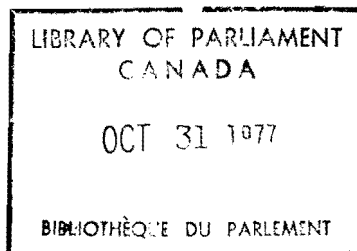


# ANTI-INFLATION BOARD

## SECOND YEAR REPORT



Anti-Inflation  
Board

Commission de lutte  
contre l'inflation

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# TABLE OF CONTENTS

	<i>Page</i>
<b>THE IMPACT OF THE ANTI-INFLATION PROGRAM .....</b>	<b>1</b>
The Program .....	1
The Program as Implemented .....	1
Monetary Policy .....	1
Government Expenditure Policy .....	3
Mandatory Controls .....	3
The Results .....	5
Impact of the Program .....	6
The Third Year and After .....	6
<b>COMPENSATION .....</b>	<b>7</b>
Compensation Guidelines .....	7
The Response .....	7
The Results .....	10
<b>PRICES AND PROFITS .....</b>	<b>12</b>
Prices and Profits Guidelines .....	12
Reporting and Compliance .....	12
Price Pre-Notification .....	12
Profit Margins .....	13
Excess Revenue .....	14
Dividends .....	14
Professional Fees and Incomes .....	15
<b>OPERATIONS .....</b>	<b>17</b>
Communications .....	17
Research .....	17
Administration .....	18
<b>APPENDIX .....</b>	<b>21</b>
The Act .....	21
Coverage .....	21

# **THE IMPACT OF THE ANTI-INFLATION PROGRAM**

Publication of this report marks the second anniversary of the government's Attack on Inflation. Over the two-year period significant progress has been made in reducing the rate of price and cost increases in Canada. This report covers the activities of the Anti-Inflation Board during the past year in the context of the general economic situation.

## **THE PROGRAM**

The Anti-Inflation Program consists of four main elements:

1. Fiscal and monetary policies aimed at increasing total demand and production at a rate consistent with declining inflation.
2. Policies aimed at limiting the growth of government expenditures and the rate of increase in public service employment.
3. Structural policies to deal with the special problems of energy, food and housing, to ensure a more efficient and competitive economy and to improve labour-management relations.
4. A prices and incomes policy establishing guidelines for responsible social behaviour in determining prices and incomes of groups, together with machinery for administering these guidelines and ensuring compliance where necessary.

The essential element of this program is the reduction in the rate of money supply and government expenditures growth. Without this the Anti-Inflation Program could not be successful, even in the short-run.

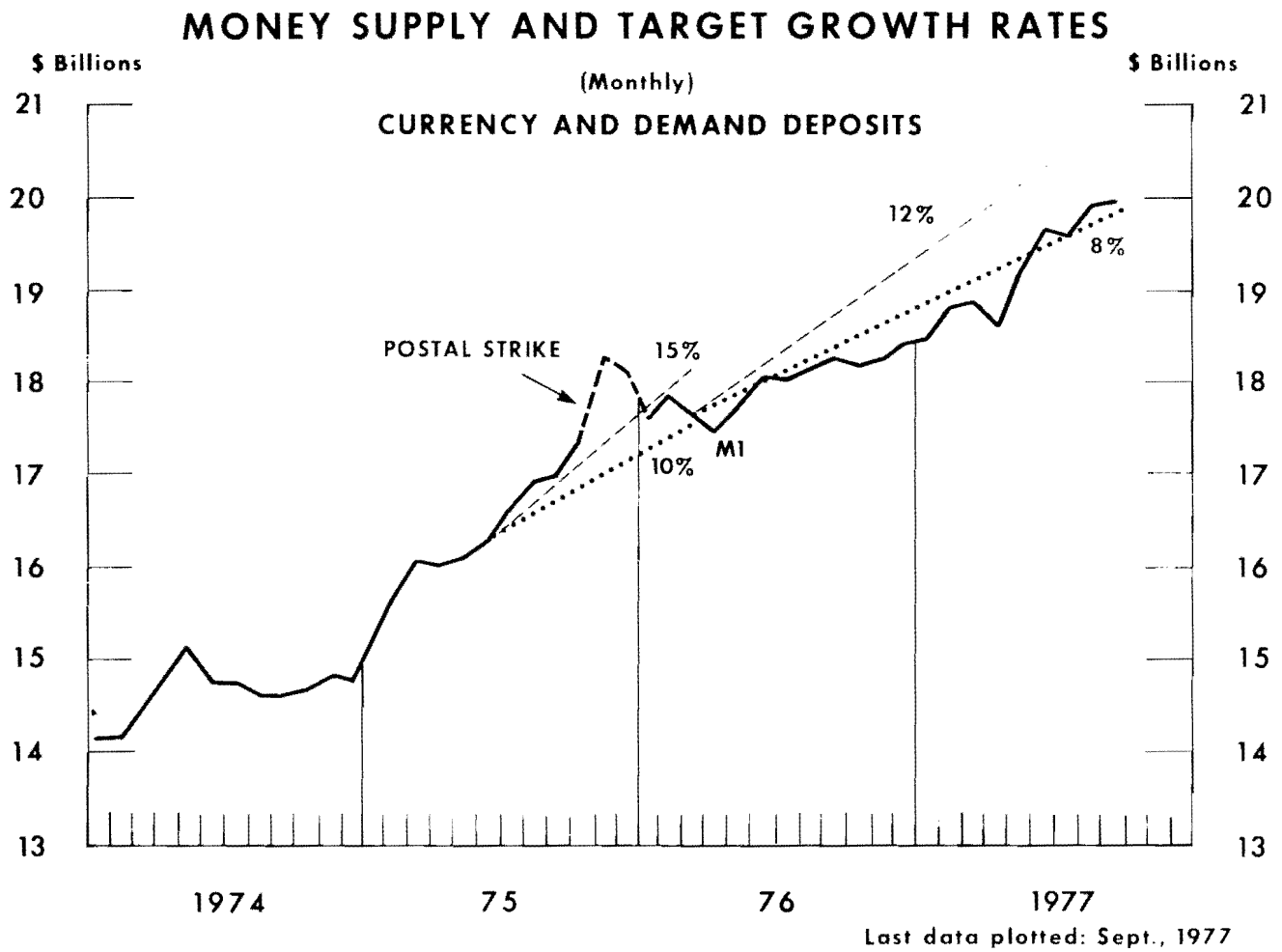
However, while restrained monetary and fiscal policies have an immediate impact on output and employment levels, there is a delay in the impact on prices and compensation. Thus temporary controls on prices and incomes were established with the aim of obtaining an immediate price and compensation response. Controls, therefore, were intended to be supplementary to the monetary and fiscal restraint, not to substitute for them.

