BUDGET ANALYSIS

Canada: Budget 2017

A Stay-the-Course Budget for Canada's 150th Birthday Year

HIGHLIGHTS

- Despite the introduction of several new initiatives, the financial impact of the measures announced in Budget 2017 is fairly limited. Admittedly, the 2016 budget had done a lot of the heavy lifting by reducing the tax burden for certain types of households and introducing a major infrastructure investment plan, leaving the government with little room to manoeuvre.
- The measures introduced in Budget 2017 emphasize long-term results and primarily aim to strengthen the middle class.
- The budget projections are similar to those set out in last year's budget. A deficit of $23.0B is anticipated for 2016–2017, followed by a $28.5B deficit in 2017–2018. A gradual improvement in the budgetary balance is expected thereafter.
- The debt-to-GDP ratio, which was 31.0% at March 31, 2016, should peak at 31.6% as at March 31, 2019 and then decline to 30.9% by March 31, 2022.

TABLE 1
Summary of transactions

	ACTUAL	PROJECTIONS					
IN $B (EXCEPT IF INDICATED)	2015–2016	2016–2017	2017–2018	2018–2019	2019–2020	2020–2021	2021–2022
Budgetary revenues	295.5	292.1	304.7	315.6	327.7	340.3	356.0
Variation (%)	*4.7*	*-1.2*	*4.3*	*3.6*	*3.8*	*3.8*	*4.6*
Program spending	-270.8	-290.9	-305.4	-313.7	-319.8	-328.6	-338.5
Variation (%)	*6.7*	*7.4*	*5.0*	*2.7*	*1.9*	*2.8*	*3.0*
Debt charges	-25.6	-24.3	-24.7	-26.3	-28.3	-30.4	-33.3
Variation (%)	*-3.8*	*-5.1*	*1.6*	*6.5*	*7.6*	*7.4*	*9.5*
Adjustment for risk	---	---	*-3.0*	*-3.0*	*-3.0*	*-3.0*	*-3.0*
Budgetary balance	-1.0	-23.0	-28.5	-27.4	-23.4	-21.7	-18.8
Federal debt[1]	616.0	637.1	665.5	692.9	716.3	738.1	756.9
Variation (%)	*0.6*	*3.4*	*4.5*	*4.1*	*3.4*	*3.0*	*2.5*
Budgetary revenues (% of GDP)	14.9	14.4	14.4	14.4	14.4	14.4	14.5
Program spending (% of GDP)	13.6	14.4	14.5	14.3	14.1	13.9	13.8
Public debt charges (% of GDP)	1.3	1.2	1.2	1.2	1.2	1.3	1.4
Budgetary balance (% of GDP)	0.0	-1.1	-1.4	-1.2	-1.0	-0.9	-0.8
Federal debt (% of GDP)	31.0	31.5	31.6	31.6	31.5	31.3	30.9

[1] Debt representing the accumulated deficits including other comprehensive income.
Sources: Department of Finance of Canada and Desjardins, Economic Studies

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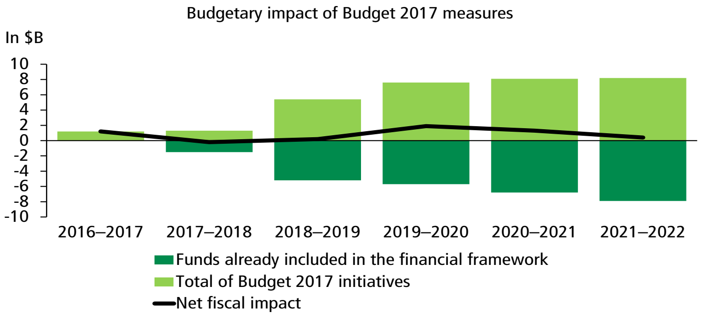
Few Changes to Budgetary Projections

Although Budget 2017 includes a wide range of new measures, it is clear that their net financial cost is quite small, all things considered. For 2017–2018, the new measures' total cost comes in at $1.3B. However, the Government of Canada plans to recover $1.5B for the fiscal year by reallocating department and agency funding. The resulting net fiscal impact for fiscal 2017–2018 is +$0.2B, leading to a slight reduction in the deficit. The net fiscal impact is -$0.2B for 2018–2019, -$1.9B for 2019–2020, -$1.3B for 2020–2021 and -$0.4B for 2021–2022. As a result, the total impact of the measures announced today on the budgetary balance is very limited (graph 1).

