

The Fiscal Monitor

A Publication of the Department of Finance

Highlights of financial results for June 1997

Budgetary surplus of \$1.5 billion recorded in June 1997

A surplus of \$1.5 billion was recorded in June 1997, marking the second consecutive month in which a budgetary surplus was recorded – the first time that this has occurred since the late 1970s. As a result, there was a net improvement in the federal government's budgetary position of \$2.2 billion on a year-over-year basis. Budgetary revenues were up \$1.8 billion (16.3 per cent), while program spending declined \$0.1 billion (0.9 per cent). Public debt charges were down \$0.3 billion (6.6 per cent).

The increase in budgetary revenues was primarily due to higher personal income tax and goods and services tax (GST) collections, each up \$0.5 billion, and increased corporate income tax collections and employment insurance premiums, each up \$0.3 billion. The increase in personal income tax collections reflected strong growth in employment income, reflecting the advances in employment. The strong increase in GST collections was primarily attributable to timing considerations, as collections in the first two months were unusually low. The higher corporate income tax collections reflected the continued strength in corporate profits, while the higher employment insurance premiums were largely attributable to the acceleration of monthly payments.

The decline in program spending reflected the impact of previous budget actions. Lower spending was reported in major transfers to other levels of government, payments to Crown corporations and defence. The impact of these declines was partially offset by higher elderly benefit payments, increased subsidy transfers, and the costs incurred by Elections Canada related to the June 1997 federal election. The decrease in public debt charges was attributable to the effect of lower interest rates.

Deficit for April to June 1997 down \$4.8 billion

Over the first three months of the 1997-98 fiscal year, the deficit was reported at \$0.5 billion, down \$4.8 billion from the same period last year. This year-over-year decline in the deficit was largely attributable to the increasing strength in the economy and the impact of previous budget measures. Budgetary revenues were up \$3.3 billion (10.9 per cent), program spending declined \$0.9 billion (3.8 per cent), while public debt charges were \$0.6 billion lower (4.9 per cent).

Financial requirements significantly lower

Financial requirements, excluding foreign exchange transactions, amounted to \$483 million in the first three months of 1997-98, compared to a net requirement of \$6.7 billion over the same period last year. Foreign exchange transactions provided the government with a net source of funds amounting to \$1.0 billion over the April to June 1997 period, compared to a net source of \$0.4 billion over the first three months in 1996-97. As a result, there was a total financial source (surplus) of \$0.6 billion to date, compared to a net requirement of \$6.2 billion over the same period last year. There was a net repayment of unmatured debt of \$6.0 billion in the first three months of 1997-98.

Caution should be exercised in extrapolating these monthly results to gain an assessment of the possible outcome for the year as a whole. For example, all of the current increase in employment insurance premiums will be reversed by the end of the calendar year, thereby having no impact on the deficit outcome for the year as a whole.



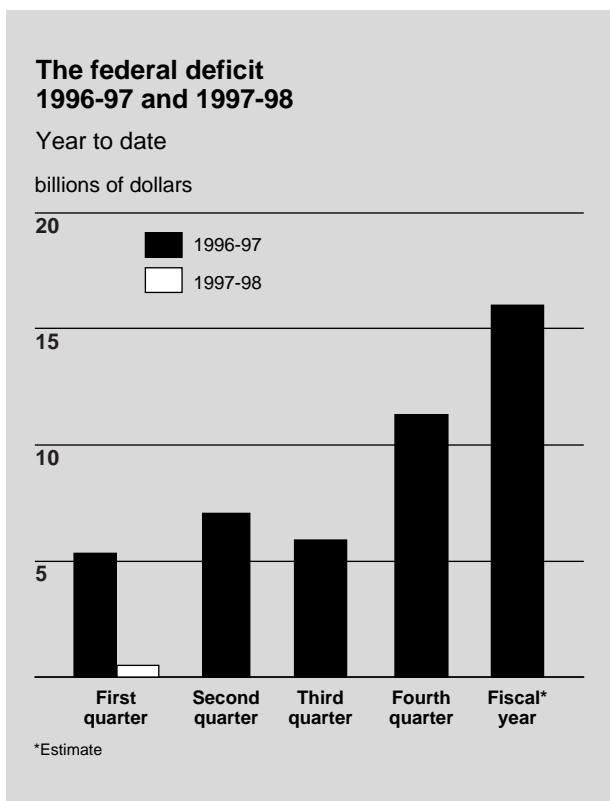
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Table 1

