

previous year. At 17.3% the rate of growth of total borrowing by the domestic non-financial sectors was more rapid than that of nominal GNP which grew by 14.5%. Placed in perspective to the flow of final goods and services produced by the Canadian economy, the flow of credit raised by these sectors was 20.6% of GNP. This ratio was not unlike those of the previous two years, although relatively high by historical standards. The heavy credit demands contributed to the maintenance of interest rates in Canada which were high by international norms and a large volume of borrowing overflowed into foreign capital markets.

**Summary of trends.** In broad terms financial activity in Canada was characterized by: an increase in the proportion of total funds raised going to the private non-financial corporate sector, reduced borrowing by the government sector proper but heavy borrowing by the associated enterprises of governments, some downward movement in interest rates but the continued existence of large international interest rate differentials, increased emphasis on the foreign sector as a source of long-term funds for Canadian borrowers, and a gradual reduction in the rate of growth of the narrowly defined money supply. There was increased emphasis on intermediated credit flows in 1976 compared to the preceding year. In 1975, approximately 72% of the increase in financial assets of the domestic non-financial sectors was represented by claims on financial institutions; in 1976 this percentage increased to over 91%.

Following a recession that was milder than in many of the western industrialized countries, the Canadian economy entered a recovery phase in mid-1975. Gross national product increased at rates of 14.5% and 4.6% in nominal and real terms respectively during 1976. While these rates of expansion were higher than in 1975 (with 9.8% and 0.2% respectively), there was a perceptible slowing in the expansion of economic activity as the year progressed. Much of the growth in 1976 was concentrated in the first quarter of the year when seasonally adjusted real GNP increased at an annual rate of 13.0%; during the fourth quarter seasonally adjusted real GNP declined at an annual rate of 2.5%. A spasmodic recovery was also characteristic of economic conditions in a number of Canada's trading partners including the United States. As a consequence, while the growth in Canada's exports was reasonably strong, the foreign sector did not provide as much stimulus to final demand in Canada as had been previously generally anticipated.

During 1976, macroeconomic policy in Canada was directed toward facilitating a return to reasonable price stability. The approach adopted was that of gradualism. In Canada this policy involved a reduction in the rate of growth of the money supply, a somewhat more restrictive fiscal stance and wage-profit-margin guidelines designed to speed up adjustments to progressively lower rates of inflation. Broadly similar policies were pursued in several OECD countries.

An increase in expenditures on fixed capital formation typically follows and reinforces other expenditures which initiate a revival in economic activity. In several industrialized countries, including Canada, investment expenditures in 1976 failed to turn up decisively several quarters after what appears to have been the beginning of a recovery. Over the year real capital formation in Canada increased by less than 1%. The flow of investment expenditures by business was particularly insipid. In real terms, investment by business (including government enterprises) in plant and equipment was essentially flat and expenditures by business on non-residential construction declined by close to 7%. Observers suggested a number of reasons for the malingering aspect of investment expenditures including the following: the existence of substantial amounts of excess capacity, low anticipated rates of return on new investment, the increase in energy costs, high unit labour costs in Canada relative to the United States, some misgivings by entrepreneurs about the strength and duration of the recovery which began in mid-1975 and political uncertainties.

**The corporate sector.** Despite the weakness of capital expenditures, the demands placed on capital markets by the private corporate sector were higher in 1976 than