The overall goal of this co-ordinated effort was to reduce the rate of inflation by about two percentage points per year.

## **THE PROGRAM AS IMPLEMENTED**

### **MONETARY POLICY**

Since mid-1974 there has been a marked deceleration in the overall growth rate of the money supply in Canada, although in late 1975 the mail strike effects on demand deposits tended to obscure the deceleration during that period. As shown in Chart 1.1, the money supply defined as currency and demand deposits (M1) has remained at the lower end of the target range for both the first and second set of targets enunciated by the Governor of the Bank of Canada in the autumn of 1975 and the summer of 1976. By September, 1977, M1 was only slightly above the level indicated for that month by the level of the target growth rates applicable to this period.



## GOVERNMENT EXPENDITURE POLICY

Also since 1975 there has been a marked deceleration in the growth rate of expenditure by all levels of government in Canada. As Table 1.1 indicates, spending has moved very sharply in the direction of restraint. Total spending through the first half of 1977 over the same period in 1976 was up by 9.9 per cent compared to 12.4 per cent in 1976, 22.3 per cent in 1975 and 24.2 per cent in 1974.

**TABLE 1.1**

**Government Expenditures National Accounts Basis  
(Percentage Changes)**

	1972	1973	1974	1975	1976	1977*
Federal Government	15.8	11.4	28.7	22.9	9.4	13.7
Provincial Governments	11.6	12.6	22.9	23.8	12.9	12.1
Local Governments <sup>1</sup>	7.5	12.3	18.1	19.0	14.8	7.4
Total Governments <sup>2</sup>	12.9	13.4	24.2	22.3	12.4	9.9

\* First half 1977 over first half 1976

<sup>1</sup> Including hospitals

<sup>2</sup> Including Canada and Quebec Pension Plan expenditures as well as net federal, provincial and local expenditures.

These developments are an important indication that since 1975 monetary and fiscal policies have been consistent with reducing the rate of inflation.

## MANDATORY CONTROLS

Since the mandatory controls were implemented in October, 1975, the Anti-Inflation Board and its staff have reviewed the compensation plans of some 3.8 million employees, and the price and profit reports from some 3,300 Canadian companies.

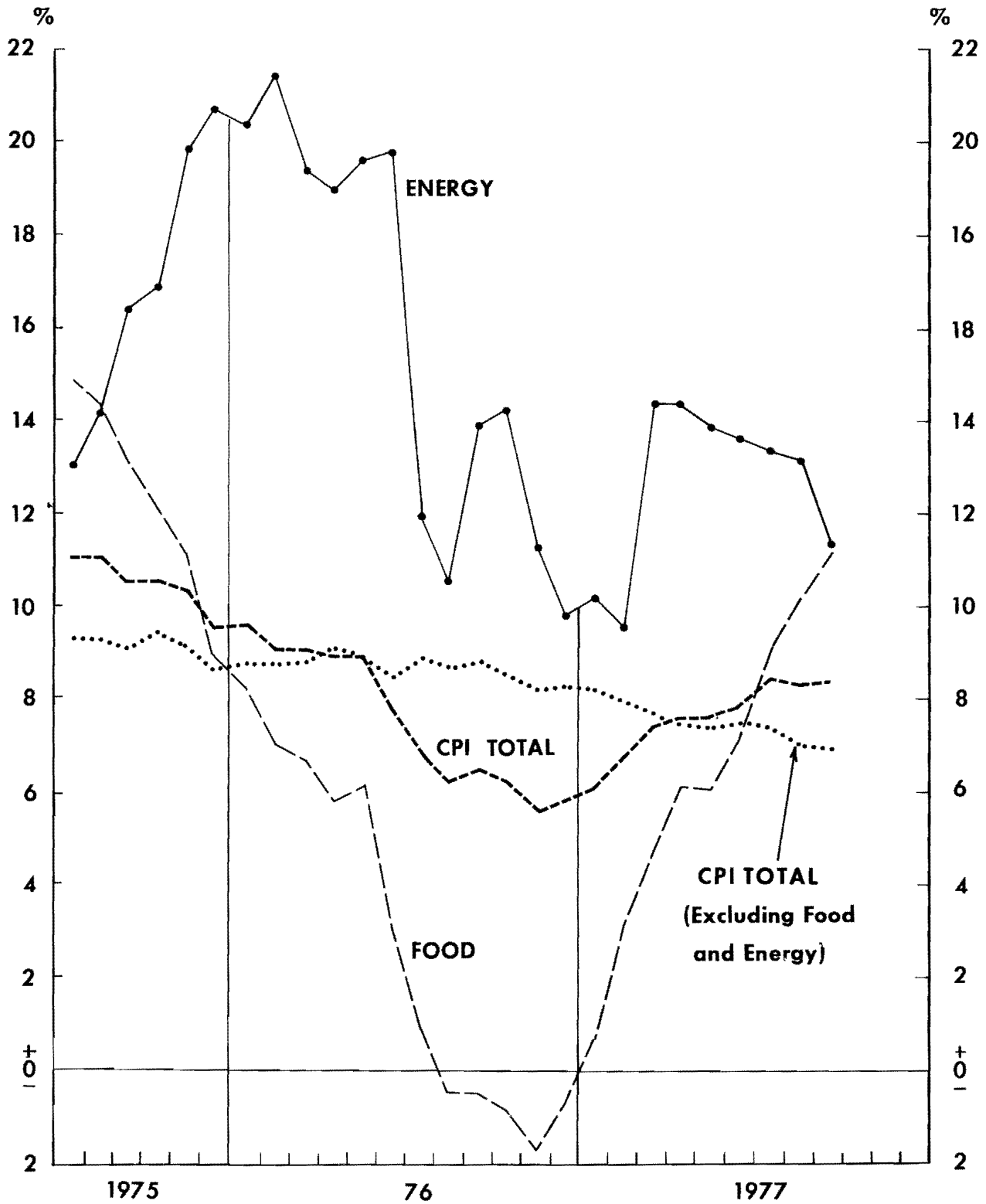
The compensation reports received to date by the Board indicate an increasing number are coming in within, or close to, the arithmetic guideline. By way of example, for the pre-program period—before October 14, 1975—compensation plans covering 77 per cent of the employees whose cases came before the Board contained proposed increases in excess of the arithmetic guideline. These were the compensation plans which took effect prior to October 14, 1975, but which were not settled before that date. However, during the first program year, the proportion coming in over the guideline dropped to 41 per cent, and for the second program year it dropped to 30 per cent. Thus, while the guideline itself is reduced in each program year, more and more proposed compensation increases are being submitted at or below the guideline.

