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on

A SURVEY OF CANADA'S FEDERAL INCOME AND EXPENDITURE.

by

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Chapter I Pre-Confederation

Any survey of Canada's federal finances must of necessity include some reference to the condition prevailing in the provinces of British North America prior to 1867. In all of these provinces customs revenue was the major source of government income and improvement in transportation and communication the major source of government expenditure. Particular reference will be made to the provinces of Upper and Lower Canada in this preliminary sketch of the background of our federal finances.

In 1840 the Act of Union between Upper and Lower Canada was passed by the British Parliament. Its main clauses with respect to fiscal matters provided for turning over of all hereditary or casual revenue from the Crown to the legislative assembly of the united province. This completed the assumption by the popular assembly of all revenues accruing from customs duties and casual dues for application at their discretion to the expenditures of the government. Customs revenues from duties imposed by imperial statutes had been paid into the provincial treasuries since 1831, by virtue of an act of the British parliament. In addition to this surrender of hereditary dues the Act of Union took the power of introducing money bills away from private members except by consent of the Governor General. A consolidated revenue fund was established to which all receipts were to be credited. The British Parliament expressly reserved to itself the right to impose duties and otherwise control the trade and commerce of the colony until 1842 when all colonies were permitted to alter or reduce the duties on foreign goods. In 1849 the imperial government repealed the restrictive navigation laws and so freed the St. Lawrence River to all vessels. From this time on the Legislative Assembly in Canada exercised complete control over government receipts and expenditures.

The main revenue receipts of the united province were, as was indicated above, derived from duties on imports and excise revenues. This reliance on indirect taxation was accepted popularly as the best method since direct taxation was considered to be "as repulsive to the Canadian as to the American mind."[1] Duties on imports were levied to pay interest charges on British capital invested in railroads. The great imports of capital for the construction of railroads created a very serious situation for the government. The railroads stimulated industry and agriculture, and increased imports, and therefore revenues. But the effects of the Crimean War, the slow returns on railroad investments, bad harvests and the depression of 1857 and 1858 meant that exports were fluctuating and declining, and with this trend in exports, imports and revenues also declined. As one writer at the time put it "A diminished demand for our staple products has produced a corresponding check upon the purchasing power of our people and a corresponding loss to the principal sources of our revenues."[2] From 1841 - 1867, four-fifths of the receipts of the Province of Canada were obtained from customs duties,[3] and their decline meant continual government deficits. Through the early sixties the deficit increased due to a decrease in revenues. Since the deficits of the government were due to heavy fixed charges caused by railway and canal building, together with a decline in customs revenues, the remedy seemed to lie in increased traffic on canals and railways, which would cure both causes of government deficits. That is, increased traffic would mean greater earnings by such services and so lessen the fixed charges borne by the government,

1. p. 24 Innes Sel. Doc.
2. p. 645 Ibid
3. p. 36 V & W.

while, at the same time, an increase in traffic would mean greater imports, and so greater customs and excise revenues. Many schemes were advanced to achieve this end, but the most effective was Confederation.[1]

CONFEDERATION

The British North America Act, 1867, was the result of many conferences among leaders of the various provinces of British North America. The financial arrangements between the provinces and the new Federal Government constituted one of the most serious problems facing the "Fathers of Confederation." Prior to the federation period the separate provinces, as we have seen, derived the bulk of their revenue from customs and excise duties. Federation called for a distribution of governmental services between the Dominion and the provinces, and a corresponding division of sources of public revenue for the maintenance of these services. The results of the deliberations in this regard found the Dominion Government assuming the management, control and expense of the public works existing in each province, which were obviously of benefit to all.[2] In regard to debt, it was agreed that the Central Government should assume all debts and liabilities of each province on a per capita "allowed" debt, which was meant to preserve equity among the amounts passed onto the Dominion Government by the various provinces.[3] The granting to the Federal government of the power to raise money by any or all means or systems of taxation[4] involved a further arrangement by which provincial revenues could be maintained when their chief source, customs revenue, was no longer

1. p. 215 H.L.Innes
2. p. 3 A. W. Boos
3. p. 5 Ibid
4. p. 7 Ibid

available. The final arrangement arrived at was a payment by the Dominion to the provinces which took the form of (a) interest on debt allowance, (b) grants paid annually to the several provinces for the support of their governments, and (c) grants-in-aid made annually on a per capita basis.[1] These provincial subsidies", as they came to be called, have proven an ever present bone of contention between the various provinces, and the Dominion government, and to-day the most serious menace to the Dominion is the bitter sectionality which has grown as a result of this solution of the problem of division of taxing powers.

The fiscal system established by the B.N.A. act provided for a consolidated fund to which was to be accredited and out of which was to be paid those revenues and expenditures which are usually to be found in supplying government services -- i.e. "ordinary" receipts and expenditures. In addition there are miscellaneous accounts dealing with loans, debt redemption, railway administration, capital expenditure on public works, and a variety of other subjects.

"Consolidated Fund Receipts" are classified under two main heads, tax revenue and non-tax revenue. The latter class may be left out of our consideration since it consists of revenues from government services such as the post office which usually approximate closely to expenditure on such services. Tax revenues are further classified on three bases -- i.e. customs duties, excise duties, war-tax revenue, which includes income tax and sales tax, and other taxes first imposed during the Great War.

Federal Expenditures are divided into Consolidated Fund Expenditures, Capital Expenditures and Other Expenditures. The first are "ordinary" expenditures covering the cost of usual government services, debt charges and

1. Canadian Forum Nov. 34 N.M.Rogers
   "Crisis in Federal Finance"

so on. The second includes outlays of a capital nature on canals, railways, public works and such enterprises of the Federal Government. The last class includes expenditures on "Railway Subsidies" (Negligible since 1920), War and Demobilization Charges since 1915, and miscellaneous charges to which the distinction between capital and revenue expenditures has not been subject to hard and fast rules.

CHAPTER II SURVEY OF FEDERAL INCOME AND EXPENDITURE 1867 - 1900

1. The following survey of federal revenue and expenditures is divided into periods of years which vary from 7 to 13 in length. The division is merely one of convenience -- a means of simplifying the survey. The method followed is somewhat varied, also, due to the differences in relative importance of the various periods. For the earlier years of the Dominions' history, the different periods are treated as single phases with only incidental references to any particular year. After 1900, the important yearly changes were held to be worthy of more specific consideration, so yearly changes were given more attention. The war period and the post-war years up to the present were also considered on a year to year plan rather than as single phases since the very fact of their closeness to the present ensures that a year to year discussion will give a fair indication of the general outline of each period.

The method followed in considering each period is as follows in general: the salient features of economic activity are outlined and some estimation is made or implied as to the conditions of the people -- i.e. whether they are prosper~~i~~ous, or the reverse, etc; following this economic survey the outstanding features of federal economic survey the outstanding features of federal income and expenditure are presented.

I 1867 - 1873

Following Confederation a somewhat peculiar state of affairs existed in the new Dominion. There was the shell of a great state, the institutions and machinery of a country which stretched in nominal union from ocean to ocean and covered three million square miles of territory. But the population was thinly scattered over its vast area; the progress of national prosperity was slow; the Provinces leaned considerably in matters of trade and exchange both socially and economically upon the states to the South; railway communication between the Pacific and the Great Lakes had not been established, and lack of it seemed an almost insurmountable obstacle to the eager growth of this youthful nation. Despite the very definite pushing of programmes of expansion in transportation and communication comparatively little exchange of thought or commerce passed as yet between the provinces.

The Ministers of Finance after Confederation had been compelled to evolve a new financial system to bring together varied threads of conflicting Provincial experience; to create a new and broad fiscal policy suited to several Provinces, and many diverse interests, and build up a Dominion banking system. It was not an easy task. The country from ocean to ocean also had to be considered and studied in its public works, its possible public improvements, its vast requirements for transportation facilities, its complex and antagonistic railway and waterway systems. Intricate questions of revenue, of relations between the new federal government and the Provinces and with the United States and the Mother Country had to be considered. Difficult constitutional and administrative points in connection with the admission of new Provinces had to be met, the wants of vast areas of the far West satisfied from time to time, the Indians looked after and controlled, the whole postal system of half a continent organized or reorganized.

The first two years of Confederation saw the new federal government putting forth all its endeavors to meet successfully the problems outlined above. In spite of the abrogation of the Reciprocity Treaty in 1866, the American Civil War and its effects -- the withdrawing from productive enterprise of many thousand of men in the States and the enormous destruction which the war entailed -- brought a demand even at enhanced prices for Canadian goods, which was of great aid in the first trying years of the Dominion. The change from a pioneer community, with practically only exports of timber in the world market, to an important commercial and financial country which was becoming apparent with the signing of Reciprocity, became still more visible with a national structure seeking a place in the sun. The growth of trade with the States and the expansive development of all contemporary projects which marked the early 50's returned with renewed vigor after the setback of late years of that decade. By the time Confederation was completed the early stages of general economic reanimation were passed and the stage was set for a progressive development of all institutions of the new nation.

The expansion, to some extent artificial, that took place in Canada in 1867-73 had gone on keeping pace in some degree with the tremendous development of the American West, following the Civil War. Canadian manufacturers had benefitted greatly by the preoccupation south of the border in the absorbing struggle between the North and the South. The cessation of production in the States has been mentioned above, and the return of full powers of their productive capacity had not as yet brought any repercussions in Canada.

During these years the small 15% tariff was enough to prevent serious competition with the tiny and still tentative industrial development of Canada, although it was not protective in the sense of encouraging home industry. From 1868 to 1873 Canadian exports to the States increased by 50% to 36 millions, while her imports from the same country doubled, reaching a total value of 45 million in the last year of this period.

Prices which had been high since the Crimean War continued at a high level during the American Civil War but started on a slight but distinct decline in 1867, largely due to the termination of hostilities in the latter struggle. Agricultural products suffered in large degrees in this recession, which saw the price index fall from 120.1 in '68 to 117.3 in '69 (1900 = 100) Other commodities were firmer until in 1869 the great rise began that carried prices to a very high point in 1872 - 3 - 4. Many factors contributed to this rise in the price level, which reflected the world-wide rise in these years. Railroad building in the United States and in Europe, the opening of the Suez Canal, and the outbreak of the Franco-Prussian War stimulated prices in their respective ways. The boom continued until the great collapse in Wall Street in September 1873.

Immigration figures are an indirect prosperity barometer which in the years in question illustrate the rising trend of ecomomic activity. In the calendar year 1867, 14,666 immigrants settled in Canada. The number decreased slightly in 1868 then rose swiftly to 50,050 in 1873, the highest tide of influx until the year 1882.

Some reference to the financial problems facing the new federal government has been made above. The methods used and results attained are the questions to be answered. The accounting forms and methods have been outlined and also the nature of public federal revenues has been explained -- i.e.

i. e. practically sole dependence on "indirect" taxation by customs and excise duties. With these facts in mind the course of the federal fiscal system can be sketched.

The rise in the price level in conjunction with increasing external trade was very favorable a factor for the youthful Dominion's income. Based as it was largely on import duties, many of which were of the "ad valorem" type, the federal ministries in the first years after Confederation were fortunate in having at their disposal an ever increasing flow of funds with which to meet the pressing needs of the newly formed nation. The fondest hopes of its "Fathers" were fulfilled as far as fiscal matters were concerned in this period of prosperity, during which a substantial surplus was the usual thing in each budget. The reliance for revenue on customs duties with corresponding excise duties seemed to have been established as the best method of deriving federal funds. Customs duties rose from $8,518,000 in 1868 to $12,954,000 in 1873, and constituted almost 3/4 of all federal income. The remainder came largely from the internal duties on tobaccos, etc., which by 1873 reached $4,460,000 -- an increase of 1/3 over the amount received in 1868. Total receipts on the Consolidated Fund Account increased steadily as a consequence, reaching almost 21 million dollars in 1873.

Current or ordinary expenditures in this period exhibit the characteristics of such disbursements that are to be expected in the light of the political set up then existing. Quite obviously the first minister of finance, Hon. T. A. Galt, was content to feel his way to obtain a complete knowledge of the tasks confronting him before any sort of financial policy was embarked upon. Reassured by the steady increase in revenue receipts a programme of public works was entered upon in 1871 and pushed forward rapidly. The postal service was organised and extended and the beginning was made on the building or acquiring of suitable federal buildings in the leading centres. One serious defect in the current accounts which became more noticeable in the depression of the middle 70's was the tendency of fixed charges to predominate in ordinary expenditures. This was unavoidable due to the assumption of debt by the federal government and the payment of the provincial subsidies, but instead of seeking alleviation it was let slide and became a heavy burden in times of depression.

Capital outlays reveal the procedure followed with regard to the north-west, transportation, etc., by the first government. Substantial amounts were applied to canal building and deepening, railroad building and development of the North West Territories. A large increase in the amount appearing as "debts allowed to the provinces" came in '73 when these allowances were re-adjusted so that a larger proportion was borne by the Dominion. Total capital expenditures reached the huge total of $19,889,000 in 1873 but over $15,000,000 occurred in the increased provincial debt allowances.

