BUDGET ANALYSIS

Canada: Economic and Fiscal Update 2021

More Favourable Economic Conditions Have Improved the Federal Government's Financial Situation

HIGHLIGHTS

- Improved economic conditions mean that budget deficits will be lower than expected. A total of $59.8B has been shaved off the deficits expected between now and 2025–2026.
- The budgetary balance for the 2020–2021 fiscal year will drop from -$354.2B to -$327.7B.
- The federal government's debt should rise to $1,358.9B by March 31, 2027, compared to $721.4B on March 31, 2020. The debt-to-GDP ratio could peak at 48% on March 31, 2022, and then edge back down to 44% by March 31, 2027.
- The new measures introduced in the update are relatively modest. We will have to wait for the next budget to find out what the federal government's truly new policies will bring, reflecting the measures promised in the last election campaign.

TABLE 1
Summary of transactions

	ACTUAL	PROJECTIONS					
IN $B (EXCEPT IF INDICATED)	2020–2021	2021–2022	2022–2023	2023–2024	2024–2025	2025–2026	2026–2027
Budgetary revenues	316.5	370.5	391.7	413.9	435.7	458.9	481.0
Variation (%)	*-5.3*	*17.1*	*5.7*	*5.7*	*5.3*	*5.3*	*4.8*
Program spending	-608.5	-480.2	-416.3	-420.4	-427.0	-442.5	-455.2
Variation (%)	*79.8*	*-21.1*	*-13.3*	*1.0*	*1.6*	*3.6*	*2.9*
Debt charges	-20.4	-24.5	-26.0	-31.4	-35.6	-38.6	-40.9
Variation (%)	*-16.7*	*20.3*	*6.1*	*20.8*	*13.4*	*8.4*	*6.0*
Net actuarial losses	-15.3	-10.3	-7.9	-5.9	-2.3	-0.5	2.0
Budgetary balance	-327.7	-144.5	-58.4	-43.9	-29.1	-22.7	-13.1
Federal debt[1]	1,048.7	1,191.6	1,250.0	1,293.9	1,323.0	1,345.7	1,358.9
Variation (%)	*45.4*	*13.6*	*4.9*	*3.5*	*2.2*	*1.7*	*1.0*
Budgetary revenues (% of GDP)	14.3	14.9	14.8	15.0	15.2	15.4	15.6
Program spending (% of GDP)	27.6	19.3	15.7	15.2	14.9	14.9	14.8
Public debt charges (% of GDP)	0.9	1.0	1.0	1.1	1.2	1.3	1.3
Budgetary balance (% of GDP)	-14.8	-5.8	-2.2	-1.6	-1.0	-0.8	-0.4
Federal debt (% of GDP)	47.5	48.0	47.3	46.9	46.2	45.3	44.0

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

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NOTE TO READERS: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively.

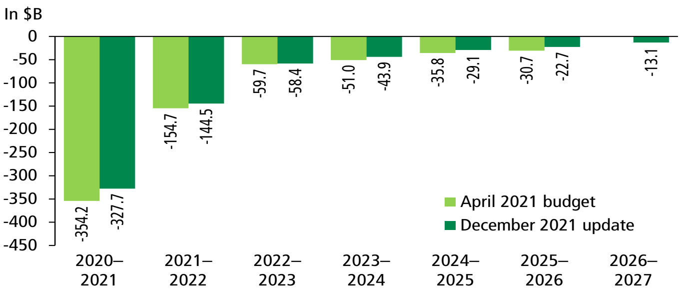
Despite some hiccups, the Canadian economy has continued to recover since April's budget. Real GDP should be back to pre-pandemic levels at the first quarter of 2022. The number of jobs has been higher than before the pandemic since last September, and the unemployment rate has fallen almost to the February 2020 level. In addition, prices have risen faster than expected, leading to more sustained growth of nominal GDP. The update predicts a 12.5% increase in nominal GDP for 2021 (similar to our forecast), which is substantially higher than the 9.3% increase set out in last spring's budget.

