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OpEd

Opportunity missed to lower growth; Funds to provinces

March 5, 2010, Kelowna.com – Finn Poschmann

Cautious, empty, risk averse, politically timid — or politically shrewd— Finance Minister Jim Flaherty's fourth federal budget is as mainstream as they come.

That is not entirely a criticism. Budget 2009 and subsequent updates committed Ottawa to "stimulus" spending through 2011, and although the economic downturn is now past, failure to deliver would not have fared well in a minority Parliament. So spending growth continues.

Certainly much of the addition to spending will prove unnecessary, and so, too, will the new spending on politically correct initiatives, such as so-called green jobs programs.

And Mr. Flaherty missed an opportunity to signal lower growth, in future, of otherwise unsustainable transfers to the provinces for health and social programs, with an eye to preparing provinces to one day take more responsibility for financing the programs they deliver. Neglecting to do so will one day prove expensive, but for the moment the Minister has produced a budget that will attract only limited fire in Parliament.

Nor does Budget 2010 take even a gentle slice out of federal Crown corporations' bloated mandates or balance sheets, leaving Export Development and Canada Mortgage and Housing, for instance, occupying huge shares of the financial marketplace.

Looking beyond these unfortunate nods to political reality, however, this is a good budget.

The message on spending is key. Given a prior commitment to tax relief — personal tax relief, a lower GST, and a long-run corporation income tax rate relief plan, plus a commitment to returning to budget balance, something has to give, and that something is spending.

Until recently, the Finance Minister and the Prime Minister were talking about "growing" out of deficits, meaning to depend on economic growth to float the budget into surplus. This talk was never very plausible, and denied the existence of a self-evident structural deficit. The budget reverses course on this front and implements spending controls that will restore the budget to rough balance by 2014-15.

Spending will be limited in part by freezing departmental operating budgets at 2010-11 levels. In the meantime, public sector wage increases will have to be funded within existing operating budgets. These are not huge steps, they lock in spending at an horrifically high level, but they are an important signal — a signal that easily can be strengthened in future years, for instance by requiring public sector employees to fund a fairer share of their pension costs.

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The defence budget will grow, but by much less than previously planned. This will hurt — few would argue that Canada is over-defended — but the coming scaling down of spending in Afghanistan will relieve stress on the armed forces.

More controversial will be a pullback relative to planned international assistance after 2010-11. However, prior plans had such spending growing at an untenable 8% rate and, in a field where spending effectiveness is so often in doubt, more modest plans are defensible.

Better control over spending means useful tax measures remain possible, and currently planned rate relief remains on course. Federal and provincial corporate income tax reductions, coupled with sales tax reform in British Columbia and Ontario, will put Canada's effective tax rate on new business investment at such a low rate that Canada can contemplate becoming a low-tax jurisdiction — a magnet for investment, jobs and growth.

Budget 2010 implements some helpful improvements on the tax front, and holds out the possibility for more. First among the improvements is the elimination of tariffs on intermediate manufacturing inputs, machinery and equipment — a significant boost to the potential productivity and competitiveness of the manufacturing and processing sectors. Almost as importantly, Canadian leadership in tariff liberalization can be a significant force in shaking loose multilateral reforms, promising broader growth widely shared.

At home, an easing of trivial tax reporting requirements will make Canadian venture firms more attractive investments for foreign private equity funds — a possible boost to the sector's innovative capacity.

Even better, the budget raises the possibility of implementing a loss-transfer system or consolidated reporting for corporate groups — a step that would significantly ease compliance and even improve the international investment environment, with little impact on future revenue.

Clearly this budget is timid — or shrewd, depending on whether one scores it against the full range of economically sensible possibilities or sees the world through the lens of Parliament.

But if we take the constraints of a minority Parliament as binding, success in reining in spending could be viewed as big win, even if the spending remains uncomfortably high. Balancing a budget sooner, rather than later, is certainly to be cheered. And delivering on planned tax relief is crucial to Canada's growth prospects, and to the federal government's ability to fund future demands on it.

From a slightly blinkered political viewpoint, therefore, Canadians may have to consider it good enough for government work.

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