The government of the day which was charged with lavish expenditure and extravagance by the Opposition preferred to call it a "generous" policy suited to the country's needs. There is no doubt of the necessity of much expenditure in a newly formed nation, but the tendency to spend without stint, which was a natural result of the over sufficiency of income from customs duties in times of prosperity, marked this as all subsequent periods in which government revenues came largely from this source.

II 1873 - 1880

The panic of September 1873 produced a disastrous setback in Canada, and the already bad business conditions were far from improved by the ceaseless cutthroat competition waged by American exporters in the Canadian market. By 1872 it was becoming apparent that the United States had fully recuperated in regard to industrial and agricultural production from the ill effects of the Civil War. American manufacturers had revived, prospered, then over produced. They had supplied their own market then turned to the nearest and most exposed of other fields, which was the Canadian. Canada, in the word of the day, became a "slaughter" market, swamped with goods offered at ruthlessly cut prices by American exporters. The small Canadian firms could not hope to meet this competition, and many were forced to the wall. The depression which followed the overexpansion of the years '70,1-2-3 was far reaching in its effects. Banks closed their doors and a severe commercial reaction set in which was made even more severe by the dumping of American goods. Misery was heaped on misery when an agricultural depression set in parallelling that in the United States in the middle 70's. The situation became so bad that in 1876 a Commission of Inquiry into the existing conditions of affairs was appointed. Under the chairmanship of Mr. I. David Mills a Report was submitted admitting the financial stringency and the industrial depression but condemning the adoption of protection which had been advocated as a cure by the Opposition. The reasons for this policy were that such a system would diminish the consumption of foreign goods, would lessen the revenue by $9,000,000, would increase the price of home manufactured goods, would impose a heavy tax on the consumer and was generally a proposition to relieve distress by re-distribution of property. Meanwhile matters went from bad to worse in a commercial and financial sense.

High duties restricted the entrance of Canadian goods ~~on~~ into the United States' markets while similar U. S. goods entered Canada free or with small duty. The financial stringency is shown by the decline in value of imports of British goods from 68,000,000 in 1873 to 37,000,000 in 1878.

The drop in prices after the panic of 1873 was sweeping the index of wholesale prices falling from 129.7 in 1873 to 103.2 in 1878. The fall in prices and the decrease in demand brought a sharp decline in import values from the record height of 124.5 million dollars in 1873 to 78.7 million in 1879. Export totals in the same years fell from 86 millions to 71 millions.

The heavy blow taken by Canada in this period is clearly seen in immigration figures, which reveal that the number settling in Canada fell off sharply after 1873. In the calendar year 1876 only 26,000 people settled in Canada -- just over half the number who settled in 1873. This period of depression presented a problem to the government in that revenue receipts fell off due to the decline in customs revenues. The favorable large income from ad valorem customs duties that accrued in the prosperous years of '71-2-3 was replaced by a diminution that a fall in prices and decreased purchasing power tended to magnify. Customs receipts throughout this period continued to hold at a high level until 1876, when they declined by 2.5 millions to 84% of the previous years total. Excise duties and other receipts declined slightly but the main cause of the insufficiency of revenue which led to considerable deficits in 1876-7-8 was the inelasticity of custom's revenue. The cry for increased taxation to cover these deficits was met by the Minister of Finance in the Budget Speech of 1878. The following extracts reveal the position taken by the government.

"I would say that if we possessed in Canada any tax equivalent to the income tax now in use in England, I would not hesitate to advise the House to have recourse to that means of increasing revenue.".....while increased taxation (customs and excise) if carried to any great extent, might defeat its own purpose not only by stopping the growth of this country but also by diminishing consumption and encouraging smuggling."

The above grounds were considered to be sufficient bases for postponement of any increase in tariffs while the avowed policy was to minimize expenditures and trust in probably surpluses of more prosperous years to cover the deficits of the years of adversity. The minister stated that in comparison with other countries somewhat similarly situated Canada's taxation was not only durable but lighter than some, and that the natural growth of the country would even with so light a burden soon provide sufficient revenue for all needs.

The sharp reduction in income was a serious embarassment to the government which was faced with heavy expenditures on ordinary account that practically first mortgages "out of a total nominal expenditure in round numbers of $23,500,000 no less than $11,500,000 are devoted to payment of interest, Sinking Fund and Subsidies to Provinces and must be considered as absolutely a first mortgage."[1] In addition to this large total a further $5,500,000 occurred either as cross-entries or as being to all intents and purposes a mortgage also, leaving only $7,000,000 in the form of controllable expenditure. This disproportion meant that only a small field was left in which to exercise any great economy. The condition of affairs was still more grave in view of the fact that the current expenditure was barely sufficient to discharge the purposes necessary.

Economy in ordinary expenditure had been instituted when declining revenues had become a fact, and the policy of economy was continued until 1880. Restriction on expenditures was not pushed beyond reason since as was stated further economy could only be had if "we submit to very important alterations in our

1. Budget speech'78 p.19.

present constitutional system, which would be both difficult and of doubtful expediency."[1] This latter is no doubt a reference to the possibility of reducing provincial subsidies which had grown to be the second largest item of expense, taking approximately 16% of total ordinary expenditures.

Continual pressure first by one province, then by another, for more assistance led to a bleeding of the federal treasury to meet these demands. British Columbia sought and obtained funds for her public works in 1874, Manitoba in 1875 became embarrassed and sought aid similar to that previously given to New Brunswick and Nova Scotia. Her case was scarcely disposed of when the Maritime Provinces felt a similar need for succor from the federal strong box.

Capital expenditures which aside from debt allowances to the provinces had amounted to approximately 7,000,000 per year since 1872 were kept at this level. The main outlays of this nature were for extension of communications and transportation by deepening canals and building railways.

1. Ibid p.20

III 1880 - 1890

The year 1880 stands out in Canada's history in bold outline. It was a year of innovation which saw a young nation, merely 13 years of age as such, promise to complete a transcontinental railway in 10 years, and it also marked the imposition of a system of import duties designed to protect home markets for home industries. The decade opened auspiciously with an abundant harvest in 1880 which was a forerunner of the boom of the opening years of this period. The construction of the C.P.R.,which was given added impetus after 1880,caused a boom in all forms of activity, which was reflected in many different ways. Prices were fairly steady until 1883, when the decline caused by the inadequate increase in the world production of gold began. Aggregate external trade boomed with the great expenditures on railroad and other construction, but declined after the first flush of activity died away in 1884. Population figures show the same activity -- a great influx of immigrants in the first three years, and a sharp reduction in their number in the period of reaction. That Canada's population increased by only 525,000 in this decade, while there were almost 900,000 immigrant arrivals is a fact that is explained by the reaction and depression following 1883, and also by the grants of free land in the north-west portion of the United States, which drew many Canadians. The period as a whole was one of continued but moderate growth in all forms of economic activity.

The introduction of the "National Policy" in 1880 marks the beginning of a system of protection for Canadian industry that has been followed in practice ever since. This policy has had a very great effect on Canada's federal finances due to the large part customs revenue play in the federal fiscal system.

The graph shows the effect of the rise of advaloren duty rates from the average of 13% on total imports in the years prior to 1880 to an average of 20%, 1880-1890. This increase in rates together with a huge increase in imports provided the government with an over usficient income and involved the necessity of some disposal of it. Custom's revenues had swollen to almost 24 million dollars in 1890, and this was an increase of 10 millions in ten years. Excise revenues increased by 3 millions, while total revenue receipts soared to $39,879,000 in 1880, or $8.34 for every man, woman and child in the Dominion.

Ordinary expenditures which had been quite stable from 1874 to 1880 were rapidly increased at a rate of 2 million dollars each year to 1886, but a reduction followed from the level of 39 millions reached in that year, to 36 millions at the end of the decade. This increase in expenditure was consistent with the expansion of the nation's affairs, but is interesting inasmuch as we note that interest charges on the debt due to capital expenditure on the C.P.R. consumed $2,000,000 of the increase or an amount equal to twice the increased expenditure on public works in the same period. Other items of expenditure show no startling increases but do show a steady growth.

Capital expenditures during this decade have been subjected to keen criticism both by contemporary writers and politicians and others after them. The promise to British Columbia to build a transcontinental railway as a condition to its entrance into Confederation has been acclaimed as a factor in the welding of the Dominion, and in other glowing terms. That it was of importance in uniting the east and west both economically and nationally cannot be denied, but the entrance upon such an undertaking by an adolescent nation was without doubt extravagant beyond reason. The huge burden of debt incurred as to be paid off by the great increase in trade and commerce between the east and the west, aided by the influx of people to the western areas. This expansion was handicapped however by the government land policy, which favored a few large companies and by their method of giving land subsidies to the railroad in the form of large alternate blocks along the railway.[1] It has been estimated that in the decade 1881 - 1892, 100 million dollars were spent in developing the country (notably the North West) and in aiding settlement.

Total expenditure more than kept pace with the rapid increase in income and this decade saw Canada's net debt increased from 152.4 millions to 237.5 millions -- an increase of almost $14 per capita.

1890 - 1900

The worldwide depression that began in 1880 and continued to 1895 struck Canada a heavy blow. The balloon of inflation that accompanied the building of the C.P.R. was decisively deflated by a decline in prices and in purchasing power. The bllom of manufacturing that grew under the favorable elements of the National Policy and the boom of the early 80's proved to be a hothouse variety that withered under the wide spread commercial depression. The rapid settlement of the prairies which was forecast as a result of completion of the transcontinental railway failed to materialize. Immigration declined, thousands of people crossed the border into the United States, and Canada was in the throes of the worst depression in her pre-war history.

In 1886 the Liberal Government was swept into power on a promise to reduce tariffs and on the sentiment that an opposition party always gains in a period of depression. The high protection was not removed but was modified by the introduction of the British Preference, leaving the rural population still dissatisfied. A new immigration policy was inaugurated and pushed vigorously by the government whose work was aided by the return of more prosperous conditions. Prices rose, imports increased by over 70%, exports followed suit. Everything was swung decisively upward, introducing the greatest and most spectacular expansion in

1. Social and Economic Conditions in Canada p.38.

Canada's history.

The graph showing the course of federal income illustrates the close correlation between the price level and other factors in the value of imports, and the total revenue receipts. From 1890 - 95 customs revenues declined by over six millions and total revenue by practically the same number of dollars. The drop in customs revenue was in large part due to the decrease in the value of imports, the effect of which was heightened by the change of many duties from a specific to an advaloren basis in 1892. Another factor contributing to this decline was the increase in the quantity of free goods entering that were formerly dutiable. Excise revenue increased slightly over this five year period, and the net surplus of $7,500,00 was largely due to this increase coupled with the maintenance of ordinary expenditure at approximately $37,000,000 for this period. The economy in ordinary expenditure (since 1887 a rise of only $2,000,000) was instituted in capital account also to the extent that it was cut to the lowest level since 1871 and 2.

The bottom of the depression, insofar as public finance data indicate, was reached in 1895. In the following year, although prices declined further, imports and exports were increased. After a pause at the 1896 level throughout 1897, the upward trend was continued at rapid pace to 1900. Customs revenue varied with the value of imports rising from just under 18 million dollars in 1895 to over 28 million in 1900. Excise revenue increased over the five year peiod by two million dollars, which, with customs and other receipts, gave a total of $52,029,000 for use in federal expenditures in 1900.

Expenditures on the Consolidated Fund rose slowly but steadily from 38 million to 43 million —— an average increase lf $1,000,000 per year. Capital expenditure was steady at approximately $3,000,000 per year, until 1897 when the vigorous pursual of expansion in the west brought the yearly totals up to 6 and

7 million dollars.

CHAPTER III

THE " DECAS MIRABILIS" 1900 - 1913

The opening decade of the twentieth century marks the adoption of a programme of expansion unique in Canada's history. Filling the vacant West with human beings was the end sought, and to further its attainment many devices were used. The principal methods were the granting of free land by the government and the development of communication and transportation by lavish expenditures on government and privately built railways by means of public grants and subsidies.

The munificence of the Federal Government inspired similar policies by provincial and municipal governments, and by private individuals and companies. A vast programme of construction was started, immense railroad systems, elaborate irrigation projects, public services of all sorts, road and highways, all forms of construction were undertaken. Under such forced growth, land values soared, and an orgy of speculation in real estate began.

Population increased rapidly due to the response to the government's immigration policy. A disappointing feature of this growth in population to those who wanted to develop a large agricultural population was the enormous increase in urban population. This tendency toward urbanization meant that the cost of living rose sharply and a more "artificial" mode of life prevailed.[1]

The vast capital expenditures required funds of unlimited size, far beyond any that Canada herself could supply, so recourse was had to borrowing. This borrowing, mainly from Great Britain, took the form of commodity and machinery imports, as well as capital, so a huge increase in imports resulted. Govern-

1. Soc. and Econ. Conditions in Canada P.42.
2. Viner

ment expenditures took only part of this importation of capital which rose from a few million dollars in 1900 to almost half a billion in 1913, and amounting, for the period, to over two billion dollars.[1] In addition addition to the various governments, private individuals, corporations and all sorts of companies were building factories and homes, opening real estate divisions, and speculating in land. High prices and ever increasing demands from a rapidly gorwing population meant high and regular profits to manufacturers of all kinds of goods so factories were built and extended continually.