The average amount proposed has also been declining, from 15.6 per cent for the pre-program period to 10.1 per cent in program year one and 7.8 per cent in program year two. More importantly, in those cases where the amount proposed has been over the guideline, the average excess amount proposed has itself declined, from 6.5 per cent for the pre-program period to 2.8 per cent for the first program year to 1.8 per cent for the second program year.

Price increases indicated by the larger firms, who are required by the Board to prenotify the AIB of proposed price increases, averaged 4.1 per cent during the first eight months of this year, down from an average of 6.9 per cent during the same period in 1976.

In addition, the price and profit reports received to date by the Board indicate that, throughout the life of the program, the average profit margin (the measure used to effect price restraint), has remained below the average target profit margin allowed by the guidelines. In aggregate, the companies reporting to the AIB were operating at 67 per cent of their target margins in the first compliance year, and at 51 per cent of their target margins in the second compliance year.

1.2  
**CONSUMER PRICE INDEX**  
**Monthly**  
**(YEAR OVER YEAR PERCENTAGE CHANGE)**



Last data plotted: Sept./77

## THE RESULTS

Since October, 1975, first year increases in base rates of major wage settlements have declined substantially. The average first year increase obtained in 1975 was 21.0 per cent. In 1976 the rate dropped to 12.3 per cent. During the first two quarters of 1977 the rate has averaged 8.5 per cent.

Broader measures of compensation for Canadian workers also show deceleration. For example, in the third quarter of 1975 average industrial earnings were up by 13.6 per cent over the same quarter in 1974. By the third quarter of 1976 the rate had declined to 11.7 per cent. During the latest three month period for which new data are available, ending in July, 1977, the rate of increase over the same three month period in 1976 declined to 9.7 per cent. Thus over the past two years the rate of increase in weekly earnings has decelerated by almost four full percentage points.

But, during the last two years, food, energy and import price movements have obscured somewhat the success that has been obtained in reducing the rate of inflation. In 1976 consumer prices for food fell, and import prices increased very little. This was reflected as an improvement in the overall rate of inflation as measured by the increase in the total Consumer Price Index. But in 1977 food and import prices increased substantially. This resulted in a more rapid increase in prices as measured by the total CPI. And during both years large energy price increases have added almost three-quarters of one per cent to the growth rate of inflation.

If food and energy prices are eliminated from the CPI the index left is more closely related to underlying cost developments in the Canadian economy. The average rate of growth of the CPI, excluding food and energy prices, is a fairly good measure of the overall rate of inflation that would prevail if the main determinant of price increases in Canada was the increase in domestic costs.

Using the usual procedure of calculating the inflation rate—the percentage increase in the price index over the period for the latest month available compared to the same month a year earlier—we find that consumer prices, exclusive of food and energy, have decelerated from a rate of increase of 9.5 per cent in October, 1975, to 8.5 per cent in October, 1976, and to 6.9 per cent in September, 1977. (See Table 1.2 and Chart 1.2).

**TABLE 1.2**  
**CONSUMER PRICE INDEX**  
**Percentage Change from Same Month a Year Ago**

	October 1975	October 1976	September 1977
Total Consumer Price Index	10.5	6.2	8.4
Food Prices	12.0	-0.9	11.2
Energy Prices	16.9	14.2	11.4
CPI excluding food and energy prices	9.5	8.5	6.9

A better indication of the most recent price trends is given by another procedure of calculating the inflation rate, which compares the average level for each index in a given half year to the average level of the same index in the previous half year, expressing the percentage change between subsequent half years at annual rates. This procedure shows that, during the first half of 1977 consumer prices, excluding food and energy, were increasing at an annual rate of 6.5 per cent, well down from the rates of 8.8 to 8.9 per cent that had existed over the previous year and a half\*. (See Table 1.3).

\* During the third quarter of 1977, compared to the second quarter of 1977, the CPI excluding food and energy increased at an annual rate of 6.3 per cent.



**TABLE 1.3**  
**CONSUMER PRICE INDEX**  
**Percentage Change from Previous Half-Year at Annual Rates**

	1975		1976		1977
	1st half	2nd half	1st half	2nd half	1st half
Total Consumer Price Index	9.7	11.4	6.3	6.2	8.4
Food Prices	10.6	14.1	-1.2	0.1	9.3
Energy Prices	8.0	26.5	13.7	10.1	15.3
CPI excluding food and energy prices	9.5	8.9	8.8	8.9	6.5

This table indicates clearly that there has been a marked deceleration taking place in the underlying rate of price increases. At the same time, one of the major underlying costs in the economy, unit labour costs, increased by 9.6 per cent in 1976, and by 6.3 per cent at annual rates during the first half of 1977 compared to the second half of 1976.

### **IMPACT OF THE PROGRAM**

It was anticipated that the Anti-Inflation Program would show early success through its mandatory controls aspect with the impact of the restrained monetary and fiscal policies not expected to be felt as strongly until later in the program. Quick deceleration of first year increases in major wage settlements within six months of the program's announcement, at a time when the economy was still growing at a fairly reasonable pace, is evidence that this was the case. That deceleration resulted mainly from the impact of the 10 per cent average compensation guideline.

It was also anticipated that, over time, the impact on the market of monetary and fiscal restraint would be felt more. Average proposed increases in compensation moving closer to the arithmetic guidelines, and average price prenotification generally below the guidelines, particularly in the second year of the program, are evidence that this influence is being felt.

