Federal Deficit Reductions to Continue

Canada will reduce its budget deficit to one per cent of Gross Domestic Product (GDP) or C$9 billion by 1998-99, Finance Minister Paul Martin announced on October 9. This represents an 80 per cent reduction in the shortfall since 1993-94, when it reached $42 billion or almost 6 per cent of GDP.

In an economic and fiscal update presented to the House of Commons Standing Committee on Finance, Mr. Martin reported that the government had bettered its deficit target in 1995-96 for the second year in a row and was on track to meet its targets for the next two years.

The target figure for 1998-99 marks a major milestone in the government's efforts to eliminate the deficit and bring down the debt: that year Canada will no longer need to borrow new money from financial markets. Borrowing requirements are the measure the U.S. and many other countries use to assess fiscal health. (The difference between the deficit and borrowing requirements is due to non-budgetary transactions that provide funds to the government, such as surpluses in the government employees' pension fund, loans and accounts payable.) By 1997-98 Canada's federal government will have the lowest ratio of borrowing requirements to GDP among the G-7 countries.

A deficit of one per cent will ensure that the debt-to-GDP ratio continues on a downward path, Mr. Martin said, so that the growth of the economy exceeds the growth of debt, reversing almost 20 years of uninterrupted increases in the ratio.

Deficit reduction has been achieved almost entirely through spending cuts. Program spending is projected to fall to 12 per cent of GDP in 1998-99, its lowest level in almost 50 years.

The provinces and territories have also greatly reduced their deficits: seven out of 12 balanced their budgets or had surpluses last year.

Controlling federal and provincial government finances has paid off in significantly lower interest rates, which will make debt reduction easier, the Finance Minister said. On October 28, the Bank of Canada reduced the rate at which it lends money to commercial banks a quarter point to 3.5 per cent. Commercial lenders followed suit, cutting the prime rate to 5 per cent, its lowest level since 1956. Since May 1995, the bank rate has dropped 4.75 percentage points to fall 1.75 points below the comparable U.S. rate.

Mr. Martin reviewed Canada's other economic fundamentals, finding evidence for a "dramatic turnaround in Canada's economic condition."

❒ Inflation remains firmly under control: consumer prices rose only .1 per cent between August and September, for an annual inflation rate of 1.5 per cent. The annual rate in September a year ago was 2.3 per cent.

❒ Foreign indebtedness has fallen: in the second quarter Canada ran its first current account surplus in 12 years.

❒ Real GDP was up by 0.5 per cent in July over the previous month, largely due to a surge in manufacturing production, for an annualized growth rate of 1.9 per cent. In the first two quarters of 1996, the economy grew at annual rates of only 1.3 per cent. The International Monetary Fund predicted in its World Economic Outlook published in September that Canada would lead the G-7 in economic growth next year.

The one area of the economy that satisfies no one, the Finance Minister said, is the high unemployment rate, which rose to 9.9 per cent in September from 9.4 per cent in August. Employment fell by 47,000 jobs, all in the service sector. The net increase in jobs since January is 106,000. Mr. Martin attributed the persistently high unemployment rate in large part to job losses in the public sector, which represents about 15 per cent of total employment. However, he said, the economy is going through a period of transition. "Ultimately, public job losses will come to an end and it is the private sector job creation figures that will count."

Mr. Martin said the government would continue to focus on deficit reduction and economic growth. He specifically rejected two options that would alter the government's course: introducing a broad-based tax cut, which could cause the deficit to rise again, or accelerating the pace of spending cuts, which could bring unacceptable hardship for many Canadians.

All figures are in Canadian dollars. On October 28, the noon exchange rate was US$1 = C$1.3448.

Update on Canada-U.S. Trade

Canada and the U.S. traded $33.7 billion worth of goods in August, bringing the total merchandise exchange for the year to $259.9 billion, an increase of 5.7 per cent over the first eight months of 1995.

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