General prosperity, buoyand rents, and high profits marked this golden age in Canada's economic history, but the decade contained in itself the source of it's downfall. The debauch of land speculation which no government bothered to check had its inevitable result in the crash of 1913. The financial stringency of world wide proportion, which began in 1912, caused a restriction in commercial credit, and a limitation in the supply of capital in international markets open for Canadian borrowing. The Balkam Wars were the main cause of this restriction, which was reflected by the drop in imports into Canada from 671 million in 1913 to 619 million in 1914.[2] This check on expansion, together with the collapse of the land boom, caused a general business reaction and a slackening in trade.

The financial history of the federal government during this period is worthy of close study, but only the main features can be notes here. Ordinary revenues increased at an amazing rate, reflecting the enormous increase in business, and more especially the phenomenal increase in imports. The enormous influx of goods to meet the ever growing needs of commerce and industry, further increased by a rapid growth in population, accounted for a rise in the value of

1. Viner

2. White p.11

imports from 172.6 million in 1900 to 671.2 million in 1913. This huge increase in value under advalorem duties that averaged 16.6% of total imports, meant an increase in custom's revenue from 28 millions in 1900 to 111 millions in 1913, an increase in 13 years of 260%. Excise duties more than doubled with the growth of general business, and they, with custom's revenue, were responsible for a growth of $117,500,000 in total revenue receipts in the 13 years under consideration.

The graph shows two distinct set-backs in this phenomenal growth, the first due to the change in computing the fiscal year, which was made in 1907, and the second due to a financial stringency in 1908, that caused a sharp decline in imports in 1909.

The huge income accruing to the Consolidated Fund was readily spent by the government, which managed to add $49,000,000 to the net public debt, although in the same period net surpluses amounted to $265,000,000 in the aggregate.

The main outlay was, as we have seen, on capital account, but ordinary expenditures were increased by 160%, although only in 1909 did they approximate to ordinary revenue. The increase in ordinary expenditure was mainly due to the founding of Alberta and Saskatchewan, which increased the amount of provincial subsidies by about $1,300000. Desire of the several provincial governments to share in the enormous revenues accruing in each year to the federal government sharpened "the determination to obtain a general upward readjustment of the provincial subsidies."[1] This revision was made in a conference in 1906 and as a result, expenditures on this account rose to 9 millions in 1908 and to 13.7 millions in 1913, by virtue of the increase of population on which the subsidies were based. Debt charges of course increased with the in-

1. Boos, p.50

crease in the public debt, but all other increases in the ordinary accounts were thrown into the shade by the public works account (Consolidated Fund). This item of current ordinary expenditure, which had amounted to less than $2,000,000 per year, since 1890, came to life with a vengeance by increasing to $12,300000 in 1909. The monitary crisis of 1908 brought the introduction of some economies but by 1913 the ordinary expenditure for public works amounted to $13,500,000.

The increase of 69 millions in ordinary expenditure in 13 years couldn't take care of the superfluous income, so recourse was had to capital expenditure. The National Transcontinental Railway (including the Quebec Bridge) took $155,000,000 in the first 10 years of its existence. Other items of capital expenditure show no extraordinary features, except for miscellaneous public works on which, in 1913, over $6,000,000 were expended, almost six times the amount spent in 1900.

The over-expansion of railroads in this period gave rise to the serious railway problem that necessitated the formation of the Canadian National System, during the War. Duplication of services far beyond the needs of the country are still a problem of grave concern to the government, and to private companies. With huge yearly deficits on operation accounts, this result of the wild expansion of this golden decade is a crushing burden on our federal fiscal system today, and relief is still only a possibility, not a probability.

CHAPTER IV

1913 - 1920 THE GREAT WAR

A world wide financial stringency marked the pre-war years of 1912 - 13. Constantly increasing expenditures on armaments and militarism, the exhausting Balkan Wars and personal and public extravagance, speculation and price inflation, all co-operated to bring financial embarrassment. The check on loans available for construction in Canada was a good thing in that expansion had been carried far beyond the bounds of prudence. The slowing down of the influx of British capital showed in steadily declining imports. Though restricted, they amounted to $255,000,000 in bonds alone. Banks did not suffer from stringency greatly.

The business reaction was intensified by the outbreak of the Great War in 1914, which brought in its train unsettlement in business, industrial slackness and unemployment. The latter was much in evidence in the winter of 1914-15, and the Government was faced with the necessity not only of organizing, equipping, transporting and maintaining the first contingent, but also provision of work to reduce the large number of unemployed. Public works programmes were pushed forward as rapidly as possible, including much railway, canal and other construction.

To favor rehabilitation of general business, the government arranged with the banks that liberal credits would be allowed and commercial discount rates would not be increased.

In February, 1916, the Minister of Finance, in his Budget Speech, was able to speak as follows: "Business has adjusted itself in a remarkable way to the altered conditions. We have been blessed with a most bountiful harvest--the greatest by far in the history of the Dominion, and this, coupled with the demand for war materials, supplies and munitions, has given such a stimulation and impetus to trade and industry that notwithstanding the war we are experiencing a high degree of prosperity.[1]

This was the year of the great wheat crop in the Canadian Northwest, and the year in which Canada began to manufacture munitions. Perhaps the most significant indication of the changed conditions was the alteration in the trade balance from an "unfavorable" balance of 36 millions in 1914-15, to a "favorable" balance of over 200 millions with a total trade of over 1200 millions, the largest in the history of the Dominion up to that time.

The influence of the war upon Canadian manufactures was profound and far reaching, tending to promote diversification of products and production for home consumption of many commodities formerly imported. On account of the practical suspension of importation of many manufactured good, Canadian producers had practical control of the market. This, with the great agricultural prosperity, produced by the unprecended prices of war time,meant that industry worked at high pressure to produce not only munitions and war supplies, but also to make the manifold varieties of goods required for the stimulated civilian consumption. The building of many new factories with greater efficiency and a higher degree of administrative ability established Canada in a new position, as one of the leading manufacturing nations of the world. The great boom in Canadian manufacturers continued to 1920, when it reached its height with a gross value of production of 3,772 millions which stood as a record high until 1929.

Employment was excellent and wages were rising rapidly; in the munitions services they reached unheard of levels. The "cost of living" in Canada during the war period rose by 100% from 1914 - 1920, but the preoccupation of the people with the serious problems of the war meant that it was given little public attention.

1. Budget Speech 1916 - p.9.

Prices as the above indicates rose sharply from an index of 131.3 in 1914 (1900 - 100) to an indix of 287.5 in 1920.

Immigration fell off sharply in total numbers 8556 - 7879 = 677 from 1914 to 1918, in response to the increased demand for labor.

It was clear by the opening of 1915 that large additional sources of revenue were a most pressing necessity. Industry and general business were still suffering from the initial shock of war and customs revenues had declined heavily from 111.7 millions in 1913 to 75.9 millions in 1915. At this time the British treasury was supporting not only the cost of our war expenditure, but also that of public works in the Dominion designed to relieve unemployment. This situation obviously could not go on. The year 1914 - 15 saw a deficit of $2,500,000, the first since 1897. To raise additional revenue the Budget of 1915 levied special taxes on banks, trust insurance, loan companies, on sleeping car tickets, steam boat tickets, upon cheques and bills of exchange, express and post office money orders and increased the postal rates on letters and postcards. Wines, patent medicines and perfumery were also taxed while liquors, cigars, cigarettes and tobaccos had been dealt with at the special session of August 1914.

These luxury taxes were only a part of the means of raising additional revenue. The main fiscal measure was a uniform increase in general customs duties of 7½% on the general rate, and of 5% in British Preferential rate, staple foodstuffs and anthracite coal were excepted.

This indiscriminate raising of duties was excused on the plea of urgency and the immediate result of it was to increase national revenue.

The first domestic Canadian War Loan of 50 millions was floated in November 1915, and completely upset the opinion of leading financial experts who under-estimated the amount of funds available for such investment. It is true that the loan was loaded with all the possible extras to make it more appealing, such as a tax-free privilege, and a privilege of conversion at issue price to any succeeding Canadian domestic issue. The issue was energetically supported by all financial houses and banks and was over subscribed by fifty million dollars. The extra fifty millions were used to establish credits in Canada for Great Britain, and the confinement of the issue to fifty million was overcome by application to the bond-holders for an increase of its allotment to 100 million. In 1916 and 1917, two further loans were made and both were over subscribed -- the first by one hundred million over the one hundred million sought, and the second by one hundred million over the one hundred and fifty million sought.

The feature of the Budget of 1916 was the Business Profits War Tax which provided for the taking off a percentage of profits of companies, firms and persons carrying on business in Canada. Large profits had been made due to enhanced prices of stocks held at the outbreak of the war, Public opinion demanded that some portion of these unearned increments should be applied to the public expenses in a time of stress and strain. This was the main reason with, of course, the necessity of increased revenues for the imposition of this tax. Under normal conditions, such a tax is unsound, since it leads to evasion by "ploughing in" and excessive advertising, as well as discouraging enterprise and efficiency in administration if graded too steeply. With improving conditions and the increase in taxation in 1916, revenue rose to one hundred and seventy million, and the consolidated fund account showed a surplus of almost 42 millions. This was applied to capital and war expenditures, which were met with two loans. One loan was 100 millions and a New York loan was 75 millions.

The year 1917 was the most trying period of the war while it marked the entry of the entry of the United States on the side of the Allies, it was the year of the Russian revolution and subsequent collapse. The German submarine campaign was at its height, and in order to preserve food for shipment overseas Canada was placed upon rations. Conscription was introduced,and in all a spirit of sacrifice and self denial was prevalent. This popular feeling demanded increased taxation, partly due to the failure of some of the well-to-do to contribute generously to patriotic and war funds. In response to this desire, the Business Profits War Tax was made much more drastic. It was increased from the former rate of $\frac{1}{4}$ of net profits over 7% and 10% for corporations and private firms respectively, to $\frac{1}{4}$ of such excess profits up to 15%, $\frac{1}{2}$ on 15-20%, and $\frac{3}{4}$ on any over 20%.

This same year saw the passing of the Income Tax Bill which marked a distinct step forward in federal public finance. The bill had been drafted in 1916, but the minister of finance had not wished to bring it in until absolutely necessary since it was not desired to have direct taxation in Canada heavier than in the States. "This is a maxim, which, on account of Canada being a country inviting immigration and business enterprise, I think should be observed as nearly as may be.[1]

Many difficulties had to be faced in imposing an income tax. Organization and administration over so vast an area and so scarce a population was difficult. Moreover, several provinces and municipalities were already using such taxation and the imposition of a federal tax would not only be confusing but would involve a heavy aggregate. However, rapidly mounting expenditures of the war, and the necessity for revenue, made it imperative that such tax ation be imposed. Another factor was that increased taxation on luxuries, such as wines, could only be had by breaking a treaty with France, which was considered inadvisable.

At this time, not only were war expenditures being met but also large credits were being given to Great Britain, in order to permit her to buy Canadian goods and war materials. Twenty-five millions per month were being lent to Great Britain, as well as ten millions for ship building being carried on in Canadian yards.

1. Story of Can. War Fin. p. 54

Thus a large part of government expenditure was immediately returned to Canadians in the form of wages, and in purchase of raw materials. The third domestic loan of 1917 of one hundred and fifty millions and one hundred millions secured in New York on two year notes were used for establishing British credits in Canada. An additional fifty millions was borrowed on collateral given by the British treasury and a portion of the first Victory Loan issued in the latter part of 1917 was also used for the above purpose.

"Canada's business literally depended on her ability to finance the greater part of our external trade."[1] To meet this requirement the three Victory Loans of 1917, 18, 19 were floated and raised 1700 million dollars. These sums were the foundation of the enormous volume of business done in these years in Canada. Great Britain's credits in Canada were used for purchase of particular products such as munitions, foodstuffs, ships, airplanes and money was distributed among all classes in the fomr of wages, rents, purchases, etc. In effect it was taking a dollar out of the bank one day and returning it the next as far as the public was concerned.

For the fiscal year 1917, ending March 1, 1917, under the enormous expansion of trade, the revenue rose higher than ever to the record total of $232,701,294 - an increase of 100 million over the 1915 total and giving a surplus of 84 million, more than double that of the previous year. In 1910, revenue first exceeded $100,000,000, in 1917, it exceeded $200,000,000. The greatest increase accrued in the item for customs, the receipts from which in 1916-17, viz. 134,043,742. exceeded the total revenue of the country in 1914 -15. In his Budget Speech of April 24, 1917, the Minister of Finance stated that during the fiscal year 1916-17 the revenue had enabled the country to pay from income all current and capital expenditure, all interest charges upon increased national debt, all pension out-

1. Story of Can. War Fin. p61

lays, and in addition, to devote the sum of $60,000,000 to payment of the principal of war expenditure.[1]

In 1917 - 18, the imposition of the income tax, with other taxes, and the large volume of trade, resulted in an increase of revenue receipts to almost 261 millions. Ordinary and capital expenditure took about 222 millions, which meant that after meeting all outlays, 40 millions were left to be applied to war expenditures. The main increase in items of expenditure were interest payments of $47,800,000 -- an increase of $12,000,000 and increase of $6,000,000 in pensions. A capital expenditure of $32,000,000 was made in the account of the Canadian National Railway which was a necessary organization of transportation facilities.

