



# TD Economics

## Special Report

October 16, 2008

### CANADA'S FEDERAL GOVERNMENT FACING SIGNIFICANT DEFICITS

We have received many requests in recent days to estimate the status quo budget balances of the federal government. Our estimates are shown in the table below. These estimates are based upon our September 25, 2008 Quarterly Economic Forecast with a few adjustments. That forecast featured a 0.7 per cent growth rate for Canada's real GDP in 2008, 1.2 per cent for 2009 and 2.7 per cent in 2010. Even though that forecast was prepared only a few weeks ago, we feel it appropriate to downgrade the growth rate somewhat for the end of this year and the beginning of 2009 to account for the very weak recent data coming out of the United States. While some of the latest Canadian indicators have been positive, such as September's astonishing employment surge, it is only a matter of time, and not much time, before the worsening situation

in the U.S. economy spills over to Canada. This adjustment weakens federal government revenue growth in our estimates. But the 50 basis point rate cut by the Bank of Canada since our forecast and our assumption that another 50 basis points will be shaved off at the next Bank meeting offsets somewhat the impact on the budget balance by lowering public debt charges.

A few assumptions and features of the projection should be noted:

- This is a status quo projection in that tax rates are left unchanged and spending programs (the growth rates) are left in tact relative to the 2008 Budget plans. The new Government could of course alter these parameters.

FEDERAL GOVERNMENT FISCAL POSITION							
<i>(Billions of dollars, unless otherwise indicated)</i>							
Fiscal Year	Actual		Projection				
	06-07	07-08	08-09	09-10	10-11	11-12	12-13
<b>Budgetary revenues</b>	<b>236.0</b>	<b>242.4</b>	<b>238.6</b>	<b>236.7</b>	<b>246.2</b>	<b>258.5</b>	<b>269.6</b>
% change	6.2	2.7	-1.6	-0.8	4.0	5.0	4.3
% of GDP	16.3	15.8	15.2	14.6	14.7	14.9	15.0
Program spending	188.3	199.5	207.8	217.2	225.9	232.7	239.7
% change	7.5	5.9	4.2	4.5	4.0	3.0	3.0
% of GDP	13.0	13.0	13.2	13.4	13.5	13.4	13.4
Public debt charges	33.9	33.3	30.8	29.9	30.2	31.3	32.3
% change	0.3	-1.8	-7.7	-2.8	1.0	3.6	3.2
% of GDP	2.3	2.2	1.9	1.8	1.8	1.8	1.8
<b>Total expenditures</b>	<b>222.2</b>	<b>232.8</b>	<b>238.6</b>	<b>247.1</b>	<b>256.1</b>	<b>264.0</b>	<b>272.0</b>
% change	6.3	4.8	2.5	3.6	2.8	3.1	3.0
% of GDP	15.4	15.2	15.1	15.3	15.0	14.9	14.7
<b>Budget balance for Planning</b>	<b>13.8</b>	<b>9.6</b>	<b>0.0</b>	<b>-10.4</b>	<b>-9.9</b>	<b>-5.5</b>	<b>-2.4</b>
<b>Federal debt:</b>							
<b>Accumulated deficits</b>	<b>467.3</b>	<b>457.6</b>	<b>457.6</b>	<b>468.0</b>	<b>477.9</b>	<b>483.4</b>	<b>485.8</b>
% of GDP	32.3	29.8	28.8	28.7	27.8	26.9	25.8

Source: Department of Finance Canada

- We estimate that the recent health of budgetary revenues will soon begin to deteriorate and there will be a significant negative adjustment to revenues for 2008-09 in the Supplementary Period when revenue data are converted from a collections to an accrual basis. As such it may be well after the March 31, 2009 end of the fiscal year before the full extent of revenue weakening in 2008-09 is apparent. In part this adjustment will reflect corporations having overpaid on their installments of corporate income taxes and individuals having much lower capital gains. Past cyclical experience shows that these sources of revenue can turn very quickly.
- We have not incorporated any amounts for contingencies or economic prudence.
- We have assumed that the proceeds of this year's \$4.25 billion spectrum auction will be spread evenly over 10 years (\$425 million per year), beginning in 2008-09.
- We have not incorporated any impact from the expansion to the Canada Mortgage Bond program recently announced. This will raise public debt charges and non-tax revenues. There will be a net impact of lowering the deficit with the magnitude determined by the rate set by reverse auctions. It is likely that the net impact on the deficit will be a reduction of a few hundred millions of dollars spread over this and next fiscal year.
- We assume that Ontario becomes eligible for equalization payments as of 2009-10 and hence the new floor for the equalization program becomes the B.C. standard. Both aspects raise equalization payments and total program spending above the pace set in the 2008 Budget.

*Don Drummond*  
*SVP & Chief Economist*  
 416-982-2556

*Derek Burleton*  
*AVP & Director of Economic Analysis*  
 416-982-2514

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