Summary statement of transactions

	June		April to June	
	1996	1997	1996-97	1997-98
	(millions of dollars)			
Budgetary transactions				
Revenues	11,200	13,029	30,276	33,568
Program spending	-8,009	-7,934	-24,127	-23,219
Operating surplus	3,191	5,095	6,149	10,349
Public debt charges	-3,844	-3,592	-11,444	-10,882
Deficit/surplus	-653	1,503	-5,295	-533
Non-budgetary transactions	-1,692	-2,013	-1,366	50
Financial requirements/source (excluding foreign exchange transactions)	-2,345	-510	-6,661	-483
Foreign exchange transactions	1,448	-844	446	1,048
Total financial requirements/source	-897	-1,354	-6,215	565
Unmatured debt transactions	300	2,360	41	-5,957

Note: Positive numbers indicate net source of funds. Negative numbers indicate net requirement for funds.



The increase in personal income tax collections due to higher taxes paid on filing, with respect to the 1996 taxation year, is a one-time development and will not be repeated in subsequent months. In the fall, the Minister of Finance will present the government's annual update on economic and fiscal developments. At that time, there will be an assessment of current developments on the government's deficit targets.

Budgetary revenues up

Over the April to June 1997 period, budgetary revenues were up \$3.3 billion, or 10.9 per cent, on a year-over-year basis. Of this increase \$1 billion was attributable to the timing in the receipt of employment insurance premiums, which will be reversed over the latter half of the calendar year, with the remainder attributable to strength in the economy.

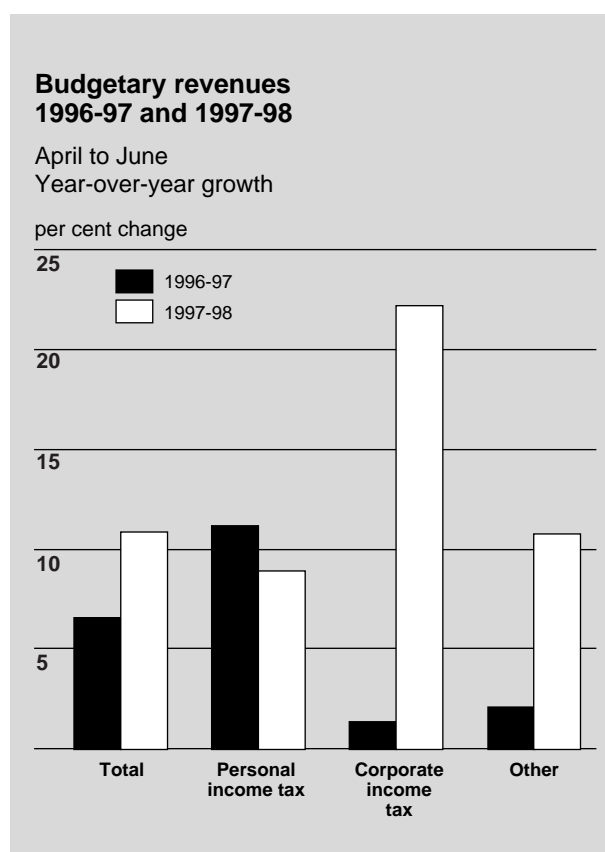
- Personal income tax collections were up \$1.4 billion, or 8.9 per cent. This increase was due to higher taxes paid on filing, relating to stronger income growth in the 1996 taxation year and to the increases in the number of people employed this year.
- Corporate income tax collections were up \$0.6 billion, or 22.2 per cent, attributable to an increase in corporate profits, in line with the strengthening economy.