Up to March 31, 1918, the total outlay for war was approximately $878,000,000. In 1917 and 1918, approximately $113,000,000 of surplus of ordinary receipts over ordinary and capital outlay were applied to war expenditure. Interest and pensions attributable to war and covering the entire war period amounted to approximately $75,000,000.

In 1918, the Business Profits War Tax was applied to companies and firms having a capital between $25,000 and $50,000, the latter figure being the previous minimum taxable. The income tax was substantially increased, and customs and excise duties were levied on a considerable range of articles of luxurious use or consumption. Special War Revenue Taxes on tickets for seats and berths were increased also.

The upward revision of all taxes and continued expansion throughout 1918 brought receipts of the Consolidated Fund up to approximately 313 millions in the fiscal year 1919 in spite of the unsettlement consequent to the Armistice. All receipt items were higher but the largest increase was in War Tax Revenue, which more than doubled due largely to the addition of over 9 millions from the income tax, and a further nine million from sales, transportation and such taxes. Ordinary expenditures increased by over 33% mainly for increased interest charges and pensions to which a total of $232,731,283.

The big problem of the day for both British and Canadian interests was to obtain money for the purchase of the Canadian wheat crop of 1918. Canada was thrown on her own resources in meeting this problem, and a solution was found in the second Victory Loan, which gave nearly seven hundred million dollars late in 1918. This money supplied credits for the purchase of Canada's wheat by Britain and also supplied funds to cope with the social and economic problems of demobilization and the cessation of production in munitions and other war industries.

The government distributed one hundred and thirty million dollars as gratuity to the soldiers in making available credits for the purchase of Canadian products by Britain and other foreign countries, in carrying on ship building, in giving large orders for rolling stock and making extensions to the national railway system, the transition period from war to peace was bridged with no serious trouble in the industrial world and no business or financial panic.

In 1919 repeal of the extra 5% advalorem added to the British preferential tariff in 1915 as a war measure was made. Partial repeal was also made in the case of the intermediate and general tariff of the excess of 7½% advalorem levied under the same act as the above increase. Free entry where such was reciprocated was given to wheat flour and potatoes, and general downward revision of duties was made.

The post war years were marked, as was stated above, by a record height of prices which, after the collapse of the boom of 1919, engrossed the people's attention due to the high cost of living (index 1920 = 202.3 with 1914 = 100) Exports dropped precipitously from the 1918 total and continued through 1920 at approximately 1,275,000,000 while imports rose sharply in 1920 to 1,060,000,000 and to 1,240,000,000 in 1921.

Consolidated Fund Receipts continued to rise through 1919 and reached a total of 350,000,000 in the fiscal year 1920. Every item of both taxation and other receipts showed an increase over the 1919 figures. Taxation totals increased by 37,000,000 to $233,000,000. The rise in imports despite an unfavorable exchange was a carry over of the disregard of price which the war period had impressed on the Canadian buyer, and resulted in an increase of $21,000,000 in customs revenues in the face of decreased tariff rates.

Current expenditure in 1920 was greater due to the necessity of acquiring the Grand Trunk Railway to provide Eastern Terminals for the national railway system, to prevent duplication of services and to avoid the insolvency of the Grand Trunk and consequent failure of transportation facilities in the regions it served. In addition to the increase in the capital outlays, above ordinary expenditures, increased by approximately 1/3 to almost three hundred and four million dollars. Heavier interest charges on the hugely increased national debt provided thirty of the increase of seventy one millions.

CHAPTER V.

The months immediately following the war found business in a state of uncertainty which was followed by a year of feverish activity ending in the spring of 1920. This period of inflation marked the end of the transition from war to peace and we may say 1921 and subsequent years were in large degree marked by economic activity controlled by normal influences. The war was a very important factor but its effect was now indirect, working through factors more specifically economic.

This period began with a decided slump in reaction to the post war inflation of 1919-20. The physical volume of business went sharply down reaching its lowest level, as revealed by the index prepared by the Dominion Bureau of Statistics, in the middle of 1921. At that time it was only 62% of the normal as determined by a long run trend for the period 1919 to 1935. Ther serious condition of the farm population resulting from the heavy decline in values of agricultural goods was influential in the reduced business activity. Other primary industries suffered from reduced prices but not to the same extent.

The lack of purchasing power as a consequence of a decline of 23% in the national income was a serious problem. The cessation of orders and fall in prices brought not only a universal dullness in manufacturing with many plants idle and few fully occupied but also heavy losses to wholesalers and retailers on their inventories. Index of wholesale prices dropped from 155.9 to 110 in 1921 while the retail prices index (including rents and costs of services) fell from 124.2 in 1920 to 109.2.

From the low of early summer of 1921 Canada began the climb which with, in spite of, temporary setbacks found her in 1929 at the height of the universal boom which prevailed through 1928 and 1929. The general business conditions rapidly improved during the latter part of 1921 and after a slight reaction early in 1922 continued the sharp upward trend reaching a new high level at the end of the year.

Canada's interval trade was substantially lower in 1922 than in either of the two preceeding years although the decline in prices was a large factor in the 37½ per cent drop in the value of aggregate trade. Internal trade statistics show business as being less "spotty" than in 1920 and 1921 in which years the artificial condition of unduly high prices of inventories had been a barrier to the return to normal of some businesses.

1923 went on record as slightly better, the index of the physical volume of business closely approximating to the normal trend of the 1919-1935 period. Trade totals indicate there was a greater activity which in the case of imports was largely due to the heavier buying of raw material. Canada's position as a world economic power was confirmed by the large increase in her export trade in the face of bitter complaints of unemployment abroad. The wholesale price index reflects the greater stability of the year rising only slightly from the level of the previous year. A feature of the year was the marked gain in the amount and value of building contracts awarded.

Small profits and a large volume of business characterized 1924. The only alternative to this was complete shut down (such were world economic conditions). The continual increase in farm acreage throughout these years testifies to the perserverance and courage of the farmers in spite of 3 years of low prices and small markets. A world shortage of farm products in 1924 meant better prices and also that some profits came to the farm population although there was a reduced yield. All primary industries were similarly benefitted and the activity in this group of industries was a great aid to business in general. In spite of advanced grain prices and in the primary industries general improvement the general trend was definitely downward. Stock prices, bank loans and the physical volume of business all revealed this trend. The buoyancy of the latter half of 1925 accounted for a higher activity than in either of the preceding years. The first six months had shown a continuance of the downward trend that had been in evidence since 1923. An excellent crop yield giving over $1,150,000,000 in returns was a basic factor in the latter months of the year. Employment subsequent to July was more active than in any time since 1923, especially in the manufacturing industries. Trade was buoyant with both imports and exports showing marked advances. The trade balance was decidedly "favorable" being in this respect 50% greater than in 1924. An expansion in credit and a rise in the prices of securities reflected the increasing confidence in the definite revival from the post-war depression.

The upward trend of economic activity that started definitely in 1925 continued at an increased rate in 1926. All branches of business commerce and construction were rapidly increasing in activity. Business as a whole showed a much better tone than in 1925 and increased production and quick turnover were the common to most industries. Although prices were somewhat lower than in 1925, employment and general activity indicated that a better state of affairs existed than in any year since 1920. Construction of homes, arterial highways and municipal improvements doubled the number employed in such work during the summer. Manufacturers felt the increased purchasing power and responded with a quite universal increase in production.

Canada's position as a world trader was completely established by 1926. In volume of trade she ranked fifth among the commercial nations of the world being surpassed by United States, Great Britain, France and Germany. In per capita trade she was seond only to New Zealand, while her per capita favorable balance, $29.34 was the largest in the world.

Record crops in the West that exceeded the high yelds of the previous year were the basis of continued rise throughout 1927. The wheat crop was the second largest on record and other crops reached new highs while prices were well-maintained. The mining output set a new record, capital imports for such developement and for hydro-electric installations, rivalling the huge imports of capital in the pre-war decade.

Manufacturing was extended more than in 1926 and continual amalgamations and reorganizations marked the administration of many industries. The index of physical volume of production rose from 135 in 1926 to 146 with a consequent increase in employment of 2-5% above the 1926 level. The year as a whole saw a marked continuance and acceleration of prosperity. Imports and exports reflected this in greater volumes and increased value.

The year 1928 may be said to have marked the highest point of industrial and trade activity ever reached in Canada. The production of wheat and newsprint, the two leading exports of the Dominion established new high records, the former totalling 532 million bushels, an increase of 60 millions over 1926 while the latter reached 2,381,102 tons the previous high yield being 300,000 tons less. Agricultural conditions in general were buoyant and the whole country rode on the crest of this wave of prosperity of the farming class. Mining reached a new record for value of total production exceeding by $24,000,000 the 1927 total of $237,000,000. General manufacturing showed a marked increase in activity while all previous records for new construction were broken with $300 million of contracts under way.

There was a phenomenal volume of trading with an increase of 10% in physical volume. The balance continued to be favorable and the possession of the hgihest per capita favorable balance was still pointed to with pride. Total external trade was valued at $2,359,000,000 increasing the per capita figure to $237.70.

The great volume of trading, the prolonged rise of prices on the stock market and firm wages rendered more favorable in their incidence due to the slight downward trend in the cost of living contributed to a universal optimism. Toward the end of the year credit was somewhat hardened as a reaction to the over-speculation.

Two opposing tendencies marked 1929. The first nine months saw a progressive advance in the general economic expansion which had been continuously in progress since the close of 1924. World conditions were the ultimate bases of this but the Canadian expansion was intensified by the four exceptionally large harvests of '25, '26, '27 and '28. Exploitation of new forest and mineral regions in Northern Quebec and Ontario and the large capital expended in this way tended to increase the rate of advance.

By September 1929 new record highs, in many cases higher than in any time in the previous history of Canada, were reached in industrial, commercial and financial fields. Such statistics as the volume of total industrial production being 14% higher than 1928, bank debits 8.2% higher and general employment 6% greater in volume.

Prices of industrial stocks measured as 100 in 1926 far surpassed the 237.3 mark reached in December 1928 and soared to 315.8 in September 1929. New high records in mining, hydro-electric installation, iron and steel production and general construction reflect the universal expansion.

Two serious checks to this speculative growth came in the Autumn of 1929. A drastic decline in the current crop which saw wheat production fall from 566 million bushels in 1928 to 299 million bushels and a decided deflation in security prices after the crash on Wall Street brought a marked change. Business activity fell off, credit was tightened and many liquidations occurred.

The decline during the last quarter of the year didn't prevent total trade reaching $2,654,000,000 the greatest amount in the history of the Dominion to date. Both imports and exports were from $150 to $160 million greater than in 1928. Per capita value of the aggregate external trade reached $262.23 a mark exceeded only by the last year of the war and in '20 and '21 when government credits financed a large proportion of our export trade.

FINANCIAL REVIEW

A pay-as-you go policy was introduced in 1920 with the imposition of new taxes. These produced abounding revenue which was very gratifying to the minister of finance. The luxury taxes imposed with a view to reducing the expenditure on non-essentials were particularly helpful. The large returns from this source and from sales, transportation and cheque taxes the income received under this head increased by more than $63,000,000 to more than four times the 1920 total. Increases in the income tax and a more vigorous and efficient collection policy more than doubled the return from this source. Other war taxes were slightly higher giving a total of $168,385,000 as receipts accuring in the War Tax Revenues" account.

Customs and Excise Duties were slightly lower reflecting the decline in prices as well as the decline in volume. An interesting feature of this years receipts is that for the first time in the history of the Dominion, customs duties lost their position as the largest contributor to the Consolidated Fund to the greatly increased war tax account. This condition continued until 1928. Total revenue for the year thanks to the buoyant returns on war taxes reached and exceeded for the first time the 400 million dollars mark. Receipts exceeded the total receipts of 1916 and 17 combined, reaching $436,292,000, more than eight times the amount received in 1901 and almost four times the 1911 total.

Strict economy in controllable expenditures was instituted along with the pay-as-you-go policy but as this portion of ordinary expenditures was small compared to the fixed charges total current outlay soared to $361,118,000 the highest mark in the Dominion's history. Large increases in charges for debt and for pensions were responsible for the increase of almost $60,000,000 over the 1920 total.

The field wherein the policy of restriction on outlays was applied with greater effect was the capital account where the total spent was cut by more than a third. Completion of the vast public works programmes and acquisition of the Grand Trunk which had consumed huge sums in 1920, freed the budget of 1921 from the necessity of such large outlays. The transition from war to peace was by this time almost completely accomplished so the large sums voted to smooth conditions in this period were not needed.

