

I. PRICE EFFECTS OF THE GST

A. Minimum Estimate

- (1) The Government estimates that introduction of the GST would result in a one-time increase in the Consumer Price Index (CPI) of about 1.25%. While several economic "think-tanks" concur with this estimate, it has been criticized on at least two grounds. First, the Government's 1.25% estimate assumes that the savings from removing the current Federal Sales Tax would be fully passed along to consumers. Many groups believe that this assumption is unrealistic and fails to take into account a number of special circumstances including inadequate inventory rebates and regulated or uncompetitive markets.
- (2) Second, the Government assumes that organized labour is either naive or is powerless to address a reduction in the purchasing power of its wages. According to the information received by this Committee, members of organized labour are well aware that the GST would reduce their real income and are extremely skeptical about the Government's price estimate. This is already being reflected in new labour contracts that contain GST protection in the form of cost of living allowance clauses and fixed wage increases. To the extent that labour is successful in obtaining further wage hikes because of the GST, this will feed into firms' cost structures and result in higher prices. In the real world, expectations are crucial but there is no indication that the Government has built a wage response into its price impact estimates.