GRAPH 1
The net financial impact of the new measures in Budget 2017 is slight



Sources: Finance Canada and Desjardins, Economic Studies

That said, other factors will also impact the budgetary balance in the years ahead. Economic conditions seem to be improving, as shown by the relatively strong growth in real GDP in the second half of 2016. Indeed, most economic forecasters have recently raised their projections for 2017. With that being the case, the assumptions used in the Budget and based on last December's survey of private-sector forecasters seem somewhat conservative. According to Finance Canada estimates, improvements in Canada's economic and budgetary situation since last fall's economic statement should result in a $2.4B decrease in the budget deficit for 2017–2018, and a $1.9B decrease for 2018–2019. Needless to say, these amounts could be higher in the light of recent economic forecasts.

On the other hand, even though economic conditions are improving, considerable uncertainty continues to weigh on the economy. Among other developments, the resurgence of U.S. protectionism, the uncertain future of North American Free Trade Agreement (NAFTA) and the potential impact of future changes to U.S. tax rules on the competitiveness of Canadian companies are major concerns. In such situations caution is advised, and we welcome the return of the adjustment for risk, which had been eliminated in the fall update. To improve transparency, the adjustment for risk was not applied to the nominal GDP (reducing government revenue) as in the last few budgets, but directly to the budgetary balance instead. However, the leeway of $3B per fiscal year, included in the budget as of 2017–2018, is only half the amount found in last year's budget. However, the degree of uncertainty is not the same due to the recent improvement in economic conditions and the stabilization of the energy sector.

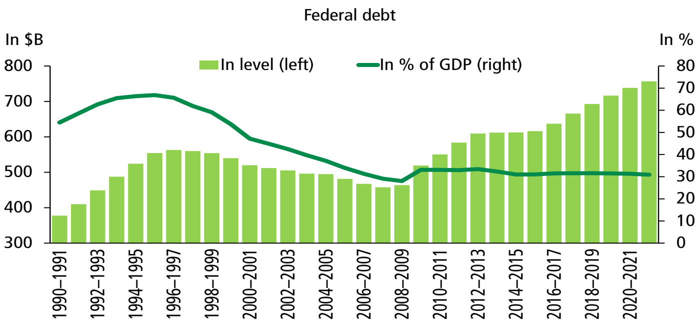
Ultimately, the outlook for the budgetary balance presented in Budget 2017 for the coming fiscal years is very similar to the one provided last year. Nevertheless, the numbers show a slightly smaller deficit for 2016–2017 due to stronger economic growth and delays in implementing the infrastructure investment plan. On the other hand, the deficits forecast for subsequent years are slightly higher. Debt growth is in line with last year's projections, and the debt-to-GDP ratio should remain slightly above 30% until March 31, 2022 (graph 2 on page 3).

TABLE 2
Economic and financial forecasts

	2016			2017f			2018f		
AVERAGE ANNUAL GROWTH IN % (EXCEPT IF INDICATED)	2016 Budget	2017 Budget	Desj. Group	2016 Budget	2017 Budget	Desj. Group	2016 Budget	2017 Budget	Desj. Group
Real GDP	1.4	1.3	1.4	2.2	1.9	2.2	2.2	2.0	2.0
GDP deflator	0.9	0.6	0.6	2.4	2.1	2.1	2.1	2.0	1.8
Nominal GDP	2.3	2.0	2.0	4.6	4.1	4.4	4.3	4.0	3.8
Treasury bills—3-month	0.5	0.5	0.5	0.7	0.6	0.6	1.6	0.9	0.8
Federal bonds—10-year	1.6	1.3	1.3	2.3	1.8	2.0	3.0	2.3	2.3
Unemployment rate	7.1	7.0	7.0	6.9	6.9	6.7	6.5	6.7	6.5
Exchange rate (US¢/C$)	72.10	75.50	75.50	75.90	74.50	74.00	79.10	76.10	72.00
Real GDP—United States	2.3	1.6	1.6	2.4	2.3	2.2	2.4	2.3	2.4

f: forecasts
NOTE: Data may not add to totals due to rounding.
Sources: Department of Finance of Canada, Statistics Canada and Desjardins, Economic Studies