The economy practiced can be realized by a glance at the figure of total expenditures which dropped by $250,000,000 to the sum of $528,302,000. Even with such a precipitous decline in outlays this amount was greater than the total expended in the four years 1909-10-11-12.

In 1921 the minister of finance announced the abolition of the business profits war tax and the luxury taxes some of which had been dropped by an order-in-council in December, 1920. To replace the revenue thus abandoned heavier duties were placed on playing cards, wines and spirits and most important of all the sales tax was increased.

Due to the universal dullness which characterized business the fiscal year 1922 found revenue substantially decreased. The already large sums derived from war taxes increased to even larger totals so that this item contributed $177,484,661 an amount greater than the revenue from all sources in the year 1917. This was a very fine record when in light of the fact that only back taxes on the business profits account were available and that the minor war taxes on financial companies gave smaller amounts than in 1921. The sales and transportation taxes etc. also revealed a decreased revenue but the almost doubled return from the income tax more than made up for all reductions in other items.

The universal reduction in purchasing power together with the "consumers strike" of those dependent on primary production in Canada caused a drastic fall in imports which caused customs duties to fall precipitously from $163 to $105 million. Excise duties also declined not only in spite of, but to a large degree because of the increased rates levied. Together with a decreased volume of business. All receipt items totalled just over $382 million a decline of $54,000,000 from the previous year's total.

The pay-aspyou-go policy which involved a strict economy in expenditures began to bear fruit in this connection by 1922. In spite of an increase in the net debt in the fiscal year 1921 interest charges were 4 million dollars lighter than in the above year. Minor reductions were made in most of the current expense accounts so that ordinary expenditure fell by $14, 000,000 leaving a current outlay of $347,560,000. This reduction was accomplished in the face of large expenditures on railways and public works according to the efforts of the government to make the transition from war to peace conditions easier.

Capital expenditures were cut to the bone, being less than in any year since 1908. The public works account reflecting part of the building programme instituted as above was the only major item of capital outlay taking 10½ of the $16,000,000 spent. Thanks to this decrease total expenditures dropped to $463,528,000 or $81 million more than was received the latter amount being added to the next debt. On ordinary account there was a surplus of over $35,000, 000 so the current account was being satisfactorily controlled.

With the system of taxation in operation the minister of finance was certain that all current expenditures of the next year could be met and even some of the capital outlays. However the probable need of a further addition to the public debt impilled him to impose increased taxation. The sales tax was raised 50%. Excise taxes were increased. The tax on cheques was increased while various taxes were imposed on banks and insurance companies.

The outstanding features of the financial operations of the Dominion Government during the fiscal year 1923 were the buoyancy of the revenue and the success of the financing in the United States. The sales tax proved to be a wonderful revenue producer in 1923, the 50% increase in the rate coupled with a revival in business brought a huge increase in the returns from this tax. Together with transportation and other like taxes the sales tax contributed over 106,000,000 almost 50% more than was received from it in 1922. By a very efficient and persistent organization, back taxes to the amount of over 13,000,000 were collected under the business profits tax. The income tax returns declined by about $19 million, but the increase due to the sales tax brought the war-tax items to a new high of $181,634,000.

The general upward tendency in business following the dull conditions of 1922 resulted in a substantial increase in customs revenues while strangely enough excise duties were lower than in 1922. This latter condition came about through increased smuggling across the United States border which the heavy rates on tobaccos etc. induced.

Total receipts once again exceeded the $400,000,000 mark due to the heavier returns from war taxes and customs duties.

Strict economy was still the guiding principle in spending during the fiscal year and the valiant efforts of the minister of finance to reduce expenditures were rewarded. Current outlays dropped from $347.5 millions to $332.3 millions due to a reduction of a substantial amount in every item but that for interest charges which was uncontrollable. In relation to ordinary revenue the reduced expenditure gave a surplus of over $70,000,000 which was very gratefully accepted. This surplus was applied to capital and other expenditures but failed to meet these requirements by $31,641,000 which was the net amount added to the national debt.

Additions to the net debt which beginning in 1914 with $21,000,000 and reaching unprecedented heights in the later years of the war seemed to have become the usual thing in every budget. The banner year was 1920 when $674,000,000 was added and a further yearly increase seemed unavoidable. By 1923 the yearly addition had diminished to $31,641,000 and hope was held out for a continual decrease and in the near future abolition of this unwelcome item in the yearly accounts. It was felt that continued additions to the net debt would prove more advantageous than the opening of new forms or sources of taxation.

The opposition to introducing new taxes didn't go so far as to militate in present rates. The desire for a budget balance (against increases) led to an increase and revision of the hitherto quite complex sales tax to a straight 6% rate. The tariff rates under the British Preference were revised to increase the preference by 10% while the duty on imports of refined sugar was lowered with other minor reductions. The increase of the excise rate on cigarettes which led to so much smuggling was removed and an unproductive excise tax on beet sugar was abolished The cheque tax was reduced, also that on notes and bills of exchange. On the whole the changes were toward a lighter burden. A large volume of external trade in the fiscal year 1924 found exports of Canadian produce jumping to a total greater by $114,000,000 than that of 1923. The import total rose by $91,000,000 and customs duties rose in conequence. This item increased to $121,500,000 while the excise duties, which many though would be smaller due to reductions in the rates on several commodities, rose on the contrary to over $38,000,000 a total exceeded only by that of 1920. The income tax returns due to increased exemptions fell off by $5 million but war tax revenue remained at practically the same level, due to an increase of $14,000,000 in the sales, transportation and other tax accounts Total Consolidated Fund Receipts were $3 million more than in 1923 reaching $406 million.

The expenditure account reveals a continuation of the struggle to reduce current outlays so as to render a balanced budget possible. Total expenditures on the Consolidated Fund were reduced to $324,813,000 or by just under $8,000,000. The increase in ordinary revenues coupled with a decrease in ordinary outlays resulted in a handsome surplus on current account of almost $82,000,000 which was applied to capital and special expenditure. These latter outlays were slightly higher than in 1923 but nevertheless total expenditure was reduced to $370,589,000, a decrease of $64,000,000 from the previous year. The entire operations of the year found the fondest hopes of the finance minister realized when almost 36 million dollars was applied to reduction of the national debt.

The reduction of the net debt led to a demand for decreased taxation to which the government complied. The duties on agricultural impliments was reduced and machinery used in other extractive industries was also given reduced rates. The sales tax generally was reduced from 6% to 5% and the list of exempted articles was considerably extended.

The universal reduction in taxation brought a sharp decline in Consolidated Fund Receipts to $351,515,000 in 1925. The reduction in tarrifs together with a decline of $96,000,000 in imports caused a drop of 13,000,000 in returns from this tax. Excise duties were steady but war tax revenue fell off sharply The lower rate of the sales tax was a major factor in this, the total fall in it and like taxes amounting to $35,000,000. This represented almost exactly the amount by which total war taxes failed to meet the 1924 totals.

Current expenditures were still further reduced so that on ordinary account there was a surplus of about $32,000,000 When other expenditures had been accounted for there was still a fa favorable balance even though it was a small one. The attainment of a balance between total income and total expenditure which includes debt reduction meant the accomplishment of an end sought since 1922. In the fiscal year 1926 revenues were more buoyant again, exceeding the 1925 returns by $30 million. The decided upswing during the last months of '25 and the early part of 1926.

was reflected in a definite increase in all taxation returns. The remarkable strides made by Canada toward a premier position as a world trader resulted in a substantial rise in Custom's duties. From the 1925 total of $108,146,871, the lowest but for 1922, since 1916, the receipts from this source rose to $127,355,000. The increased business activity of the year resulted in a excise tax returns swelling to $48,513,000. War tax revenue was $10 million higher than in 1925.

Interest charges the largest item of ordinary expenditure dropped from $134, to $130,000,000 thanks to the debt reduction in 1924 and '25. Small increases in the amount spent on pensions public works were responsible for an increase of $2,000,000 over the 1925 total.

Strict economy still prevailed in all expenditures especially in those of capital nature. Capital expenditures were kept at the 1925 level while special expenditures were cut sharply. Total disbursements were only slightly higher than in 1925. A surplus of over $62,000,000 on current account gave funds to meet all capital and special expenditure and left $27,706,000 for application toward reducing the national debt.

The abundant funds received by the government brought renewed demands for lessened taxation to which the government agreed. The income tax was reduced all along the line, the reductions to apply to payments on the 1925 incomes. The stamp taxes were abolished while a number of items were placed on the list of exemptions from the Sales tax and the return to Penny Postage was announced. A general reduction in the tariff on automobiles and

and a modification of other schedules was included but the entire budget was rather left in the air without Royal assent when Parliament was dissolved on July 2nd. However the various changes were passed when the election was decided.

The marked activity that began to characterize business and the swelling external trade found all revenues higher. The most notworthy feature was the decided increase in customs duties due partly to more trade but in a far larger part on the tightening up of cumstom's regulations which followed in the wake of the Customs Inquiry. The receipts from customs were $14,000,000 greater than in 1926 while excise taxes brought in $48,513,000 six millions more than in the previous year. War tax revenue was practically the same as in '26 largely because of a $7,000,000 increase in receipts of sales, transportation and other such taxes which balanced a similar decrease in the income tax. Total ordinary revenues were up to the 400,000,000 level again, the fourth time in the Dominion's history to that time in which this level was reached.

Current expenditures were slightly lower due to lower interest charges and a decrease in the amount expended on public works. On the ordinary account a surplus of $81,000,000 was recorded which fully covered all other disbursements and still left $41,000,000 by which the public debt was diminished.

The 1927 budget announced several reductions in taxation. The income tax was cut by 10%, the sales tax by 20% while other excise items were reduced. No tariff changes were brought down since the newly formed Tariff Board had not as yet reached the conclusion of their inquiries.

The high tide of industrial and general economic activity that marked 1928 found federal revenues swelling also. Custom's and excise duties were both larger than in the previous year, the former more than 10% higher, the latter almost 20% higher. War tax revenues largely because of the reductions in the sales tax. In the account which groups the sales, cheque and other minor taxes there was a reduction of $15,000,000. The rise in national prosperity was reflected in the income tax returns which despite the cut of 10% in rate brought in $9,000,000 more than in the preceding year. Total taxation receipts were $364,705,803 while total revenue was $429,642,000.

The strings on the federal purse were loosened a bit in the face of universal prosperity so that $336,167,000 were spent on the Consolidated Fund Account. A greater sum was spent in pensions and the public works account shows a slight increase. A surplus of $93 million on the Consolidated Fund was applied to other expenditures which amounted to approximately 23,000,000, while the net debt was reduced by fifty million dollars.

Tax changes in the 1925 Budget included a further decrease of 10% in the income tax, a general cut of 25% in the sales tax and an increase in the exemptions under the income tax. Many changes were made in the tariff schedules in consequence of the decisions of the Advisory Board on Tariffs.

The fiscal year 1929 saw the largest amount of revenue in the history of the nation entering the federal coffers. A grand total of $460,157,000 was received, more than the total received in the first 22 years of the Dominion's career customs duties reached $187,206,000, a larger than total receipts in any year up to 1917. Excise returns were higher by more than 10% but war taxes contributed less than in 1928. The income tax gave slightly higher receipts but the sales tax again fell off so that a decrease of $5,000,000 was recorded in war tax revenues. The buoyant revenues almost $100,000,000 more than was spent enabled the government to meet all disbursements which in the total amounted to $388,805,000 and as well to reduce the net debt by more than $71 million.

This was the largest ever made, bringing the net debt to $2,225,504,000 in 1929 as compared to $2,453,776,000 in 1923. In this 6 year period the total reductions amounted to $228,000,000.

CHAPTER VI.

The economic reaction which followed the boom of 1928-29 was marked by wider extent and deeper intensity during 1930,31 and 32. All the characteristics of an acute depression were present, falling commodity and security prices, "over-production, declining imports and exports and wide-spread unemployment. Indexes of different business and industrial activities show a steep declines reaching the lowest levelin the first quarter of 1933. From May of that year there was a general upswing which recovered by the end of 1934 a considerable portion of the ground lost in the years previous to 1933.

The first year of the depression was featured by a calamitous decline in the price of wheat, and a considerable demoralization in newsprint, which are commonly supposed to be the cornerstones of Canada's prosperity. The world wide drop in wheat prices was a considerable hardship to the western farmer and the presence of a huge yieldfor which there was little demand even at the low prices promised to constitute a real problem. The other primary industries suffered from similar causes and began a decline that rendered the conditions of those people dependent on them ever more serious as time went on. All forms of industrial activity suffered in like manner the volume of manufacturing falling considerably below the 1929 level. Building and construction fell off to approximately the 1928 level. Adding to the number of unemployed which was already swollen by the shut-down or reached out put of many plants. Logging, especially, reported less than half the employment of November 1929 for the same month in 1930.

The index of employment compiled by the Dominion Bureau of Statistics shows a drop from 119-0 in 1929 to 113 in 1930.