Table 2

Budgetary revenues

	June		April to June		Per cent change (%)
	1996	1997	1996-97	1997-98	
	(millions of dollars)				
Income taxes					
Personal income tax	5,759	6,239	15,899	17,318	8.9
Corporate income tax	1,118	1,422	2,765	3,380	22.2
Other	137	146	513	556	8.4
Total income tax	7,014	7,827	19,177	21,254	10.8
Employment insurance premiums	1,566	1,862	4,575	5,564	21.6
Excise taxes and duties					
Goods and services tax	1,208	1,717	2,856	3,029	6.1
Customs import duties	216	118	480	333	-30.7
Other excise taxes/duties	652	786	1,718	1,864	8.5
Total excise taxes and duties	2,076	2,621	5,054	5,226	3.4
Total tax revenues	10,656	12,310	28,806	32,044	11.2
Non-tax revenues	545	719	1,470	1,524	3.7
Total budgetary revenues	11,200	13,029	30,276	33,568	10.9

- Employment insurance premiums were up \$1.0 billion, or 21.6 per cent. This increase was entirely attributable to timing considerations, which will be reversed over the latter half of the calendar year, thereby having no effect on the deficit outcome for 1997-98. In January 1997, there was a change to the base on which premiums are levied, from weekly maximum insurable earnings to annual maximum insurable earnings. This change results in an acceleration of premium payments from the latter half of the calendar year to the first half. This change does not affect the amount paid by employees and employers for the calendar year as a whole. However, those earning above the annual maximum insurable earnings will pay more of their premium liability earlier in the calendar year and less at the end.
- Net GST collections were up \$0.2 billion, or 6.1 per cent. In the first two months of the current fiscal year, net GST collections were down on a year-over-year basis, reflecting the impact of timing considerations, given remittance procedures. This was largely reversed in June 1997, with the result that the year-to-date growth is more in line with the strength in consumer demand.
- Customs import duties were down \$0.1 billion, or 30.7 per cent, in large part reflecting the impact of tariff reductions. Other excise taxes and duties were up \$0.1 billion, or 8.5 per cent, reflecting higher receipts from energy taxes and from the air transport tax.



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- Non-tax revenues, consisting of return on investments and other non-tax revenues, such as fees and proceeds from sales, among others, were up 3.7 per cent, primarily reflecting higher other non-tax revenues, as return on investments was lower due to the effect of lower interest rates.

Program spending lower

Program spending declined by \$0.9 billion in the first three months of 1997-98, compared to the same period last year. With the exception of other transfer payments, all other major components of program spending were lower in the April to June 1997 period than in the same period last year.

The profile of program spending by major component, in the first three months of 1997-98, primarily reflects the timing and the nature of the restraint measures introduced in the 1994, 1995 and 1996 budgets. Restraint measures introduced in the February 1994 budget and the impact of the Program Review I measures introduced in the February 1995 budget primarily focused on program spending excluding the major transfers to persons and other levels of government (operating and capital costs, defence, payments to Crown corporations and subsidies). As a result, this component of program spending declined by 10 per cent in 1995-96. In contrast, changes to the major transfers to other levels of government were largely delayed until 1996-97, thereby providing the provinces and territories time to plan for the restructuring in these transfers. Furthermore, the reductions in cash transfers to other levels of government are largely being phased in over two years – 1996-97 and 1997-98. As a result, whereas reductions in all other program spending accounted for most of the reduction in total program spending in 1995-96, the reductions in cash transfers to other levels of government is the major factor contributing to the decline in program spending in 1996-97 and 1997-98. However, cash transfers to other levels of government are expected to remain at \$12.5 billion post-1997-98, whereas all other program spending is expected to continue to decline as the impact of Program Review II restraint measures takes effect.

