

# Federal Budget 2010

**Summary:** The direction of this federal budget is to eliminate deficits by 2015. The plan includes continuing with previously planned fiscal stimulus spending. The projected deficit is to be eliminated by a mix of economic growth, spending restraint and spending cuts while not raising tax rates or cutting major transfers to persons or to provinces for health/social services or equalization. For various reasons outlined in this report, projected revenues seem high and expenditures seem low. While laudable, the budget plan is unlikely to result in eliminating the deficit by fiscal 2014/15.

**Fiscal Plan:** The federal government budget deficit is projected at \$53.8 billion in the current fiscal year, declining to \$49.2 billion in fiscal 2010/11, \$27.6 billion in 2011/12, and to a negligible deficit by fiscal 2014/15. Projected gains in the ratio of revenue to GDP reflect the forecasted economic recovery. Projected declines in the ratio of program spending to GDP reflect the savings measures proposed in this budget. The total federal debt rises each year in the fiscal plan and reaches \$622.1 billion in 2014/15. As a percentage of GDP, the total federal debt rises to 35.4% in 2010/11 before declining to 31.9% by 2014/15.

**Summary Statement of Transactions (\$ Billions)**

	Actual	Projection					
	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
<b>Budgetary Revenues</b>	233.1	213.9	231.3	249.0	266.5	282.7	296.5
Program Expenses	207.9	237.8	249.2	241.4	245.2	251.4	257.7
Public Debt Charges	31.0	29.9	31.3	35.3	38.9	39.8	40.6
<b>Total Expenses</b>	238.8	267.7	280.5	276.7	284.0	291.2	298.3
<b>Budgetary Balance</b>	-5.8	-53.8	-49.2	-27.6	-17.5	-8.5	-1.8
Federal Debt	463.7	517.5	566.7	594.3	611.9	620.3	622.1
<b>Per Cent of GDP</b>							
Budgetary Revenues	14.6	14.0	14.4	14.8	15.0	15.2	15.2
Program Expenses	13.0	15.6	15.6	14.3	13.8	13.5	13.2
Public Debt Charges	1.9	2.0	2.0	2.1	2.2	2.1	2.1
Budgetary Balance	-0.4	-3.5	-3.1	-1.6	-1.0	-0.5	-0.1
Federal Debt	29.0	33.9	35.4	35.2	34.4	33.3	31.9

Source: Budget 2010.



**Economic Forecast:** Budget 2010 incorporates moderate economic growth projections through to 2014 with nominal GDP growing 4.5% to 5.0% per year. The unemployment rate declines slowly to 7.0% in 2014. No recession is foreseen, which is consistent with the consensus view and in any case is difficult to accurately predict and the main reason for forecast allowances and contingencies.

Average Private Sector Forecast						
	2009	2010	2011	2012	2013	2014
Real GDP % change	-2.5	2.6	3.2	3.0	2.8	2.6
Nominal GDP % change	-4.6	4.9	5.4	5.3	4.9	4.7
Unemployment Rate %	8.3	8.5	7.9	7.4	6.9	6.6
3-Month T-Bill Rate %	0.3	0.7	2.4	3.8	4.3	4.4
10-Year T-Bond Rate %	3.3	3.7	4.3	4.9	5.2	5.3
Consumer Price Index % change	0.3	1.7	2.2	2.1	2.1	2.1
U.S. Real GDP % change	-2.5	2.7	3.0	3.4	3.1	2.9

*Source: Budget 2010.*

**Analysis:** Generally, the Department of Finance's (DoF) macroeconomic forecasts are in line with the latest Consensus Forecast (CF) from a large group of widely published economic forecasters. The only notable difference through 2011 is a more conservative forecast by the DoF of 2.7% for growth in real US GDP in 2010 (versus 3.1% CF). In this case, Central 1 Credit Union's (C1CU) forecast agrees with the DoF.

Central 1's macroeconomic forecasts through 2013 are somewhat more conservative than the DoF's. C1CU's forecast for real GDP growth in Canada is lower by 30 basis points (BP) in 2010 and 40 BP in 2011. According to the DoF's own sensitivity estimates, C1CU's forecast will result in the deficit being 2% to 3% higher than projected due to lower revenues and higher expenses. The DoF is also forecasting the unemployment rate will drop an average of 30 BP per year faster than C1CU's forecast.

On the term structure of risk-free interest rates, the DoF forecasts short-term rates will rise more quickly and long term rates will rise less quickly than C1CU's forecast. According to the DoF's sensitivity estimates, C1CU's forecast will result in the deficit being approximately \$500 million higher than projected.

**Revenue:** Projected total revenue declines 8% in fiscal 2009/10 due to the weaker economy and implementation of previously planned income tax relief measures. Thereafter, projected revenue increases 8% through fiscal 2011/12 and an average of 6% per year through 2014/15. These revenue gains result from resumed growth in the economy which increases personal and corporate income taxes, GST revenue, E.I. revenue and other agency or fee revenue. Partly offsetting these sources of revenue growth are implementation of previously planned corporate tax relief and corporate losses carried forward from the recession.