The large number unemployed and the restriction that low prices laid on production caused a decline of 10% in the net purchasing power of the country, the per capita figure dropping from $607 to $500. The decrease in purchasing power was too precipitous for prices to match it, wholesale prices falling by about 9% while retail prices (including rents and costs of services) fell by an almost negligible amount.

Imports due to lower prices; decreased volume further restricted by stiff tariff increases fell off in 1930, the total value for the year ending March 31, 1931, being $906 million, a decline of over 25% from the previous year. Exports were down 27% in the same period largely because of the reduced volume of wheat exports. An analysis of the trade returns reveals a decline of only 13% in volume of exports and a 16% decline in volume of imports as compared to the drop in total value for the two years.

The depression became more acute in 1931, the trend of all activities being definitely down. The physical volume of business which is perhaps the best measure of prosperity reveals a drop by the end of the year of 14% from the long run trend. (1919-1935 by Bureau of Statistics). Agricultural production was much lower than even the law yields of 1930 due an extended period of draught throughout Canada. The serious effect on the farmer's purchasing power is to be seen from the gross agricultural revenue estimate made by the Financial Post Business Year Book which indicates a 40% decline from the 1929 level.

The physical volume of manufacturing fell below the 1930 level, and only slightly exceeded the 1925 figure. The decreased volume with lower wholsale and retail commodity prices meant a considerable decline in the value of manufactures which wrought a corresponding decline in the value of the net national production which fell to $4,000 million compared to $5,150 in 1930 and $6,072 in 1929. This estimate is the basis on which purchasing power is estimated the decline per capita being 24%. The spread between prices and purchasing power was increased since wholesale prices fell by only 16% while the retail index referred to above fell by 10%.

External trade data reveal a further decline in total trade amounting to $560,000,000 to which imports contributed a drop of $328 million and exports a drop of 232 millions. (fiscal year 1932) The sharp upward revision of the tariff was an important factor in reducing import totals while the world wide extent of the depression accounted for a decline in exports.

The year 1932 was the worst experienced by Canada in many years. The general picture may be summed up by the estimate of the Bureau of Statistics which places the decline in the general level of productively throughout the Dominion at 20%. The decline in productivity varied greatly between various provinces and industrial and financial groups. Manufacturing which accounted for 53% of the total productivily was down 24%, newprint production fell by 11%, wheat flour production fell 10%, automobiles 26%, pig iron 69% and steel 51%.

The list of recessions from the 1931 level also includes gross agricultural revenue which fell by 9%, building and construction car-loadings etc. The record of the year is one of decline in some cases precipitous from the already low levels of 1931.

Prices had returned to the pre-war level, the wholesale index dropping to 66.7 (1926-100) about 7% lower than in the preceeding year. The retail index indicates a decline of 9% compared with a decline of approximately 20% in purchasing power which was $324. per capita. The decline in prices and less purchasing power found imports and exports 25% lower in the aggregate.

The absolute low of the depression was reached in the opening months of 1933 when almost all indexes on a monthly basis reveal the greatest diviation from the normal trend of business. Several factors combined to bring about the decided reversal of the trend of the previous three years. A substantial increase in industrial employment which occurred with increasing velocity through the last three quarters of the year and an improvement in agricultural prices which benefitted all areas having crops for sale were the main influences causing the upswing, both rising from the New Deal in the U.S.A. and apparent higher sales as result of Ottawa Conference. The favorable crop of 1932 was probably a contributing factor also.

The recovery pervaded the entire field of activity in Canada, the price improvement givig a favorable impitus to general business. The wholesale price index rose slightly, retail prices however were still lower, but tended to improve late in the year. A feature of the year was the very large volume of Christmas trade as compared to the total of the previous years.

Manufacturing from the extremely low levels of the first months of the year, in February the index of volume stood at 58.7 (1926-100) rose so rapidly after that month that by September it stood at 97.0. The average for the year was about 8% higher than in 1932. The primary industries had a very small share in the improvement. A vertual crop failure throughout Western Canada and very depressed conditions in the "Capital" goods industries such as construction, railway,rolling,stock etc, were unfavorable features of the year. The net national production was down slightly to $3,360 millions.

Trade figures reflect the upswing in business, both imports and exports recording gains, in the latter a very substantial one. Imports in the year ending March 1934 were up to 433,798,000 compared to $406,383,000 in the year previous. Exports were 20% higher than in 1932 reaching $585,654,000.

The most impressive evidence of the continued improvement in Canadian business during 1934 is shown by the 19% increase in the national income as estimated by the Financial Post Year Book. Increased manufacturing out put, higher farm prices and enlarged foreign trade were the leading contributing factors to the moderate but sustained advance.

The physical volume of business was 18% above the 1933 level while industrial activity averaged a 15% gain. Manufacturing led in this general improvement with the so called "durable" or "Capital" goods industries featuring the advance. Construction gained almost 30% but was still substantially below the pre-depression level.

Prices were higher, both wholesale and retail indexes showing rises. A most hopeful sign of prosperity was the closer correspondence of these prices and also of those of raw materials and manufactured goods.

The pronounced gain in external trade in 1934 with 28% larger import total and 23% larger export total reflects the increasing confidence in the movement toward prosperity. Trade with the Empire countries was larger and that with foreign nations was also increased.

The trend of economic conditions continued irregularly upward in 1935 with the "durable" goods industries again the feature in an increased industrial output. The level of business operations was still below the 1929 level but the index of physical volume shows a gain to a position above the 1926 figure. That conditions were still abnormal is to be seen in the large number of unemployed, many idle plants and a larger number operating much below capacity.

The budget of 1929, presented in April of that year belongs to the preceding group of years in that it contemplated a continuance of the boom. With this in mind the Minister of Finance announced the abolition of various "nuisance" taxes, such as that on cablegrams, insurance premiums and sleeping car tickets, and of more importance a major reduction of one third in the sales tax. The returns from taxation were of course influenced greatly by the crisis and its after effects which introduced the opening stages of the depression late in 1929. It must be observed that the fiscal year 1930 runs from April 1st,1929 to March 31st,1930 and it therefore was a year of half-prosperity and half reaction.

Revenues present no outstanding changes in 1930 aside from a decline in total receipts to $445,916,000.

The cut in the sales tax and the reduced volume of business in the winter of 1929-30 found receipts from this source approximately one third below the 1929 total and due to its large part it plays in war tax revenues a decline of eleven million dollars in this account. Lower yields from both customs and excise duties were a natural result of the lower volume of trade and business that marked the last half of the fiscal year. Total receipts amounted to very nearly 450, millions or $43.69 per capita of which over $37 was derived from taxation.

All expenditures were still the subject of close scouting due to an expressed desire of the Minister of Finance that Canada "live within her income" so that maturing debt could be retired and further reductions effected in taxation. The continual expansion throughout the first half of the fiscal year and the fact that estimates were subject to consideration with a continued boom as a basic assumption meant that extensive reduction in outlays was very improbable. Ordinary expenditures were restricted to the extent that they were increased by only $7 million above the previous year's total, a very commendable feature in the light of the hysteria of the boom period. Capital outlays amounted to $22,561,000 slightly less than the 1929 figure. The decrease was in large part due to a cut of ten million dollars in the public works account. "Other" expenditures were higher due to an increase of 8 millions in "other charges" in which account unemployment relief and farm relief costs are placed.

Total expenditure during the year amounted to $398 million being slightly higher than in 1929. This total includes an advance to railways of almost $2½ millions over which the government has little control. On a per capita basis ordinary expenditure at $35.06 was almost the same as the 1929 total while total disbursements were about 22 cents per person larger at $39.01.

The net debt was reduced by $47,740,000 which represented the net surplus of total receipts over total disbursements, continuing the decreases that had been made in each year since 1924.

The success of the -pay-as-you-go policy and very natural underestimation of the probable extent of the economic reaction induced the Minister of Finance to announce a further reduction in taxation in presenting his 1930 budget. The sales tax was cut from 2 to 1% while the income tax was reduced by increased exemptions allowed on government and like annuities and by extension of exemptions to certain dependent relatives. The budget also announced some minor tariff reductions but the year was unusual in that there was a second tariff revision at a special session in September of the year. At this session the anti-dumping clauses were re-written and a general increases were made in the duties on a wide range of goods.

The outstanding feature of federal finance in 1931 was the decline of $90,000,000 in ordinary receipts. The universal downward trend was the main cause of this disastrous drop but the evil effects as far as government revenue was concerned were magnified by the reduction in taxation and a combination of stiff tariffs and reduced purchasing power which cut imports. By three and one-quarter million dollars. The serious falling off in revenue was due to decreased receipts on all accounts with custom's excise and war-revenues leading in the fall. Customs were off $8 million, excise fell 8 millions while the reduced sales tax was responsible for a fall of 24 millions in war-tax revenues in spite of a slight increase in income tax returns.

The restriction on expenditure went by the Boards as the government tried to stem the falling tide of economic activity. Almost every ordinary account was larger than in 1930 with pensions public works and provincial subsidies revealing major increases. The first two were to a large extent part of the governments attempt to alleviate the first pangs of the depression among the people, more than $15,000,000 being spent on these accounts.

To the 31 million increase in current expenditures there was added an increase of 6 million on capital account again largely for public works. The programme of building was intended as a sop to the ever-mounting wave of unemployment and further relieve appeared in the "special" account which were 16 millions higher. Total disbursements were $40 million as compared to total receipts of $356 millions leaving a deficit on ordinary account the first since 1897 of $33 and on the year's total operations of almost $84 million. This latter amount was added to the national debt, the first of a rising tide of such additions.

The disastrous drop in receipts compelled a definite increase in taxation in the 1931 Budget. The sales tax was raised from 1 to 4 per cent while the tax-free limit on cheques, money orders etc. was reduced from $10 to $5. A special excise tax of 1 per cent was imposed on importations and the tariff schedule was given another upward revision.

The deepening intensity of the depression through the fiscal year 1932 resulted in another drop in receipts despite the heavier taxation imposed. The decline in receipts was however much smaller than in the previous year being less than $20,000,000 below the 1931 returns. The three per cent increase in the sales tax more than doubled the amount received in 1931 and did this in spite of a drastic fall in the volume of business. The income tax receipts reflected the lower national income by falling off by $10 million. Customs duties continued to fall, paralleling the reduced volume and value of imports while excise taxes suffered heavily from the decline in trade showing a 16% fall.

Despite the marked reduction in income the government was faced with heavy obligations many of which were "uncontrollable". Others were practically so in view of the conditions prevailing, leaving only a very small portion of the current and even of the total expenditure open to the practice of economy.

The ordinary account was freed from the heavy burden of relief charges by the assignment of such outlays to a "special" account. With this burdensome charge removed the Minister of Finance was able to announce that expenditure on the Consolidated Fund had been reduced by $14,000,000 mainly by cutting expenditure on public works. The total ordinary outlay amounted to $35.73 for every person in the Dominion.

The various "capital" accounts were cut by more than $11, 000,000. A drop of 38 per cent from the previous year. The policy of cutting all relief expenditure in the "emergency" class and the necessity of freeing as large a portion of the receipts as possible for meeting such needs found all the "capital" outlays lower for the year.

Special expenditure, mainly for farm and unemployment relief, was more than tripled, taking $55,384,000 or about 1/8 of the total disbursements. The latter amounted to approximately $451,000,000, necessitating further loans to make up the deficit of $114,000,000 which was added to the national debt.

The ever mounting charges on the federal purse compelled the increase of taxes in existence and the re-enaction of some of the war-taxes. Tickets and notes, cheques, money orders etc. were again taxed and the sales tax was boosted 50% and a number of commodities were removed from the exempt list. The special excise duty on imports was tripled and the income tax made heavier by repeal exemptions and special surcharges.

Since the fiscal year from April 1st to March 31st that of 1933 encompassed the very worst period experienced in Canada during the depression. The general declines in all forms of business, trade and industry were reflected by a sharp falling off in receipts of the federal government. Customs duties were 33 per cent lower, excise duties were 23 per cent lower and a calamitous fall in receipts was prevented only because the sales tax produced $15 millions more than in 1932. The income tax gave slightly higher returns but the drying up of the income from customs caused a fall of total receipts to $311 million, less than was received in any of fourteen years preceding 1933.

Strict economy was still the policy as regards ordinary outlay which was again cut, this time by $13 million despite a increase of over 10% in the largest item, interest charges which took nearly 38 per cent of total current expenditure. On the Consolidated Fund account there was another deficit this time of 47 millions.

Capital expenditures were cut to the bone, amounting during the year to only $8½ million. Other expenditure was however fully able to satisfy any desires of spendthrift members, outlay on this account very nearly doubling the previous year's total. Total expenditure exceeded $530 million, a record high but for the war and inflation years of 1918,19, 20. The national debt was increased to cover the deficit of $220,634,654, which indicated an expenditure by the government of $1.41 for every $1 received.

