February 26, 1991

the Budget in Brief

Canada

PREFACE

My previous budgets have introduced a wide range of fundamental economic and fiscal reforms. This budget proposes further far-reaching initiatives.

- It deals resolutely with our fiscal challenges.
- It imposes strong disciplines on government spending.
- It requires vigorous restraint in government operations.
- It sets out a clear path toward lower inflation and lower interest rates.

It is designed to give Canadians confidence that we are facing directly our immediate economic and fiscal problems.

It establishes a clear direction as to how we must face the more fundamental problems undermining the competitive position of our economy. It is sensitive to those in greatest need.

Our policies have been challenging for Canadians and for the government. But they are essential to help our country manage the risks and seize the opportunities of a rapidly changing economic world.

In difficult times, it is easy to lose perspective as well as confidence. But it is times like this when a clear, realistic perspective is most needed to rebuild confidence and to chart a sound, sensible course of recovery.

We are a resilient, resourceful country. A stronger, more confident Canada is well within our reach, if we are prepared to work for it.

We all wish to see a strong, united and prosperous Canada. Our **Plan for Economic Recovery** will help us achieve that goal.

The Honourable Michael H. Wilson
Minister of Finance

THE PLAN FOR ECONOMIC RECOVERY

The budget sets out the government's **Plan for Economic Recovery**. Its goal is not only to end the recession but to restore strong, continuing growth that leads to renewed prosperity.

The key to recovery is lower interest rates. This will be achieved through the following actions.

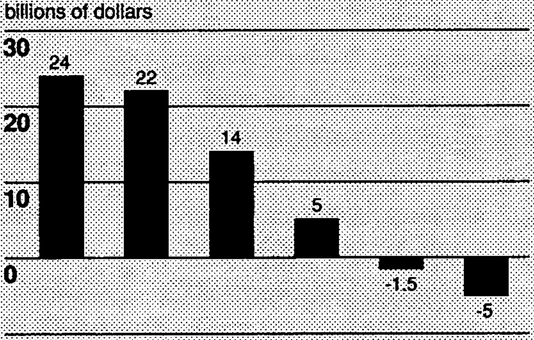
- **Clear, achievable inflation targets have been established to reduce inflation to 2 per cent by the end of 1995.**
- **Government finances will be put firmly on course to a balanced budget.** The existing Expenditure Control Plan will be extended and backed up with legislated program spending limits. All revenues from the Goods and Services Tax and privatization will flow into a Debt Servicing and Reduction Fund.
- **The operations of government, including wages and salaries, will be severely restrained.**

As a result of these actions, key fiscal goals will be achieved.

- New federal borrowing in financial markets will be eliminated after 1993-94.
- Program spending growth will be limited to an average of 3 per cent per year after 1991-92.
- The deficit will be held to $30.5 billion this year and next, despite the pressures of recession. In 1992-93, with recovery and lower interest rates, the deficit will fall below $25 billion for the first time in a decade.

The budget will result in a better balance between fiscal and monetary policy. **This will provide the lower interest rates and greater confidence essential to economic recovery.**

Chart 1
Financial requirements[1]
1990-91 to 1995-96



[1] Excluding foreign exchange transactions.

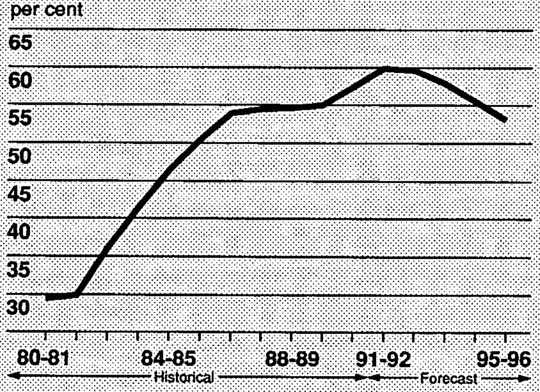
FACING UP TO ECONOMIC REALITY

The budget reflects sensitivity to current economic difficulties. While program expenditures are tightly controlled over the medium term, they will increase by 6.9 per cent in 1991-92. More than 80 per cent of the increase will go for assistance to the unemployed, the elderly and farmers in difficulty, as well as to support Canada's role in the Persian Gulf.

At the same time, the **Plan for Economic Recovery** meets the need for tough, determined action to solve Canada's fundamental economic and fiscal problems. Canadians are being asked to share the burden of restraint to ensure a durable recovery.

In earlier times, periods of economic weakness have been occasions for Ministers of Finance to put some extra money in people's pockets, spend more on programs, and worry less about the government's fiscal situation. But in earlier times, Canadians did not have to face persistently high deficits, high public debt and the economic damage that would result from ignoring these problems. During the last recession, Canada's deficit doubled from $14 billion to $28 billion. We are still struggling with the problems this caused.

