legislative guarantee that any sacrifices would be for the war emergency only and, also, legislative protection for men engaged in organising workers in war industries. At first the government met these requests by legislation which, in effect, was a statement that in principle the government agreed, but the legislation remained a statement of principle and was not a real guarantee such as labour had been demanding nor a real protection for workers engaged in trades union organisation who had been penalised by their employers for such activity. At the same time the government passed an Order-in-Council extending the compulsory clauses of the Industrial Disputes Investigation Act to all war industries.<sup>1</sup> There was also a feeling amounting to dismay at the use to which the Defense of Canada Regulations—approved in principle by the Canadian Trades and Labour Congress—were being put by certain provincial Attorneys-General. Debates in the House of Commons helped to make known the misgivings that existed in some minds<sup>2</sup> and the government was able

1. The Industrial Disputes Investigation Act (1925) makes obligatory in certain national service industries the establishment of a conciliation board in the case of any industrial dispute which cannot be otherwise settled and might lead to a strike or lockout; strikes or lockouts in such industries which occur prior to the report of the Board are illegal.

2. Not all misgivings have been immediately put at rest. *The Canadian Congress Journal*, the official organ for the conservative Trades and Labour Congress of Canada, had to say editorially in its February, 1941, issue: "Organised labour would like to see the government give a little more tangible evidence that it believes that labour is entitled to be treated as an equal partner in industry . . . It also is true that a halting step has been taken to give labour some place in the war effort by the establishment of the national labour supply council. . . . Labour has also been invited to give its services in the work of the national war charities funds advisory board, a request which has been gladly complied with. It is also equally true, however, that in no case where labour's particular interests are involved, such as in the management of the twenty-eight or more government-financed and owned companies set up for war production, on the committee established to advise the director of ship construction and repairs, or on any of the numerous control boards, has labour been given any recognition whatever.

"The weakness of the national labour supply council is that it has not been allowed to function as a planning body, but instead merely called upon to give an advisory opinion, many times at extremely short notice, on measures already prepared by others. To be of real use, workers' representatives should be placed in a position where they can contribute from their experience toward the shaping of policies and not be called into consultation only after the course of action had been decided upon."

to clarify its position by a new Order-in-Council, P.C. 7440, which was promulgated December 16th. This order altered one of the most objectionable interpretations of the Defense of Canada Regulations—that which made picketing in defense industries illegal; it protected union organisers in industries working on government contracts from victimisation; it guaranteed the restoration of all standards sacrificed by labour at the termination of the war emergency; it established a day of rest for all workers in industries that were going over time but were not in continuous operation on a shift basis, and provided for automatic wage increases with increases in the cost of living. The social attitude which this Order-in-Council reflects is a more realistic recognition of the essentials of a democratic war economy, and it may create a precedent of governmental interference in the labour market of considerable significance for the future. Never before has a Canadian government gone so far in recognising organised labour and in professing the principle that the state has certain obligations to protect the security of the working man. This recognition is one of the signs that Canada, under pressure of war, is rapidly maturing from the developmental stages of a frontier economy to the position of an advanced industrial nation.

#### IV. CONCLUSION

The turn which the war has taken has given to the German Reich almost complete domination of the continent of Europe and the economic support of large sections of Asia. With an efficiency, unqualified by any scruples, she has built up a war organisation unequalled in power, as it has been unsurpassed in ruthlessness, by any regime of modern times. Against this tremendous power there remains in arms to-day only the British Empire,<sup>1</sup> among the nations of which Canada must take second place as an industrial and military state and assume the responsibilities of such a position. The assumption of those responsibilities has imposed upon her changes in the organisation of her industry, in the amount and nature of her capital equipment and in the adaptation of labour skills, which amount in their total effects to an industrial revolution. To accomplish this revolution within the time limits set by urgent military necessity, Canada has had to accept a measure of government planning and government control that has established a precedent on this continent. As the scar-

1. This is not to ignore the immense assistance of the United States, but the United States is not actually a belligerent. Greece, Holland, Norway, Poland, Czechoslovakia and Belgium also "remain in arms," but their forces are almost entirely dependent on British equipment and supply, and, except Greece, these allies are scarcely "nations in arms."