All this has positive consequences for the Canadian government's financial situation. As expected, the projections in the update include a significant reduction in budget deficits between now and 2025–2026. Furthermore, the budgetary balance for the 2020–2021 fiscal year will drop from -$354.2B to -$327.7B (graph 1). A total of $59.8B will be shaved off the expected deficit by 2025–2026. The federal government's debt should therefore grow more slowly in the next few years than was initially expected. It should nevertheless reach $1,358.9B by March 31, 2027, compared to $721.4B on March 31, 2020 (graph 2). The debt-to-GDP ratio compared to GDP could peak at 48.0% by March 31, 2022, and then edge back down toward 44.0% by March 31, 2027. That ratio had fallen to 30.7% on March 31, 2019.

The new measures introduced in the update are relatively modest. Here are the highlights:

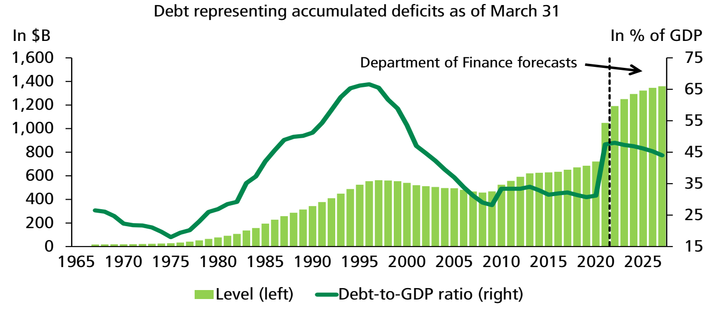
- $1.7B to increase access to rapid test kits across Canada.
- $2B to procure COVID-19 therapeutics and treatments.
- Enhancement of the Eligible Educator School Supply Tax Credit to allow teachers to claim a refundable tax credit worth 25% (up from 15%) of up to $1,000.
- $70M to support ventilation in public and community buildings such as hospitals, libraries and community centres.

GRAPH 1
The budgetary balance is improving



Source: Department of Finance Canada

GRAPH 2
The relative size of the debt should start shrinking in the 2022–2023 fiscal year



Sources: Department of Finance Canada and Desjardins, Economic Studies

TABLE 2
Economic and financial forecasts

AVERAGE ANNUAL GROWTH IN % (EXCEPT IF INDICATED)	2020		2021f		2022f	
	2021 Update	Desj. Group	2021 Update	Desj. Group	2021 Update	Desj. Group
Real GDP	-5.2	-5.2	4.6	4.5	4.2	3.9
GDP deflator	0.7	0.7	7.6	7.6	2.2	2.1
Nominal GDP	-4.5	-4.5	12.5	12.4	6.6	6.1
Treasury bills—3-month	0.4	0.4	0.1	0.1	0.5	0.6
Federal bonds—10-year	0.8	0.8	1.4	1.4	1.9	2.2
Unemployment rate	9.5	9.5	7.6	7.5	6.1	5.7
Exchange rate (US¢/C$)	74.6	74.6	80.0	79.5	80.6	80.6
Real GDP—United States	-3.4	-3.4	5.6	5.5	3.9	3.5

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

- A new Small Businesses Air Quality Improvement Tax Credit of 25% of the cost of upgrading ventilation and air filtration systems (up to a maximum of $10,000 per location and $50,000 in total).
- $60M to support workers in Canada's live performance industry through the new, temporary Canada Performing Arts Workers Resilience Fund.
- $50M to ease pressure on Canadian supply chains by launching a new, targeted call for proposals under the National Trade Corridors Fund to assist Canadian ports with the acquisition of cargo storage capacity and other measures to relieve supply chain congestion.
- $85M to reduce immigration backlogs in Canada, reunite families and welcome people who can fill some of the gaps in Canada's labour supply.

When the pandemic hit, the Canadian government introduced a whole range of measures to support Canadian individuals and businesses. Coupled with the negative effects of COVID-19 on economic growth, those initiatives seriously eroded the federal government's financial position. But even though uncertainty is still high, with the spread of the Omicron variant and the mushrooming supply problems sparked by the floods in British Columbia, economic conditions are starting to get back to normal across the country. The health emergency that overshadowed the last budget is now giving way to more favourable outlooks, due in large measure to a successful vaccination campaign. This means that the federal government will be able to start focusing on the post-pandemic future. The relative modesty of the new initiatives announced in the update is understandable, as we are in a transition period. There is still naturally a great deal of uncertainty surrounding the pandemic, and caution is required, so we will have to wait for the next budget to find out what the federal government's truly new policies will bring, reflecting the measures promised in the last election campaign.