As time passes there is increasing room for debate about the amount of separate impact that the controls are having on prices and incomes. However, it is clear that the combination of fiscal and monetary policies and the controls has achieved an improvement in the rate of inflation that is broadly consistent with the targets of the Anti-Inflation Program.

### **THE THIRD YEAR AND AFTER**

Real output growth in Canada is expected to accelerate during the final half of 1977, and for 1978 an overall growth rate higher than that of 1977 is likely. But the acceleration in growth is unlikely to significantly reduce the current levels of unused physical capacity and unemployment. Thus it is unlikely that demand pressures in 1978 will develop in a manner which would lead to any acceleration in the rate of inflation.

At this time prices on world commodity markets are relatively stable. Over the past six months most commodity prices have tended to decline, a reflection of the general softness of the economic recovery in the industrial world. Future prospects for that recovery suggest that commodity prices should remain relatively stable, although as yet the depreciation of the Canadian dollar on exchange markets has not been fully reflected in Canadian prices.

Current indicators of future agricultural commodity prices suggest that food prices paid by consumers will not rise as much in 1978 as they did in 1977. Food price forecasting is always a hazardous endeavour; however, at this time the outlook for consumer food prices is relatively bright.

In view of these 1978 prospects for the more favourable impact of international developments on Canadian prices, and for an overall lack of demand pressures, the stage is set for the achievement of further deceleration in the rate of inflation.

## **Chapter 2**

# **COMPENSATION**

Since October, 1975, there has been a general decline in rates of increase in compensation. This is indicated in the marked decline in the rates of increase in collective agreements and in other indicators of rates and earnings, as well as the increases submitted to the Board. The deceleration that has occurred has been of the magnitude anticipated at the start of the program.

## **COMPENSATION GUIDELINES**

The first full year of application of the AIB compensation guidelines ended October 13, 1976. A number of changes were made to the compensation regulations effective in October, 1976.

The more significant changes involved:

- an amendment which allowed wages or salaries of lower paid employees to be increased to \$3.75 per hour even if this resulted in an increase greater than provided for in the arithmetic guidelines;
- an amendment which permitted the exclusion of employer expenditures incurred in the introduction of a pension plan where none previously existed;
- simplification of the regulations regarding the upgrading of existing pension plans;
- an amendment to provide additional options in the selection of a base period for employee groups under bonus, profit sharing or other indirect incentive plans;
- clarification of the point that compensation plans which were in effect before October 14, 1975, and reopened after that date are subject to the regulations.

In addition to these changes, all companies which bargain in association in the forest, food and metal fabricating industries in British Columbia were brought under controls by an Order-In-Council on March 30, 1977.

Overall, these changes did not alter significantly the method of calculating compensation increases and applying the guidelines.

The Board later drew the attention of employers and employee groups to the provisions for exclusion of increases in compensation that eliminate discrimination based on the sex of employees. A statement of the Board's policy and a technical bulletin, which describes the methods to be used to calculate the amounts to be excluded, were issued September, 1977. No changes in the regulations, which already contained provision for such exclusions, were involved.

## **THE RESPONSE**

The compensation guidelines have now been in effect for two years. In the period between October 14, 1975, and September 9, 1977 a total of 57,752 compensation plans covering 3.8 million employees were submitted to the Anti-Inflation Board. On average approximately 3,400 compensation reports were received each month by the Board during the second program year.

Of the compensation plans submitted, about 50,000 plans covering 3.4 million employees have been subjected to computer analysis. Approximately two-thirds of these plans have been at or below the arithmetic guidelines, while one-third have been beyond the guidelines.

**TABLE 2.1**

**Compensation Increases Submitted to the AIB<sup>1</sup>**  
**(AIB-2 reports submitted by September 9, 1977)**

	AT OR BELOW PERCENTAGE GUIDELINES		ABOVE PERCENTAGE GUIDELINES	
	No. of Employees	No. of Compensation Plans	No. of Employees	No. of Compensation Plans
Pre-Program <sup>2</sup> before Oct. 14, 1975	53,330 (22.6%)	341 (35.9%)	182,986 (77.4%)	608 (64.1%)
Program Year I Oct. 14, 1975 to Oct. 13, 1976	1,846,205 (59.3%)	19,018 (66.9%)	1,267,478 (40.7%)	9,412 (33.1%)
Program Year II Oct. 14, 1976 to Oct. 13, 1977	1,714,231 (70.3%)	13,468 (70.7%)	724,449 (29.7%)	5,586 (29.3%)
Program Year III <sup>3</sup> Oct. 14, 1977 to Oct. 13, 1978	127,089 (51.5%)	459 (42.0%)	119,561 (48.5%)	633 (58.0%)

<sup>1</sup> *These figures describe the status of proposed increases at the time of their submission to the Board. After review by Board staff, some increases which first appeared to be above guidelines were found to be at or below guidelines. Other increases, at or below guidelines in one program year, required a Board decision because part of the compensation plan, effective in a different program year, exceeded the guidelines.*

<sup>2</sup> *Compensation plans commencing before 14 October, 1975, but not agreed to until after that date.*

<sup>3</sup> *In view of the relatively limited coverage, these figures may not be fully representative of the experience in the third year of the program.*

On average, compensation increases submitted to the Board moved closer to the arithmetic guidelines during the second program year. Table 2.2 shows how the difference between the guidelines and the average increases submitted has dropped from a figure of 4.7 per cent for plans effective in the pre-program period prior to October 14, 1975, to 0.1 per cent for plans effective in the second year of the program.

**TABLE 2.2**

**Compensation Increases Submitted to the AIB and  
Average Arithmetic Guidelines by Program Year  
(AIB-2 reports submitted by September 9, 1977)**

	No. of Employees	No. of Compensation Plans	Average Percentage Increase Submitted <sup>1</sup>	Average Percentage Arithmetic Guideline
Pre-Program before Oct. 14, 1975	236,316	949	15.6	10.9
Program Year I Oct. 14, 1975 to Oct. 13, 1976	3,113,683	28,430	10.1	9.7
Program Year II Oct. 14, 1976 to Oct. 13, 1977	2,438,680	19,054	7.8	7.7
Program Year III <sup>2</sup> Oct. 14, 1977 to Oct. 13, 1978	246,650	1,092	5.8	5.6

<sup>1</sup> *These data reflect increases as reported to the AIB for purposes of the compensation restraint program and do not include expenditures excludable under the regulations.*

<sup>2</sup> *In view of the relatively limited coverage, these figures may not be fully representative of the experience in the third year of the program.*

Compensation plans effective in the pre-program period consist largely of agreements which had not been reached by October 14, 1975. They tend to reflect the expectations present in that period and the fact that many of the groups involved had an historical relationship with other groups which had signed agreements before the introduction of controls.