GRAPH 2
The debt's relative size will remain relatively stable



Sources: Finance Canada and Desjardins, Economic Studies

Measures Focused on Innovation, Skills, Partnerships and Fairness

Budget 2017 introduces a plethora of new measures with a very small budgetary impact and effects often focused on the long term. As a result, it is hard to provide a complete list of the initiatives introduced today. Nonetheless, here is a summary of the measures that caught our eye:

- To better support family caregivers, Budget 2017 proposes to allocate $691.3M over 5 years, starting in 2017–2018, and $168.1M a year after that, to create a new employment insurance benefit lasting up to 15 weeks for family caregivers.
- Budget 2017 proposes to invest up to $950M over 5 years, starting in 2017–2018, to support a small number of business-led innovation superclusters, which have the greatest potential to accelerate economic growth. Funds will be provided on a competitive basis. The competition will launch in 2017 and target superclusters that enhance Canada's global competitiveness by focusing on highly innovative industries such as advanced manufacturing, agri-food, clean technology, health/bio-sciences, clean resources, and infrastructure and transportation.
- To help children and better support Canadian families, the 2016 budget called for an initial amount of $500M in 2017–2018 for early learning and child care. Building on this commitment, Budget 2017 proposes to invest an additional $7B over 10 years, starting in 2018–2019, to support and create more high-quality, affordable child care spaces across the country.
- The federal government intends to create a new National Housing Fund to address critical housing issues and better support vulnerable citizens, including seniors, Indigenous Peoples, survivors fleeing situations of domestic violence, persons with disabilities, those dealing with mental health and addiction issues, and veterans. Administered by the CMHC, the Fund will receive $5B in funding over the next 11 years.
- Budget 2017 proposes to invest an additional $4B over 10 years, starting in 2018–2019, to build and improve housing, water treatment systems, health facilities and other infrastructure in indigenous communities.
- The Department of Finance is announcing a $6B investment over 10 years for home care and $5B over 10 years to support mental health initiatives.
- The government is proposing an additional $523.9M over 5 years to prevent tax evasion and improve tax compliance. The investment will be used to fund new initiatives and extend existing programs to ensure the tax system is fair and equitable for all Canadians.
- The government will introduce legislation to establish the Parliamentary Budget Officer as an independent Officer of Parliament, with a renewed mandate to focus on costing and financial analysis of the federal government, and bring to an end the secrecy surrounding the Board of Internal Economy.
- Given the decreasing popularity of Canada Savings Bonds among Canadians, and following a review of the Program, the Government of Canada will discontinue the sales of new Canada Savings Bonds in 2017. All outstanding retail debt will continue to be honoured.

A Transitional Budget Pending President Trump's Decisions

Expectations were not very high for Budget 2017, and it is clearly not likely to make history. Numerous initiatives were announced, with a particular focus on the middle class, but, all in all, the financial impact of the measures is limited. Moreover, the government put a great deal of emphasis on the long term in this budget, as most of the new measures will not have a real impact for several years.

The budget tabled last year was a weighty one, introducing measures to reduce the tax burden on some categories of households and an ambitious infrastructure plan that was even expanded with last fall's update. Under these conditions, the government did not have much room to announce new initiatives with Budget 2017.

In addition, the federal government is clearly retaining some leeway for upcoming budgets so that it can, if necessary, adjust to any measures that the new U.S. administration could put forward in the area of trade relations between Canada and the United States and business taxation, for example.

All the same, we would have liked the budget to provide more detail on the progress of the infrastructure investment plan. It took longer than expected to implement the program and, so far, it has not had the anticipated impact on economic growth. An update on the issue would have been very useful and provided for a better analysis of the program's effectiveness.