- On a year-over-year basis, major transfers to persons (elderly benefits and employment insurance benefits) declined \$0.2 billion over the April to June 1997 period, solely due to lower employment insurance benefits, as elderly benefits were up. The decline in employment insurance benefits was primarily due to lower average benefits and a decline in beneficiaries, primarily reflecting the impact of reform measures. The increase in elderly benefits was due to higher average benefits, which are indexed to inflation, and an increase in the eligible population
- In the first quarter of fiscal year 1997-98, major transfers to other levels of government were down \$0.8 billion. This decline was attributable to the

reduction in entitlements under the Canada Health and Social Transfer (CHST) and the rising value of the tax point transfers reflecting increases in the applicable tax bases. As noted above, in order to give provinces time to plan for these reductions, total entitlements – the most appropriate measure of federal support – were largely unaffected in 1995-96. Total entitlements were set at \$29.6 billion in 1995-96, up 1 per cent from 1994-95, \$26.9 billion in 1996-97 and \$25.1 billion in 1997-98. They are being held at this level until 1999-2000. For 2000-01 to 2002-03, these entitlements will grow at an increasing pace. These entitlements are paid to the provinces in the form of tax point transfers and cash. The tax point transfer component represents the value of “tax room” which the federal government made available to provinces, allowing the provinces to increase their tax rates by an equivalent amount, with no net impact on the taxpayer. The value of the tax point transfer increases in line with the growth in the applicable tax bases. The cash transfer, therefore, is the difference between the entitlement and an increasing value in the tax point transfer. Being a residual, the cash transfer, which affects program spending, is determined not only by the change in entitlements, but also by the growth in the value of the tax point transfer. As a result, even with no change in entitlements, cash transfers would decline in line with the growth in the value of tax point transfers. Conversely, if the value of the tax point transfer declined, assuming no change in

Budgetary expenditures 1996-97 and 1997-98

April to June
Year-over-year growth

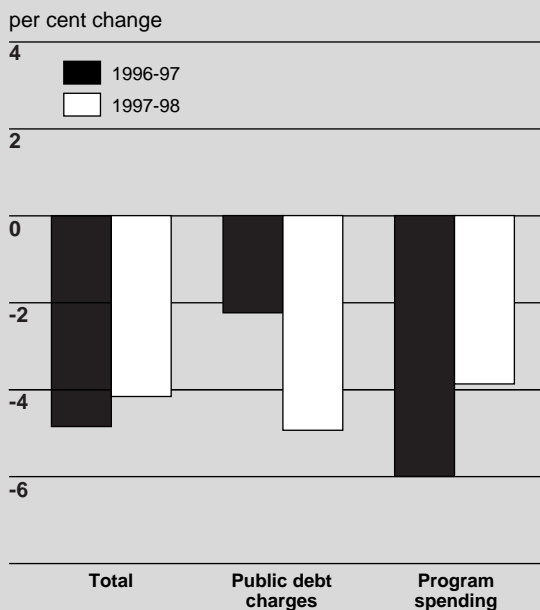


Table 3

Budgetary expenditures

	June		April to June		Per cent change
	1996	1997	1996-97	1997-98	
	(millions of dollars)				(%)
Transfer payments to:					
Persons					
Elderly benefits	1,791	1,853	5,296	5,470	3.3
Employment insurance benefits	853	846	3,265	2,914	-10.8
Total	2,644	2,699	8,561	8,384	-2.1
Other levels of government					
Canada Health and Social Transfer	1,254	1,022	3,762	3,057	-18.7
Fiscal transfers	811	787	2,506	2,452	-2.1
Alternative Payments for Standing Programs	-169	-178	-505	-533	5.5
Total	1,896	1,631	5,763	4,976	-13.7
Subsidies and other transfers					
Agriculture	15	60	66	75	13.6
Foreign Affairs	123	124	261	297	13.8
Human Resources Development	156	210	392	402	2.6
Indian and Northern Development	279	313	1,284	1,288	0.3
Industry and Regional Development	137	131	255	307	20.7
Veterans Affairs	111	114	335	342	1.8
Other	194	273	555	816	46.9
Total	1,015	1,225	3,148	3,526	12.0
Total transfers	5,556	5,555	17,472	16,886	-3.4
Payments to Crown corporations					
Canadian Broadcasting Corporation	65	66	298	249	-16.4
Canada Mortgage and Housing Corporation	177	114	451	364	-19.2
Other	103	86	303	292	-3.8
Total	345	267	1,052	905	-14.0
Operating and capital expenditures					
Defence	733	681	1,763	1,651	-6.4
All other departmental expenditures	1,375	1,431	3,840	3,777	-1.6
Total	2,108	2,112	5,603	5,428	-3.1
Total program expenditures	8,009	7,934	24,127	23,219	-3.8
Public debt charges	3,844	3,592	11,444	10,882	-4.9
Total budgetary expenditures	11,853	11,526	35,571	34,101	-4.1