Compensation plans effective in program years one and two are more representative as they include more completely that proportion of employees for whom increases are determined unilaterally by management.

Compensation plans which take effect during the third program year represent, for the most part, a mix of the second and third years of two or three year plans. In a multi-year agreement the second and third years tend to involve a lower increase than the first. To date the Board has received a relatively small number of plans effective in the third program year. It is difficult to assess whether these figures indicate what will happen in the third year. This should be kept in mind in interpreting references to the third program year in this report.

## THE RESULTS

To September 9, 1977, the Board had decided on 11,558 cases which contained increases in excess of the arithmetic guideline in at least one year of the submission.

**TABLE 2.3**  
**Board Decisions—By Program Year<sup>1</sup>**

	No. of Employees	Average Percentage Increase Submitted	Average Percentage Guideline	Average Percentage Increase Allowed
Pre-Program before Oct. 14, 1975	180,516	17.3	10.5	14.8
Program Year I Oct. 14, 1975 to Oct. 13, 1976	1,386,057	12.1	9.1	10.1
Program Year II Oct. 14, 1976 to Oct. 13, 1977	873,697	8.7	7.4	7.5
Program Year III <sup>2</sup> Oct. 14, 1977 to Oct. 13, 1978	153,650	6.2	5.7	5.8

<sup>1</sup> Some decisions involved multi-year compensation plans which were at or below guidelines for one year and above guidelines for another. Because all years of the plan were reviewed together, the number of employees affected by Board decisions in each program year will include some whose proposed increases for a particular year were within guidelines.

<sup>2</sup> In view of the relatively limited coverage, these figures may not be fully representative of the experience of the third year of the program.

In the second year of the program, Board decisions moved closer to the arithmetic guidelines. The transition into controls took place for most groups during the first program year, when many sought increases above guidelines to maintain historical relationships. There was less likelihood or justification for such increases during the second year.

In addition to the arithmetic guidelines, there is an upper limit of \$2,400 on the increase in the average annual compensation of a group of employees. The Board has decided on 535 compensation plans covering 23,609 employees in which the average proposed increase exceeded the \$2,400 limit. The average increase approved by the Board in these cases was \$2,411.

The Anti-Inflation Act provides that either of the parties to a compensation plan may, if they are dissatisfied with a recommendation of the Board, request that the matter be referred to the Administrator of the Anti-Inflation Act. In law, "decisions" of the Board are actually recommendations. The Administrator has a mandate to enforce the guidelines, and Orders of the Administrator are decisions which are binding in law.

By the end of September, 1977, compensation plans covering 152 groups had been referred to the Administrator. Of these, 151 were referred at the request of one or both of the parties and one was at the request of the Board.

During the second year of the program the Board initiated a series of compensation plan audits. These covered compensation plans for employee groups in most industry sectors.

The Board is focusing particular attention on executive compensation and is reviewing its procedures and practices to ensure that the guidelines are being observed. A detailed review of a number of compensation plans for executive groups is nearing completion and special field audits are being undertaken.

Table 2.4 summarizes what has happened to the rates of increase in compensation during controls. The "effective rate" shown in the table takes into account both those increases which were within guidelines and Board decisions on those above guidelines. The effective rate of increase has continued to decline over the life of the program.

**TABLE 2.4**  
**Effective Rate of Compensation Increases to Date**  
**and Average Arithmetic Guideline by Program Year**  
**(Data covering the period ending on September 9, 1977)**

	No. of Employees	Average Percentage Arithmetic Guideline	Effective Percentage Rate of Compensation Increases
Pre-Program before Oct. 14, 1975	233,846	10.6	13.5
Program Year I Oct. 14, 1975 to Oct. 13, 1976	2,834,421	9.7	9.4
Program Year II Oct. 14, 1976 to Oct. 13, 1977	2,261,271	7.8	7.4
Program Year III <sup>1</sup> Oct. 14, 1977 to Oct. 13, 1978	221,578	5.7	5.4

<sup>1</sup> *In view of the relatively limited coverage, these figures may not be fully representative of the experience of the third year of the program.*

Most groups have complied with the spirit and intent of the guidelines. However, in a few cases, written commitments, which have come to be referred to as "AIB clauses", have been made which provide for the reopening or the restoration of any wage rollback or some form of increase as soon as the controls are ended or a group has emerged from controls. It would be unfair to the large majority of employees who have complied with the program if some action were not taken to deal with these clauses. The Board has been concerned about this problem and has recommended that legislation be introduced to nullify such provisions where they appear.

The Board is satisfied with progress to date in reducing the rate of compensation increases. Nonetheless, it realizes that compliance with the law during controls must be distinguished from acceptance of the need for continued moderation in the future.

# PRICES AND PROFITS

Since October, 1975, both the Consumer Price Index and the Industry Selling Price Index reflect on the whole, a decline in the rate of increase. However, the declining trend in prices has been somewhat obscured in recent months. This has been caused by adverse weather conditions in the United States that disrupted the supply of fresh fruit and vegetables and the decline in the value of the Canadian dollar. Average price increases submitted to the Board under pre-notification arrangements declined from some 7.5 per cent in the early months of 1976 to about 4.5 per cent a year later and to less than 4 per cent in August, 1977.

## PRICES AND PROFITS GUIDELINES

Canadian companies reporting to the AIB are required to make pricing decisions so that profit margins permitted under the regulations of the Anti-Inflation Act are not exceeded. Price increases must also be reasonably consistent with increases in associated costs. In general, prices that are too high relative to costs of profit margins will generate excess revenue which must be returned to the market by price reduction, refunds to customers, price freezes or payments equalling the amount of excess revenue to the government.