Revenue by Source (\$ Billions)							
	Actual	Projection					
	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Income Taxes	151.8	135.4	148.0	159.4	169.3	180.3	190.8
Excise Taxes/Duties	39.8	39.3	41.0	42.7	44.4	46.3	48.3
E.I. Premiums	16.9	16.6	17.6	20.0	22.6	25.2	26.6
Other	24.6	22.6	24.8	27.0	30.3	30.8	30.8
Total Revenue	233.1	213.9	231.3	249.0	266.5	282.7	296.5

*Source: Budget 2010.*

**Analysis:** Revenues will likely come in somewhat lower than projected through fiscal 2012/13 based on CICU's forecasts. Personal and corporate income tax, sales tax, E.I. premiums and agency/fee revenues will be the main sources of realized revenue growth. As a percentage of GDP, revenues will rise steadily from fiscal 2010/11 through 2014/15.

**Spending:** Total government spending increased 12% during the recession in fiscal 2009/10 and is projected to increase 5% in the coming fiscal year. Spending is projected to edge down 1% in fiscal 2011/12, followed by annual increases of 3% through fiscal 2013/14 and 2% in 2014/15. Through fiscal 2014/15, total spending increases \$59.5 billion (24.9%). Most of the increase (\$41.7 billion) results from previously planned fiscal stimulus spending in 2009/10 through 2010/11.

Growth in spending through fiscal 2014/15 is led by elderly benefits (\$11.8 billion, OAS, GIS, etc.), transfers to provinces for health/social services (\$11.4 billion), government operating expenses subject to budget freezes (\$9.9 billion, departments), public debt charges (\$9.6 billion) and other direct operating expenses (\$5.2 billion, employee pensions/benefits, non-wage defense spending, etc.).

To restrain growth in government spending so as to almost eliminate the string of annual deficits by 2014/15, the budget outlines several policies, projected to save a total of \$17.6 billion through fiscal 2014/15. The most material policy is to end temporary fiscal stimulus spending as scheduled, largely during fiscal 2010/11. The other measures and their projected savings in the cumulative deficit are:

- Slow previously planned growth in defense spending beginning in fiscal 2012/13 (saves \$2.5 billion).
- Freeze international assistance at fiscal 2010/11 levels (saves \$4.5 billion).
- Slow previously planned growth in operating expenses, notably by freezing departments' salary and operating budgets at fiscal 2010/11 levels through 2012/13 (saves \$6.8 billion).
- Augment review of operations process for reducing costs while improving efficiency (saves \$1.3 billion).
- Close tax loopholes (saves \$2.5 billion).

#### Expense by Function (\$ Billions)

	Actual	Projection					
	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Elderly Benefits	33.4	35.0	36.7	38.6	40.7	42.9	45.2
E.I. Benefits	16.3	22.4	22.6	19.6	18.8	18.4	18.4
Children's Benefits	11.9	12.3	12.7	13.2	13.4	13.4	13.5
Health/Social Transfers	33.3	35.7	37.1	38.7	40.7	42.7	44.7
Equalization Etc.	15.2	16.1	16.4	16.8	17.7	18.6	19.5
Other Govn't. Transfers	-2.0	-0.4	3.4	0.8	-1.3	-1.5	-1.7
Other Transfers	30.2	39.8	39.4	33.7	33.6	32.8	32.1
Amortization	4.1	4.4	4.6	4.9	5.1	5.3	5.4
Other Operating Expenses	20.6	20.8	21.5	22.9	24.2	25.2	25.8
Operating Exp. s.t. Freeze	44.9	51.8	54.9	52.2	52.4	53.5	54.8
Public debt Charges	31.0	29.9	31.3	35.3	38.9	39.8	40.6
<b>Total Spending</b>	<b>238.8</b>	<b>267.7</b>	<b>280.5</b>	<b>276.7</b>	<b>284.0</b>	<b>291.2</b>	<b>298.3</b>

Source: Budget 2010

**Analysis:** For a variety of reasons, spending will likely come in somewhat higher than projected throughout the budget horizon. Based on C1CU's forecast, projected employment insurance benefits depend on a fairly optimistic forecast for declines in the unemployment rate. Phasing out stimulus spending on infrastructure projects is unlikely to be as clean cut as projected, given the long established history of cost overruns on construction projects.

While laudable, the policies to slow the growth of spending are unlikely to result in all the projected cost savings. Savings from foregone spending on defense and international assistance seem to depend on a fairly benign international environment from 2011 through 2014. Projected savings from freezing departmental salary and operating budgets depends on whether future governments will stay on this path which is far from certain in an era of minority governments.

### **Budget Measures, Credit Unions and Financial Services**

For coverage of budget measures and announcements of special interest to credit unions, follow this link to Credit Union Central of Canada's report:

<http://www.cucentral.com/Default.aspx?DN=52e4827d-4f10-4f56-a122-94a432f30af7>