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Table 4

The deficit and financial requirements/source

	June		April to June	
	1996	1997	1996-97	1997-98
	(millions of dollars)			
Deficit/surplus	-653	1,503	-5,295	-533
Loans, investments and advances				
Crown corporations	133	-31	164	-74
Other	-118	-31	-227	-61
Total	15	-62	-63	-135
Specified purpose accounts				
Canada Pension Plan Account	-139	-35	1,147	1,169
Superannuation accounts	2,476	2,651	2,105	2,067
Other	13	-138	-40	-210
Total	2,350	2,478	3,212	3,026
Other transactions	-4,057	-4,429	-4,515	-2,841
Total non-budgetary transactions	-1,692	-2,013	-1,366	50
Financial requirements/source (excluding foreign exchange transactions)	-2,345	-510	-6,661	-483
Foreign exchange transactions	1,448	-844	446	1,048
Total financial requirements/source	-897	-1,354	-6,215	565

Table 5

Financial requirements/source and unmatured debt transactions

	June		April to June	
	1996	1997	1996-97	1997-98
	(millions of dollars)			
Total financial requirements/source	-897	-1,354	-6,215	565
Unmatured debt transactions				
Payable in Canadian dollars				
Marketable bonds	3,828	6,614	7,128	9,438
Canada Savings Bonds	-245	-340	-801	-927
Treasury bills	-3,700	-5,400	-7,600	-15,000
Other	525	450	522	447
<i>Less: Government's holding</i>	144	106	423	362
Total Canadian currency	552	1,430	-328	-5,680
Unmatured debt transactions				
Payable in foreign currencies				
Marketable bonds	—	—	—	—
Notes and loans	—	—	—	—
Canada bills	-252	625	-242	-277
Canada notes	—	305	611	—
Total foreign currencies	-252	930	369	-277
Total unmatured debt transactions	300	2,360	41	-5,957
Change in cash balance	-597	1,006	-6,174	-5,392

Table 6

Cash, unmatured debt and debt balances: at June 30

	1996	1997
	(millions of dollars)	
Cash balances at end of period		
In Canadian dollars	2,358	3,969
In foreign currencies	23	5
Total cash balance	2,381	3,974
Unmatured debt balance		
Payable in Canadian dollars		
Marketable bonds	259,893	292,001
Treasury bills	158,500	120,400
Canada Savings Bonds	30,627	32,566
Other	4,000	3,915
Subtotal	453,020	448,882
<i>Less: Government's holdings of unmatured debt</i>	<i>527</i>	<i>596</i>
Total	452,493	448,286
Payable in foreign currencies		
Marketable bonds	9,501	12,460
Notes and loans	0	0
Canada bills	6,744	8,159
Canada notes	921	2,121
Total	17,166	22,740
Total unmatured debt	469,659	471,026

entitlements, the cash component would rise correspondingly. For 1997-98, cash transfers are estimated at \$12.5 billion and were expected to fall to \$11.8 billion in 1998-99. However, the government has proposed that it will ensure that over the five-year period – 1998-99 to 2002-03 – cash transfers will never fall below \$12.5 billion.

- Excluding major transfers to persons and other levels of government, all other program spending was virtually unchanged on a year-over-year basis. Declines in payments to Crown corporations, defence and all other departmental spending were offset by increases in subsidies and other transfers. The increase in the latter component primarily reflected the timing of payments, as total spending on subsidies and other transfers is expected to be lower in 1997-98 than in 1996-97 for the fiscal year as a whole, due to the restraint measures introduced in previous budgets. The year-over-year decline in the other components was attributable to the impact of restraint measures introduced in previous budgets. This was partially offset by costs incurred by Elections Canada in conducting the June 1997 federal election.