The experience with the original guidelines in early 1976 resulted in changes to the regulations which were introduced in October, 1976. The new regulations represented a simplification of the rules and applied generally for the third compliance period. The more important changes were:

- a shift from the two control regimes (cost pass through or profit margins), to a generalized application of the profit margin control;
- the introduction of a choice of two time periods on which to base allowable profit margins;
- the introduction of a special credit designed to induce greater investments;
- the introduction of a minimum rate of return of 8 per cent on equity applicable to all suppliers regardless of past experience;
- the introduction of a provision that price increases in a compliance period must be reasonably consistent with increases in associated costs in the same compliance period.

## REPORTING AND COMPLIANCE

The Board employs two methods to monitor compliance with the prices and profits guidelines:

- major firms are required to provide advance cost and profit information on proposed price increases. This serves as an early warning system concerning developing price pressures and enables both the Board and the suppliers to analyse and determine allowable price increases in the light of the restraint rules.
- all firms subject to guidelines file a report with the Board on their revenues, costs and profits either quarterly or annually or both. Profit restraint rules are applied to either the firm as a whole, or to parts of its business or product lines.

## PRICE PRE-NOTIFICATION

The group of firms required to pre-notify the Board of significant price increases has been expanded several times during the program. In January, 1976, the group numbered 117, but by June, 1977, had increased to 342, including the addition of 44 food processing companies.

Beginning in January and through to the end of December, 1976, approximately 1,300 price pre-notification applications were filed with the Board. Average requested price increases by month ranged from 8.6 per cent in January and February, 1976, to 4.3 per cent in August, 1976, for an overall 1976 average increase requested of 6.8 per cent.

During the first eight months of 1977, price pre-notifications filed had average requested increases of 4.1 per cent. During the comparable period a year ago, the average requested price increase submitted to the Anti-Inflation Board was 6.9 per cent.

**TABLE 3.1**  
**Average Percentage Pre-Notified Price Increases by Month**

	1976	1977
January }	8.6	4.2
February }		4.6
March	6.7	4.1
April	6.2	3.0
May	7.9	5.1
June	6.7	3.9
July	6.0	4.4
August	4.3	3.8
September	5.2	
October	6.2	
November	7.4	
December	7.5	

Most of the applications received to date have been consistent with the guidelines and have not required Board action. However, there have been some cases which involved either full or partial rollbacks. In many other cases, firms, considering price increases which might have resulted in excess revenue, consulted Board officials before making a formal pre-notification and often moderated their requests.

## **PROFIT MARGINS**

Suppliers' reports submitted to the Board indicate that most firms have either adjusted their prices in order to comply with the guidelines, or have been unable to increase their prices because of market conditions. Market conditions have been such that many firms have not been able to pass on all cost increases and have experienced, as a result, a decline in profit margins. As reported by Statistics Canada (Industrial Corporations: Financial Statistics 61-003), average profit margins of industrial corporations declined in 1976 to 5.18 per cent from 6.14 per cent in 1975 and from 7.19 per cent in 1974. There was a further decline in the first two quarters of 1977.

The Board's own information indicates an even larger decline in profit margins in 1976. Out of the total compliance population of about 3,300 reporting units (firms or groups of firms) reports for some 2,000 respondents covering the base period, and first and second compliance periods have been processed for the Board's statistical base. This group of respondents had total revenue from operations in the second compliance period (1976) of \$136 billion or some 85 per cent of the total revenue of all firms subject to mandatory compliance.

Profit margins of the firms under mandatory compliance declined in 1976 faster than those of all industrial corporations; 25 per cent versus 15 per cent respectively. This difference is not explained solely by the effects of the guidelines for much of it may have resulted from different industry mix and/or firm-size mix of the two groups. In aggregate, the compliance population was operating at 67 per cent of target profit margins in the first year and at 51 per cent during the second compliance year. The proportion of the population operating at 90 per cent or more of target margins declined from 38 per cent in 1975 to 20 per cent in 1976.

The decline in profit margins has resulted both from the generally soft market conditions and, to a lesser extent, from the impact of the mandatory guidelines. It is not possible to estimate the separate impact of the controls but the information in Table 3.2 suggests that about one-fifth of business profits were in 1976 being restrained by the controls program itself.

Furthermore, prevailing industry structures and competition among firms appear to have extended this restraint indirectly to at least another fifth of Canadian business profits under compliance in 1976.



It must be recognized that the levels of profit margins in Canada are now rather low in relation to long-run averages. As the economy strengthens and the volume of business rises, profit margins will recover. This is desirable in order that businesses may have the financial resources and the incentive to expand and provide the basis for strong growth of output and job opportunities.

**TABLE 3.2**  
**Profit Margins by Type of Regime**

	Distribution	Non-Distribution	
		Unit Cost	Net Margin
	(millions of dollars)		
<b>Base Period</b>	<b>1974</b>	<b>1974</b>	<b>1970-74</b>
—Gross Revenue	27,638	14,997	138,529
—Adjusted Operating Profit (Loss)	1,311	1,780	10,850
—Margins (%)	4.74	11.87	7.83
<b>First compliance Year</b>	<b>1975</b>	<b>1975</b>	<b>1975</b>
—Gross Revenue	31,047	16,503	43,637
—Adjusted Operating Profit (Loss)	1,183	1,533	2,306
—Margins (%)	3.81	9.29	5.28
<b>Second Compliance year</b>	<b>1976</b>	<b>1976</b>	<b>1976</b>
—Gross Revenue	33,737	18,582	48,049
—Adjusted Operating Profit (Loss)	896	1,030	2,206
—Margins (%)	2.66	5.54	4.59

The guidelines which have been in force since the beginning of the third compliance year (for most firms 1977) include a credit, in the form of an increased target margin, specifically designed to induce greater business investments in 1977 and 1978. According to the information collected under this provision, there seems to be little evidence to support claims that investment intentions for 1977 were curtailed as a result of controls.

## EXCESS REVENUE

Under the program firms are required to follow a pricing policy which allows them to pass on to the market place their allowable costs plus a percentage margin of profit limited by the guidelines (the target margin).

A firm may find itself with "excess revenue" as the result of a variety of factors, but is usually not considered to have contravened the Anti-Inflation Act because it is in such a position. Rather, it is a situation which must be corrected for the firm to achieve compliance with the program.