cities become more marked and the stringencies within industry more confining, we may expect to see an extension and a widening of the powers of the government to direct, control, and operate industrial undertakings. Moreover, the compulsory powers of government within the economic field may come to touch the individual citizen as well as the industrial corporation more directly. As we reach full employment, additional war effort cannot be met by increasing the total national output and will require increasingly severe restrictions of consumers' demand, restrictions which cannot be imposed by voluntary borrowing but only by compulsory schemes that will distribute the burden of sacrifice in an equitable manner according to the ability to sustain it.

One cannot of course look into the future and predict with any confidence the final effects of the organisation of the war economy on Canada's social and political life. Much depends on the great imponderables of how long the war lasts, how dreadful and exhausting are the contributions which it will ultimately exact from us and how the war ends. Of the final issue there is none who doubts but the conditions and circumstances under which victory may be achieved are completely uncertain. In the meantime, the strains and stresses of the conduct of the war have released certain forces and have initiated certain processes which are becoming clear and established, set in their channels, so to speak, and their course now runs so strong that some may well be irreversible. We see, for example, the revolution in the internal balance of the economy. Whereas in the last war the contribution of the agrarian west was as great as, and the development of the wheat economy as rapid as, the contribution and growth of the industrial centre, in this war the needs have been such that a tremendous industrialisation has taken place simultaneously with the loss of agricultural markets, a general decline in agricultural production and government-subsidized restrictions in acreage. Canada has become at once a more industrialised and a more self-sufficient nation. This has meant for one thing a greater concentration than ever before of economic power in the industrial east, particularly in the province of Ontario. In any federal state with distinct economic regions there is always an opposition between policy conceived in terms of the greatest pecuniary or productive efficiency and policy as formulated for the attainment of the highest level of social welfare in the least well-favoured as in the best-favoured regions. This opposition remains in wartime though it assumes a modified form, the opposition between the greatest war output and the equitable distribution over the various regions both of the sacrifices which war imposes and the economic benefits which it brings. In this war the federal government has thought largely in terms of the greatest efficiency of output. Such was necessary if Canada were to play the

part assigned to her in the Commonwealth war effort, but it has undoubtedly increased the power of Ontario; it has attracted and will attract still more population from the Prairies and the Maritimes to the industrial centres and it has created discrepancies which will probably become even more marked both in the severity with which the burden of sacrifice will be felt, in the volume of business activity and in the general level of social welfare. Though Canada remains and must remain united while the war emergency lasts, one can see that the strains on Canadian federalism, the disintegrating forces of regional interest and provincial jealousy will be formidable after the war.

Again, the external trading position will be profoundly modified. Canada will become a creditor nation rather than a debtor nation, *vis-a-vis* the European continent and most particularly Great Britain. This means that she will have to accept an increased volume of imports of European and British origin, but these imports will be manufactured goods and Canada will have manufacturing equipment far in excess of her domestic needs. Canadian manufacturers will be demanding export markets and will maintain with a certain justice that they cannot permit large imports of British manufactures. Moreover, the old established agricultural and extractive industries are all operating on the assumption that they can depend on export markets to accept the better portion of their output. This is bound not only seriously to complicate the problem of the control of Canada's foreign trade but also to intensify the conflict of regional interests in the development of national policy.

The war to some extent provides the remedies to its own problems, because the common war effort is breeding a national loyalty and the nature of the economic organisation of the war has vastly increased the powers of the federal government. But the growth of this power in the centre has its dangers as well as its promises for the future. Many of the emergency powers cannot be retained by the Dominion after the war without constitutional change, and the political climate may not be propitious for constitutional amendment. A central government in any federation of our day may use its growing powers to curb class and regional privilege and ambition and to promote the welfare of the common citizen and the common interest of all regions, or it may lend itself as pander to the dominant economic groups and serve as their instrument to hold in check the centrifugal forces by authoritarian methods. In the Canadian federation the forces which the war has set in motion may yet raise this issue. How it will be composed must wait for history and, it may be, the outcome of the war to determine.