Public debt charges lower

Public debt charges were down \$0.6 billion, or 4.9 per cent, on a year-over-year basis. This decline was attributed to lower average effective interest rates on the federal government's net debt, which was only partially offset by the much slower growth in the stock of unmatured debt.

Financial requirements significantly lower

Financial requirements/source measure the difference between cash coming in to the government and cash going out. Financial requirements are usually lower than the budgetary deficit, as the former includes transactions in loans, investments and advances, federal employees' pension accounts, other specified purpose accounts, and other financial assets and liabilities. These activities are included as part of non-budgetary transactions. In addition, the budgetary deficit is largely presented on the accrual basis of accounting. The conversion from accrual to cash is also reflected in non-budgetary transactions. Non-budgetary transactions usually provide the government with a net source of funds.

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Non-budgetary transactions provided the government with a net source of funds over the April to June 1997 period, amounting to \$50 million, compared to a net requirement of \$1.4 billion in the same period last year. Most of this change was attributable to a reopening of some bonds, which resulted in a one-time cash gain but has only minor impact on the monthly deficit as such gains are amortized over the life of the bond.

With a budgetary deficit of \$533 million and a net source of funds from non-budgetary transactions of \$50 million, financial requirements, excluding foreign exchange transactions, amounted to only \$483 million in the first quarter of 1997-98, compared to a net requirement of \$6.7 billion in the same period last year.

The purpose of the Exchange Fund Account is to promote order and stability in the foreign exchange market. It fulfills this function by buying foreign exchange (selling Canadian currency) when there is upward pressure on the value of the Canadian dollar and selling foreign exchange (buying Canadian dollars) when there is downward pressure. Foreign exchange transactions resulted in a net source of \$1.0 billion in the first three months of 1997-98, compared to a source of \$0.4 billion in the same period last year.

As a result, there was a financial source, including foreign exchange transactions, of \$0.6 billion in the April to June 1997 period. In the same period last year, there was a net requirement of \$6.2 billion.

In the first three months of 1997-98, the federal government reduced its holdings of unmatured debt by \$6.0 billion, compared to the same period in 1996-97. The structure of the government's debt has also changed significantly, in order to further reduce the exposure to unexpected changes in interest rates. The share of debt held in short-term floating rate instruments, primarily Treasury bills, has been reduced, while the share held in longer-term rate instruments has increased. Cash balances as of June 30, 1997 amounted to \$4.0 billion

The Debt Servicing and Reduction Account

In June 1991, legislation to establish the Debt Servicing and Reduction Account received Royal Assent. As a result, effective April 1, 1991, all goods and services tax revenues net of the applicable input tax credits, rebates and the low-income credit, along with the net proceeds from the sale of Crown corporations and gifts to the Crown identified for debt reduction must, by law, go directly to the Debt Servicing and Reduction Account. The funds in this Account can only be used to pay the cost of servicing the public debt and ultimately to reduce the debt. The Account is audited on an annual basis by the Auditor General of Canada.

Table 7

Debt Servicing and Reduction Account (DSRA)

	1991-92	1992-93	1993-94	1994-95	1995-96
	(millions of dollars)				
Gross GST collected	29,564	30,516	32,652	36,715	38,048
<i>Less:</i>					
Refunds and rebates	11,330	12,138	14,271	17,112	18,874
Quarterly low-income tax credit	2,262	2,503	2,685	2,816	2,799
Net GST	15,168	14,868	15,696	16,787	16,374
GST penalties and interest received	19	71	90	129	135
Gains from wind-up of interest in Crown corporations/disposal of shares in Crown corporations	2	110			325
Gifts to the Crown	0.4	0.1	0.2	0.5	0.3
Proceeds to the DSRA	15,190	15,050	15,786	16,916	16,835

Figures to 1995-96 are from the *Public Accounts of Canada*.

Note: Numbers in this newsletter may not add due to rounding.

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