To August 19, 1977, some 553 cases of excess revenue involving about \$109 million have been made public by the Board. In each case, compliance plans stating the manner in which the excess revenue will be returned to the market have been filed with the Board. The plans include price reductions on specific products and product lines, price freezes and a combination of price cuts, discounts or customer refunds along with absorption of rising costs.

Statistics on excess revenue do not provide a measure of the full restraining effect of the program. Many of the firms with excess revenue may well have raised prices had there been no rules.

Furthermore, numerous suppliers exercised restraint to keep within the guidelines even though market conditions would have allowed higher prices. And some firms, who would otherwise have been free to increase prices, were unable to do so because competitors' prices were restrained by the rules.

## DIVIDENDS

The Board, as of August 2, 1977, has reviewed 315 dividend cases, the majority of which involved requests for increases in dividends above the guidelines. In total, these requests involved payments of \$472 million in excess of amounts permitted by the guidelines. Of this amount, \$370.5 million (representing 105 cases) was disallowed or rolled back by the Board.

**TABLE 3.3****Decision on Dividend Cases**

Period	Number of Cases Reviewed	Amount of Excess Dividend Payments (million)	Amount of Dividend Payments Disallowed or Rolled Back (million)
Oct. 14, 1975 to Oct. 13, 1976	190	398	348.8
Oct. 14, 1976 to Aug. 2, 1977	125	74	21.7
Total	315	472	370.5

**PROFESSIONAL FEES AND INCOMES**

The AIB guidelines impose control on fees and incomes earned by professional practitioners. To effect such control, professional firms must demonstrate compliance with the guidelines by either a fees or a profit test.

To date, 31,850 firms have reported for the first compliance year. Some 29,000 of these elected to demonstrate compliance under the fees test. Approximately half of them were medical doctors adhering to provincially negotiated medicare fee schedules approved by the Board. The remaining 2,850 firms utilized the profit test to maintain compliance. Staff of the Board has undertaken some 600 audits of first compliance year reports. The findings are being analysed and it is expected that a small number will be found to have contravened the guidelines, necessitating the filing of a compliance plan with the Board.

Table 3.4 presents percentage changes in net incomes for all professional firms reporting (other than medical doctors covered by provincial medical fee schedules). The first compliance year percentages are more representative of the pre-controls time than of the controls period as the guidelines applied to less than one-third of the reporting period. Some 17,000 firms have now reported for the second compliance year. Notwithstanding the relatively smaller size of the second compliance year sample, this information shows there has been a slow-down in the rate of increase of professional incomes in 1976. The principal factors behind the declines experienced by architects and engineers, and the small income gains in the case of accountants and lawyers are generally a weak economy coupled with declining demand. The large decline in the rate of net income increases for dentists stems in part from a strong slowing down of fee increases. The Ontario dental fees, for example, showed one of the largest declines, dropping from 17 per cent in 1975 to 10 per cent in 1976 and to 4.6 per cent in 1977. Table 3.5 shows the medical fee schedules approved by the Board during the first and second compliance years. Rates of increase in fees declined significantly in every provincial jurisdiction between 1976/77 and 1977/78.

**TABLE 3.4**  
**Percentage Changes in Net Incomes**  
**of**  
**Professional Practitioners by Category**

Profession	Percentage Change in First Compliance Period	Percentage Change in Second Compliance Period <sup>1</sup>
Architects	3.4	-17.0
Chiropractors	6.8	5.3
Consultants	10.2	6.6
Dentists	17.3	8.6
Engineers	1.8	-14.7
Lawyers	8.9	1.9
Physicians <sup>2</sup>	5.5	2.2
Optometrists	9.3	6.0
Accountants	9.9	1.0
Veterinarians	5.9	5.9
All Professions	9.1	0.7

<sup>1</sup> Preliminary second compliance year date as at September 8, 1977.

<sup>2</sup> Includes physicians from Ontario only who do not adhere to the provincial fee schedule. Some 5,370 firms of M.D. s in Ontario elected to adhere to the provincial fee schedule approved by the Board, and thus did not have to submit figures on revenue, cost, and net income. In the rest of the country only a handful of M.D. s had to submit revenue and cost figures; in other words they practically all adhere to provincial fee schedules approved by the Board (see Table 3.5).

**TABLE 3.5**  
**Provincial Medical Payment Schedule**  
**Increases Approved by the Board**

Province	1976/77 Per Cent Increase	1977/78 Per Cent Increase
Newfoundland	7.50	*
P.E.I.	7.82	6.40
Nova Scotia	8.11	4.00
New Brunswick	7.78	6.30
Ontario	8.10	6.50
Quebec <sup>1</sup> (G.P.s	11.70	6.20
(Specialists)	17.50	Nil
Manitoba	9.15	6.80
Saskatchewan	7.44	6.90
Alberta	9.00	7.00
B.C.	8.16	*

<sup>1</sup> Quebec's fee schedule for "specialists" had not been changed since it expired on December 15, 1970. The schedule for G.P.s was last increased on July 1, 1972.

\* Submissions not yet received.

## **Chapter 4**

# **OPERATIONS**

## **COMMUNICATIONS**

The Anti-Inflation Board has, from its inception, devoted much energy toward public communication. Broadly, this has been with two objectives:

- to maintain public awareness of the activities, requirements and decisions of the Board;
- to promote better understanding of the inflationary processes and their dangers, in keeping with the duties of the Board as expressed in the Anti-Inflation Act.

In the first year, public communication work was, of necessity, aimed primarily at those who had to comply with the program: businesses, employee representatives and professional people.

In the second year, this type of communication need lessened and the emphasis swung to the public at large, its understanding of inflation and preparation for the decontrol and post control periods. A wide variety of communication methods have been employed. Some examples are:

- more than 400 appearances have been made by Board Members and officials on radio and television public affairs and open line shows;
- Board Members, officials and special advisors have combined to give more than 850 public speeches in about 250 Canadian communities;
- a consumer information bulletin containing material directly related to the AIB, consumer costs and prices, goes out to daily and weekly newspapers each week. Radio stations also receive this material and taped interviews with officials support the printed articles;
- a public information unit has handled some 77,000 complaints and enquiries from Canadian citizens since the start of the program;
- a 24 page publication "Inflation Debator" was prepared and used as a classroom teaching aid right across Canada. The publication described inflation, experiences of other countries, dangers and cures. More than 500,000 Canadian students received copies as a result of requests from their own teachers;
- 50,000 copies of the 36 page publication "Kick the Inflation Habit" were distributed;
- a workbook, "Conversations for Economic Change", was prepared for special interest organizations to promote public discussion by groups.