In April 1933 exemptions were reduced and rates increased in the income tax. The sales tax was left at 6 per cent but the exempt and partly exempt lists were revised with a view to additional revenue. The various war-taxes were increased as to rates and excise duties were similarly treated. The whole object of the budget was to strike a balance between so called "ordinary" income and expenditure and treating as emergency expenditure relief and like charges.

The federal revenues in 1934 benefitted by the upswing that began in 1933 although further declines were experienced in customs and excise duties. The continued buoyant returns from the sales tax featured the year, increases in this account and in other lesser war taxes accounting for a $24,000,000 increase in war-tax revenues. Total receipts recovered to $324,471,000 a hopeful sign of better times for the hard pressed federal treasury.

Salary reductions and a general curtailment of expenditures found ordinary expenses reduced by $8 million from the previous year's total. Capital outlays were almost negligible but almost $102,000,000 was spent for unemployment relief and other special charges. Another large deficit was inevitable but some optimism could be felt in view of the fact that the increase in the national debt was only slightly over half that of 1933.

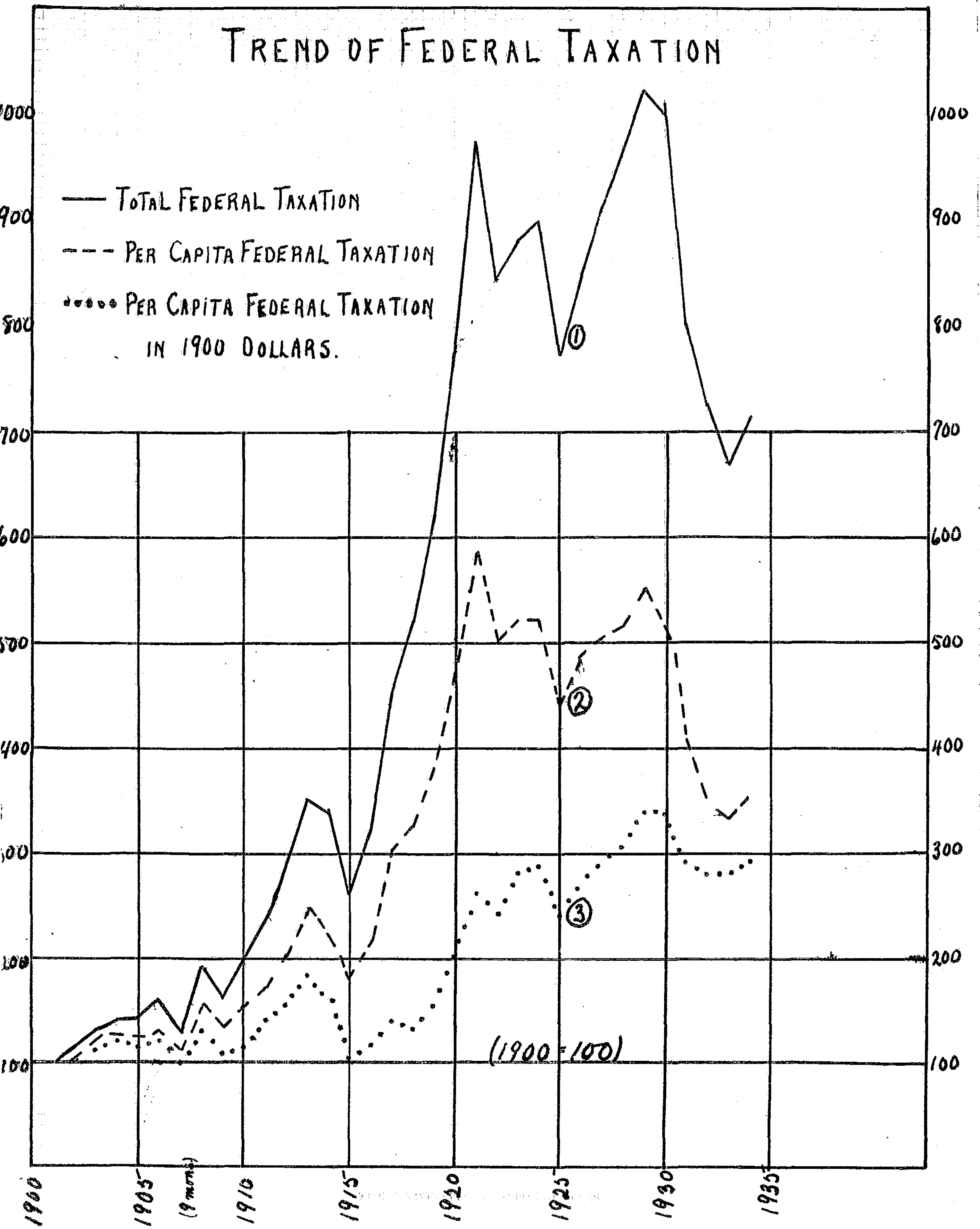
The budget presented in 1934 announced some minor changes in the tax structure. The excise tax on sugar imposed in 1933 was reduced by 1¢ per pound and some minor changes were made in excise duties. A proposed levy on the gold producers was finally enacted later in the year.

CHAPTER VII.

The Volume of Taxation in Canada.

The chart indicates the trend of the volume of taxation in Canada. The actual yearly dollar totals of taxation are inaccurate measures of the real volume of taxation in that no allowance for changes in the number of people who join in the payment of the tax bill. This fact renders a yearly comparison by such totals invalid. In addition to allowing for changes in the population, the true volume of taxation, that is the amount of purchasing power taken from the people can only be determined when the fluctuations in the price level are eliminated. The method of arriving at the index given as the volume of federal taxation in Canada was as follows: (1) The crude figures as given by the Bureau of Statistics were modified by allowing for population changes as estimated by the Bureau of Statistics for each year since 1867. (2) the per capita figure was then modified by eliminating fluctuations in the price level. This latter modification was based on a 5 year moving average of the wholesale price index made by Prof. Michell, brought up to date. The year 1900 was taken as base due to its central position in the time period.

The three indexes vary widely in level and are less closely co-ordinated as to fluctuations. The opening decade in which taxation totals soared far beyond any comparable change in population or prices. From 1903 to 1910 both population and prices


TREND OF FEDERAL TAXATION
—— TOTAL FEDERAL TAXATION
- - - PER CAPITA FEDERAL TAXATION
••••• PER CAPITA FEDERAL TAXATION IN 1900 DOLLARS.
1000
900
800
700
600
500
400
300
200
100
(1900 = 100)
1
2
3
1900
1905
(9 mos.)
1910
1915
1920
1925
1930
1935

were rising at almost the same rate as taxation and tending to keep the per capita real burden down. The three pre-war years however found the crude total reaching new heights every year and even the large increase in population and an decrease of over 30 per cent in the value of the dollar couldn't prevent a rapid rise in the real volume of taxation. By 1913 each person in Canada had to contribute $1.80 to the federal government for every $1.00 contributed in 1900.

The war period 1914 - 18 is revealed as the period of the smallest volume tax receipts since the early part of the 20th century. All three indexes show the heavy decline in government income in 1915 and the recovery after that year. The index of the crude total indicates a decline of almost 33 per cent from 1913 to 1915 but the increase in population reduced the volume to only 25% additional for each person. When we allow for price changes we see the real condition that existed. The sharp increase in prices after the outbreak of the war meant that each person was paying the government in dollars that were only worth about 80¢ as compared to 1913 and worth only 62¢ as compared to 1900 dollars. Due to these factors the per capita volume of purchasing power taken by the government in the first year of the war was only slightly larger than the amount taken in 1900. This rather anomolous condition of affairs in a time of heavy drain on the exchequer was not corrected until two years after the close of hostetiles.

The method of financing the war is reavled by the adjustment of the per capita volume of taxation. Rather than impose taxation commensurate with the meeds of the time and the ability of the people to pay (which will be considered below) the policy was to make succeding generations bear the 90% of the burden by selling huge bond issues. The complacency engendered in the hearts of the financial leaders at the success of their loan policy was unclouded by any thought as to the serious burden laid on the future when the loans inflated war dollars would have to be repaid in deflated peace dollars. It was suggested during the war and the suggestion supported since that a capital levy should have been made on the vast and easy accumulations of wealth made by quite a few Canadians in these years.

In the seven years 1915-21 $1, 489,699,316 was received from taxation and $1,490,510,948 spent on the Consolidated Fund. This left out over $284,000,000 of capital expenditure and obviously there was apparently no revenue available from taxation to meet war costs. The British Government had 26% of their war expenditure out of taxation in war years while in Canada it has been estimated 10% of costs of war were paid during the hostilities. Such a payment is indicated by analysis of the National debt though not apparent from the published public accounts as we have seen above. The total costs of the war and demobilization as given in the Canada Year Book of 1929 were $1,696,277,699. In 1913 the net debt stood at $314,301,625 in (1920 it stood at $2,248,868,624) on increase of (1919 it stood at $1,574,531,033) approximately $1,260,000 or approximately 90% of the total war costs. The post war period is marked by wide influctuations in the various taxation indexes. The index of crude totals in 1921 reached a peak of 970 as compared with 350 in 1913 and 100 in 1900.

The enormous increase in the number of dollars taken yearly in taxes in 1919-20-21 while population was increasing by approximately only 2 to 2½% year, meant a sharp upswing in the per capita payments to almost 6 times the 1900 figure. The loss of purchasing power to the tax-payer and incidentally the gain of it to the government was minimized greatly due to the inflation of post-war years. The real volume of taxation did however increase rapidly being in 1921, 4% greater than 1913 and 260% greater than in 1900. That is everyone in Canada paid $2.60 in 1921 for every $1.00 paid in taxes in 1900.

The first post was depression deflated the dollar as well as deflating the number of dollars received in taxes by the treasury. As a result all three indexes show a drop with the real volume of taxation fluctuating to a lesser degree than either the crude or per capita total. The growing prosperity that ended in the boom of 1928-29 resulted in much larger returns from taxation which were further increased by higher taxation. The desire to retire a substantial portion of the national debt was reason enough for the slow reduction, when crys for lower taxation. The continued high rates of taxation with a slowly increasing population and a steadily declining price level meant a greater amount of purchasing power was taken by the government. The reverse in economic activity in 1924-25 sharply reduced the real volume of taxation in those years but after that time the yearly larger volume was the case.

The depression beginning in 1930 became more and more intense through '31 and '32 caused a precipitous fall in the number of dollars collected by Ottawa. From the level of 1020 the index fell to 670 in 1933 with a slight rise to 710 in 1934. The sharp falling off in government revenues brought a drop of 40% in the per capita index since population from 1930-34 increased by only 5%. The continued decline in the price level which was accentuated by the depression decreased the real volume of tax payments to approximate $2.70 per person in 1932-33 as compared to $3.38 per person in 1928-29. Heavier taxation and a decrease in the value of the dollar found the volume per person in 1934 back up to $2.80 an increase of 180% over the volume in 1900.

The Sources of Federal Taxation in Canada.

Chart III shows the various sources of federal funds according to the different accounts kept as Consolidate Fund Receipts. Some idea of the relative importance of the different taxes is to be had from a comparison of the amounts each contributes. The trend of the receipts from the dfferent sources in selected years since Confederation also reveals the growth of a better fiscal policy especially since the outbreak of the Great War.

Customs revenues have always played a major role in Canada's federal income. Such duties with
up to 1915 almost the whole of the Dominion's revenues. From 1868 to 1918 the import duties gave from 72-80% in total taxation revenues. Since 1918 the percentage of customs of total taxation

has varied from 33% 1918-22 to 40-47%, 1927-30 with a drop to 24% in 1934.

Excise duties are another time-honored source of funds though they play a smaller part than do customs duties. In 1868 26% of total tax receipts were gathered from this source. In the course of years the excise duties have gradually become less important contributing in 1927 14% of total tax revenue and in 1934 13%.

The unprecedented rise in expenidtures due to the war resulted in the imposition of the "war taxes" in 1915,16,17. The more important of these are the income tax and the sales tax, war tax revenues in the total have taken over a leading place in federal receipts since their imposition as the chart indicates. Although they were enacted far too late to meet the war costs in the period of warfare they mark the emergence from a primitive financial era of sole dependence on "indirect" taxes as more enlightened period were "direct" taxes had a place in the revenue system. As a group these taxes contributed rapidly increasing amounts to the treasury until in 1921, over 45% of total tax receipts were derived from these taxes. The abolition of the business profits tax and of other of the minor taxes reduced the revenues slightly after 1924 but the important place it holds in the federal system is seen in the fact that this source alone has brought in larger revenues since the depression began in 1930. In 1934 War-tax revenues accounted for 63% of all federal tax revenues.

The income tax is the most important of the war-taxes. The value of such a tax has been fully demonstrated since its imposition the only regret being that it was not applied much earlier in the Dominion's history. Full fruition of the income tax was reached by 1922 when $78,684,000 was received from it. The rates were reduced in the course of the following 8 years and as a consequence the revenues from it were lower. In 1930 however higher rates brought increased returns so that with further increases the income tax brought in 22% of all taxation proceeds in 1934.

The Sales tax has been subject to drastic increases and decreases since it was first imposed. Despite early complenitus it has been of great aid in the post war years. One of its features that has made it valuable is its flexibility as an income producer.