Future plans include additional material for classroom study, acceleration of distribution of material to the public at large, and considerable expansion of the group discussion program.

## **RESEARCH**

The functions of the Economic Research Branch are:

- to advise the Board on all economic questions, including the economic impact of the Board's operations, the economic implications of the Board's policies, and the economics of the Anti-Inflation Program in general;
- to carry out research (or cause it to be carried out) both to assist the Board to operate its program and to promote public understanding of the inflationary process, the relationship between productivity, costs and prices and the various policies of government to deal with inflation.

To date five studies have been launched to provide a continuing assessment of the effects of the controls program on the economy. In addition 18 research projects have been undertaken to improve understanding of the inflationary process. Occasional papers containing the results of this research will be published by the Board as the projects are completed.

The following discussion papers have been completed:

- Wage Determination in the Public Sector
- Interdependence and Inflation
- The Structure of Earnings by Occupation in Canada 1931-74
- The Effect of Inflation on Household Expenditures
- An Analysis of the Effectiveness of U.S. Wage and Price Controls and Implications for Operation of the Canadian Program
- The Effect of Direct Taxes on Wages
- La transmission internationale de l'inflation.

## ADMINISTRATION

Year two of the AIB is the first complete year of operation at full capacity. Year one included a start-up period as the AIB went from zero staff in October, 1975, to 447 at the end of March, 1976, to 856 at year end. During the first year, a large number of employees were loaned without charge to the Board by other federal government departments. However, in the second year of operation, the Board was required to reimburse home departments for the payroll costs of the borrowed employees. As a result, the average number of employees being paid from Board budgets almost doubled, resulting in a corresponding increase in payroll costs.

Staff numbers were relatively constant throughout the second year, starting at 856, peaking at 917 in March, 1977, and declining to 795 at the end of September, 1977. The March, 1977, staff peak of 917 was attributable to the increased workload connected with the influx of end-of-calendar year price and profit reports that were received by the Board. This anticipated influx was handled by a corresponding increase in the number of short-term staff.

While the flow of reports has remained somewhat above the September, 1976, level, further development and refinement of processing systems and procedures enabled the Board to operate at a staff level of 61 employees lower at the end of September, 1977, than a year ago.

The Board has kept the number of indeterminate (under the Public Service Employment Act) appointments as low as possible in order to minimize the impact of AIB staff on the long term size of the Public Service. Consequently almost one-half of the AIB staff is employed on a short-term basis.

Although costs have, in general, increased, there were savings made in the communication program, in repair and upkeep activities and in the purchase of machinery and equipment. During the first year, many of the expenditures in this area were one-time costs associated with implementing the program, and were not necessary in the second year.

**TABLE 4.1**

### Staff Numbers by Quarter

	End of Sept. 76	End of Dec. 76	End of Mar. 77	End of June 77	End of Sept. 77
Indeterminate	415	450	448	450	415
Secondments	100	63	52	28	22
Executive Interchange	37	38	33	28	26
Other	304	318	414	363	332
<b>Total</b>	<b>856</b>	<b>869</b>	<b>917</b>	<b>869</b>	<b>795</b>

Note—Indeterminate: Appointment under Public Service Employment Act.

Secondments: Employees loaned from other departments.

Other: Term appointment, contract and agency.

**TABLE 4.2**

**Projected Expenditures by Object of Expenditures  
for the 12 Months Ending October 31, 1977**

	<b>(\$000's)</b>
Salaries	13,956
Transportation and Communications	1,343
Information	703
Professional and Special Services	7,265
Rentals	291
Repair and Upkeep	57
Utilities, Materials and Supplies	544
Machinery and Equipment	13
	<hr/>
	24,172

## **APPENDIX ON OPERATIONS**

### **THE ACT**

The program went into effect on October 14, 1975, and the Interim Anti-Inflation Board was formed immediately, initially under authority of the Inquiries Act. Two months later, the Anti-Inflation Act (S.C. 197 — C 75) received final parliamentary approval and Royal Assent. The Act provided for the Anti-Inflation Board to administer the guidelines, an Administrator to investigate and enforce compliance where necessary, and a Tribunal to hear appeals from the Administrator's rulings. References to the Administrator are made by the AIB at the request of a party or parties affected by an AIB recommendation, or by the AIB itself in the case of an actual or likely contravention of the Anti-Inflation Guidelines.

The Anti-Inflation Act requires the Board to:

- monitor changes in prices, profits, compensation and dividends in relation to the guidelines;
- identify actual and proposed increases in prices, profits, compensation and dividends that the Board feels contravene the letter or spirit of the guidelines;
- identify the causes of such increases that are likely to have a significant impact on the Canadian economy, and seek through consultation and negotiation with the parties involved to modify such changes to bring them within the guidelines or reduce their inflationary impact;
- refer the matter to the Administrator in cases where the Board's persuasive efforts have failed to bring increases within the guideline limits and where the Board does not find that the circumstances justify the increase; or where the Board is advised in writing of a dissatisfaction by the party or parties involved in a change in prices, profits, compensation or dividend;
- promote public understanding of the inflationary process, the policies available to government to deal with inflation, and the role to be played by businesses and employee groups; and
- monitor the effectiveness and workability of the guidelines, and recommend improvements to the government.

### **COVERAGE**

The anti-inflation guidelines apply to everyone, and all Canadians are expected to comply with them. Certain major groups are required by law to do so:

- firms with 500 or more employees in Canada including associated firms;
- firms in the construction industry with 20 or more employees in Canada, and professionals;
- firms considered to be of strategic importance to the Anti-Inflation Program, and those involved in association bargaining may also be made subject to mandatory guidelines; and
- employees of controlled firms as well as those of federal government departments, agencies and corporations, and of provincial and municipal governments and their agencies.