Merits of Federal Taxes.

The customs tariff has been a well nigh universal source of income to national governments but expereince has repeatedly shown that it should by no means be the sole or even the main source. Its elasticity makes it most unreliable either in periods of prosperity, of depression or of war. For example in the decade preceding 1913 a period of very large foreign borrowings receipts from Canadian customs taxes rose from $40. million to $112 Million. This sudden acquisition of income was to a large degree responsible for the undescriminating expenditure characteristic of that period In so far as the collection of such taxation increased the price of imports it was in effect living out of capital since the imports taxed resulted from foreign capital borrowings. With the outbreak of the war came curtailment oc consumption, restriction of all trade and a falling off of foreign borrowing and in spite of rising prices customs revenues fell to $76 million in 1915. War inflated prices with stiffer rates brought a increase to $163 millions, again to fall to $106 million in the post war collapse of 1921.

Summing up it may be said the customs tariff has consistently raised a substantial but unstable revenue. "Redundancy of revenue in time of commercial and industrial activity and insufficiency and instability of revenue in time of stress and depression in peace it has shown itself uncertain and fluctuating with every crisis and even with changes in policies and conditions in foreign nations, in times of prosperity forcing embarrassing surpluses on the country leading to extravagance in expenditure and speculation, in adversity it has left the Treasury empty necessitating the lavish use of public credit."(1) In these words R.F. Honie sums up his discussion of the adequacy of the customs revenues in the United States in various periods. In addition to their failings as above, the regressive nature of such taxes and the fact that they tend to take more money from the taxpayer than they contribute to the Treasury make them especially inadequate as a main source of income.

The excise taxes emphasize the regressive tendency in our Dominion taxation but furnishing as they do a substantial annual revenue, they are from a fiscal point of view a satisfactory

1. Sources and Relative Merits of Federal Revenues, N.H. Jocoby, Canadian Economic Essays, Vol. II, page 55.

source of revenue. Both customs and excise have much to discredit them but they have yielded large amounts of revenue with a minimum of trouble and expense and as well it is desirable to have a certain amount of taxation falling on incomes to small to be reached by a direct tax.

The income tax in its ethical aspects needs no justification. It is firmly entrenched in almost every national tax system and is universally conceded to be one of the fairest and most equitable means of raising revenue. Its progressive rates counter-act to some extent the regressive characteristics of almost all the other taxes in our federal system. As well it gives a degree of flexibility to the system which is of major importance in meeting fluctuations in business activity. Its value in the Canadian system is especially established by the strong support it has given the Treasury since the crash of 1929.

The sales tax is the only other large contributor to government revenues which is discredited by its regressive character. With properly established exemption lists this tax can be made a fairly equitable and very valuable source of revenue since its nature lends it to the product.

The Burden of Taxation.

A really accurate picture of the real burden of federal taxation in Canada can only be approximated. What it actually costs the citizens of Canada to pay their yearly tax bills can only be determined when we relate the size of the federal tax bill to the size of the average citizen yearly. Income Determination of this latter figure is quite difficult. An estimate of the net

BURDEN OF TAXATION IN CANADA

	PER CAPITA		
	National Income	Taxation	Taxation as % of National Income
1871	$ 130.00	$ 4.42	3.4%
81	159.	5.54	3.6
91	167.	6.25	3.7
1901	214.	7.19	3.4
1911	326.	12.31	3.9
1920	649.	34.31	5.3
21	478.	41.96	8.8
22	502.	35.87	7.1
23	521.	37.24	7.2
24	570.	37.38	7.3
25	556.	31.63	5.7
26	596.	34.66	5.8
27	635.	35.98	5.7
28	646.	37.09	5.7
29	607.	39.49	6.5
30	505	37.09	7.2
31	384.	28.55	7.5
32	324.	26.18	8.1
33	333.	23.81	7.2
34	369.	25109	6.8

national income has been made by the Bureau of Statistics since 1919 and from this the average per capita income is determinable f for our purposes. The table below shows the net national income; the per capita national income or purchasing power; the per capita federal tax bill and the per centage, the latter represents the average per capita income. The estimate for the years 1871,81,91, 01,11, is based on data of production given in the statistical survey of Canada in the 1934 Canada Year Book.

The influence of price changes is only of importance when comparisons of actual amounts between different years is concerned. For our purposes price changes are not relevant since the relative proportions of the purchasing power taken in each year by federal taxes is sought. Such proportions are comparable from year to year since price changes do not affect the yearly proportions used for comparison.

Federal Government Expenditures in Canada.

Chart Number II shows the index of federal "ordinary" expenditures (excluding Post Office) from 1900 to 1934 and compares the crude index with the per capita index and the per capita index modified to eliminate price changes. All indexes have 1900-100.

In the period since the turn of the century the value of modifying our crude data to render it more intelligible as quite obvious. This period may also be divided in two or three sections. The first encompassing expansion of ordinary expenditure to 1915 and secondly the phenomenal increase during and in the years following the Great War. The index of the crude totals reveals these two periods distinctly but for accurate comparable facts the modification to a per capita bases must be made and also the further modification reference to constant monetary unit.

The expansion of the opening years of the century resulted in a discarding of the stringent economies that the depression of the 90's made necessary. From 1900 to 1914 the per capita amount spent by the federal government on ordinary account amounted to $1.40 for every dollar spent in 1900. A decline in prices in 1908 and another peiod of reaction in 1910 and 1911 caused the lesser degree of correlation of the crude trend and the modified trend.

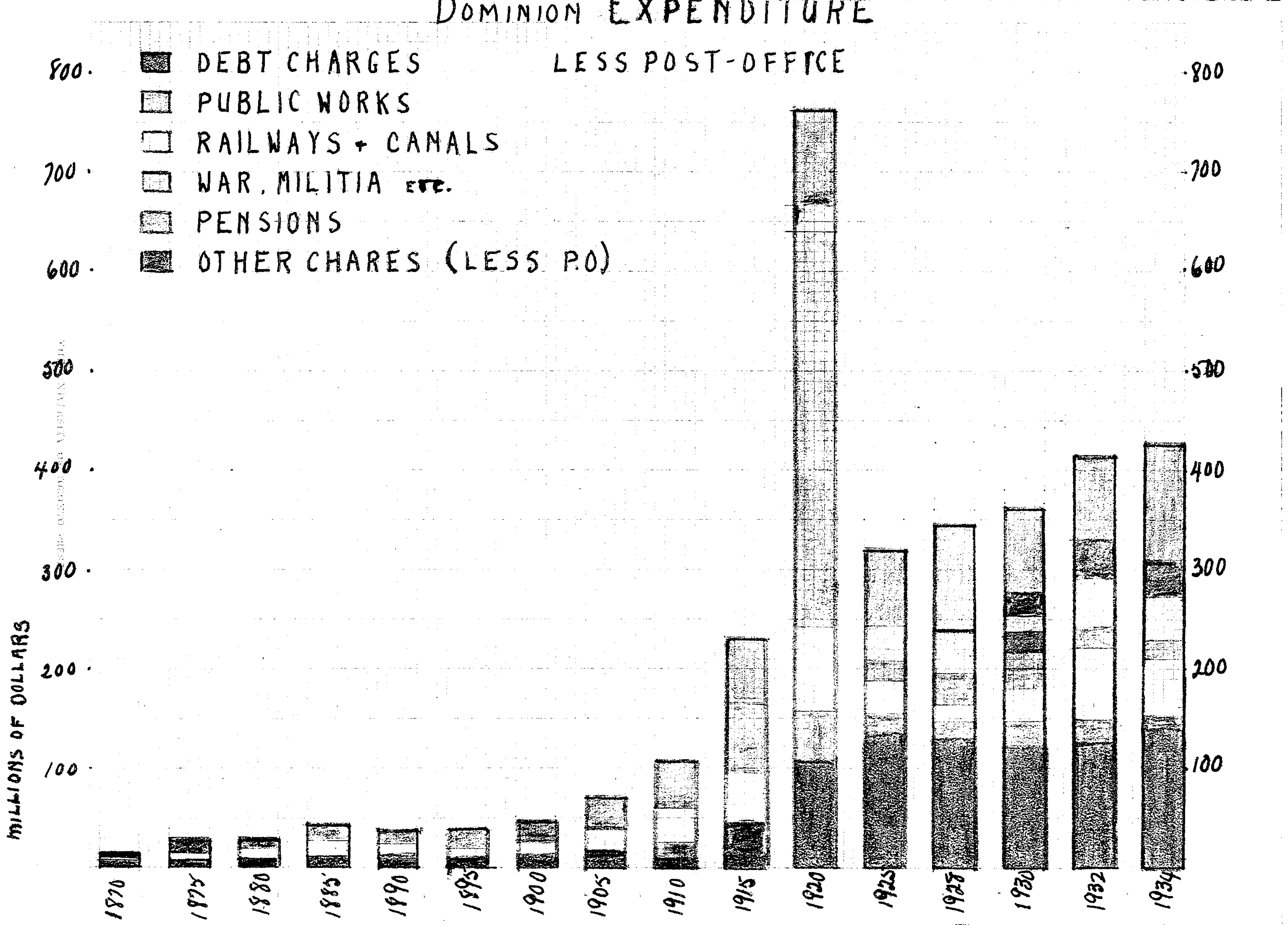
In the outbreak of the war all efforts were turned toward winning the struggle and in the face of huge capital outlays ordinary expenditures were slashed. The fall in the value of the dollar emphasized this trend so we find our modified index showing expenditures per head in 1916 and 1917 and 1918 of approximately the same amount as in 1900. After the War was over the necessity of rehabilitation meant larger amounts had to be spent, especially due to the fact the dollar was worth less than half its value in 1900. The real amount spent of federal current outlay, by 1923 $2.50 per head for every $1.00 per head in 1900. The decline in prices after the inflation of 1919 and 1920 devided to raise the real amount spent but by yearly reductions in Consolidated Fund Expenditures the amount per person was reduced to about $2.30 in 1900 dollars. The boom of '28 and '29 and a less careful supervision of accounts brought on a sharp upward trend which the large outlays of the depression tended to magnify. From the level of about $2.30 per capita in 1928 ordinary expenditures reached almost $3.30 per head in 1900 monetary units. This 43 per cent increase in ordinary expenditures meant that the government was committed to more than the outlays that were undertaken in 1900.

A short exposition of the charges met out of ordinary expenditures and total expenditure will aid in determining the major factos behind this 20th centure upward surge of federal expenditures. The diagram illustrated the main items of expenditures of the Federal Government for certain years.

EXPENDITURES OF THE FEDERAL GOVERNMENT

IN MILLIONS OF DOLLARS

Year	Debt.	Pensions	Public Works	Canals & Railways	Militia War etc.	Farm & Unemployment Relf.	Other	Total Excldg. P.O.
1870	5.4	.1	.1	2.4			9.2	17.2
1875	6.8	.1	1.9	8.5			14.1	31.4
1880	8.1	.2	1.1	10.4			13.4	32.2
1885	9.8	.1	2.5	16.3			18.0	46.7
1890	9.9	.1	5.	9.4			14.3	38.7
1895	10.7	.1	1.8	7.8			18.9	39.3
1900	10.9	.1	3.3	11.9	2.		20.7	48.9
1905	10.9	.1	8.3	19.2	2.6		33.1	74.2
1910	13.5	.2	11.8	35.3	5.9		41.5	108.2
1915	16.3	.6	30.3	49.6	70.9		64.6	232.1
1920	109.	26.	47.8	84.9	39.70		110.5	765.2
1925	135.6	34.9	18.0	33.3	19.4		80.1	321.3
1928	129.8	39.8	17.3	17.3	30.5	4.4	94.9	346.9
1930	122.6	40.4	24.7	51.9	36.6	38.3	87.0	363.2
1932	125.6	48.7	23.4	73.3	23.1	36.7	84.1	416.5
1934	140.6	43.8	13.4	56.	18.8	35.9	120.2	428.7


DOMINION EXPENDITURE
LESS POST-OFFICE
DEBT CHARGES
PUBLIC WORKS
RAILWAYS + CANALS
WAR, MILITIA ETC.
PENSIONS
OTHER CHARES (LESS P.O)
MILLIONS OF DOLLARS
800
700
600
500
400
300
200
100
1870
1875
1880
1885
1890
1895
1900
1905
1910
1915
1920
1925
1928
1930
1932
1934

Federal Expenditures in comparison with major Factors in the Canadian economy.

The table below indicates current government expenditures in comparison with value of field crops, National Income.

	Ord. Expen.	National Income	Ord. Expen. as % of Natl. Income.
1871	$15,623 (000)	$482,000 (000)	3.2%
1881	25,502	685,000	3.7
1891	36,343	815,000	4.5
1901	46,866	1,169,000	4.1
1911	87,774	2,347,000	3.7
1916	130,350		
1921	361,118,	4,215,000	8.6
1926	320,660	5,600,000	5.8
1931	389,558	4,000,000	9.7
1934	346,648	3,978,000	8.7

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