Chart 2
The debt-to-GDP ratio: 1980-81 to 1995-96



The public debt will reach $400 billion by mid-year – about $15,000 for every man, woman and child in Canada. The debt interest alone will eat up more than $43 billion next year – more than is spent on old age security, unemployment insurance and family allowances combined.

Without action, the deficit would be significantly higher than forecast over the next five years and the public debt would increase by at least $25 billion more. This would work directly against our essential goals: achieving lower inflation, lower interest rates and lower taxes, more job-creating private investment and greater economic confidence – and a stronger economy and country better able to meet the needs of Canadians.

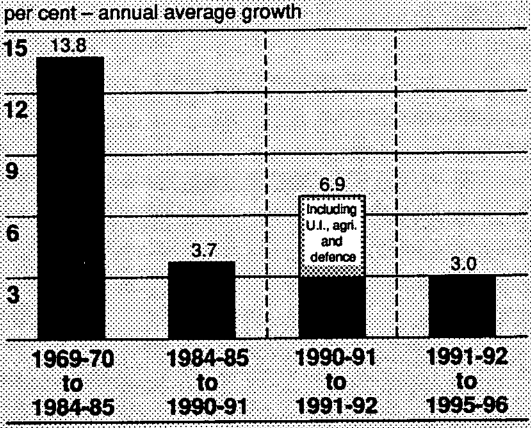
ACTION FOR RECOVERY AND PROSPERITY

The **Plan for Economic Recovery** builds confidence and certainty by restoring the financial stability of government. The budget's expenditure restraint and efficiency measures will save almost $15 billion in five years.

Extending the Expenditure Control Plan

The 1990 budget introduced a two-year Expenditure Control Plan that affected a broad range of government spending, with some important exceptions. This plan will be extended. Exemptions will be continued for income support programs for seniors, families and veterans, unemployment insurance, as well as the Equalization program and Canada Assistance Plan payments to lower-income provinces. Indian and Inuit programs will also be exempted.

Chart 3
Growth in program spending



Under the Expenditure Control Plan:

- The existing 5-per-cent cap on the growth of Canada Assistance Plan payments to the fiscally stronger provinces of Ontario, British Columbia and Alberta will be extended for three additional years.
- The existing freeze on total per capita cash and tax transfers to the provinces under Established Programs Financing will also continue through 1994-95. These transfers will continue to grow with provincial populations.
- A number of other programs will remain frozen, including payments under the *Public Utilities Income Tax Transfer Act*, payments to Telefilm Canada and concessional loan financing by the Export Development Corporation.
- Science and technology programs and cash payments under Official Development Assistance will grow at 3 per cent per year.
- The existing 15-per-cent reduction in planned funds for new social housing will continue.
- Grants and contributions to businesses, interest groups and individuals will be reduced by $75 million next year and $125 million thereafter.

Programs which are exempt from the extension of the Expenditure Control Plan, accounting for 60 per cent of program spending, will grow at an average annual rate of 3.9 per cent from 1991-92 to 1995-96. All other program spending will grow at an average annual rate of 1.7 per cent.

A number of recent expenditure decisions are being reconsidered.

- The previously announced contribution of $88 million to the Toronto Ballet Opera House will be withdrawn.
- Expenditures under the Green Plan will be spread over six years instead of five.
- Funding for the Canadian Jobs Strategy will be reduced by $100 million in 1991-92.
- The provision of financial support for the construction of concert halls in Edmonton and Montreal will be delayed.
- The cultural research institute in Montreal will be delayed.

Reforming government management

Government operating costs have been tightly restrained since 1984 and have actually declined in real terms. This was achieved by reducing the size of the public service, eliminating programs and improving efficiency.

Further actions are being taken to restrain costs and improve efficiency.

- Ministerial pay for the Prime Minister and Cabinet members will be frozen for one year.
- Wage budgets of departments will not be adjusted in 1991-92 for any increases in costs arising out of new collective agreements. Departments will have to absorb any higher costs from within existing budgets. Each increase of 1 per cent in average wage settlements across the public service could lead to a loss of about 2,000 jobs.
- Over the next three years, the government is not prepared to contemplate public service wage increases beyond 3 per cent at an annual rate.

- Rates of salary increase for the executive category in the public service, deputy ministers and heads of Crown corporations will be limited to the average of negotiated settlements in the federal public service.
- Salaries of Members of Parliament and the Senate, which currently increase at the rate of inflation minus 1 per cent, will be limited to the lesser of that formula or average public service settlements.
- Layers of management will be eliminated and the number of senior managers in the public service will be reduced by 10 per cent.
- Capital spending and non-wage operating budgets will be frozen at 1990-91 levels and growth will be tightly constrained thereafter.

These restraint and efficiency measures will generate savings of $3.6 billion over the next five years.

Wage policy

Continuing wage restraint is a key element of the **Plan for Economic Recovery**. It contributes to fiscal progress and helps ease inflationary pressures. Pay restraint is also needed at the provincial and municipal levels where wage settlements have been running ahead of inflation. Some provinces have already introduced programs to limit the pay increases of their employees. It is vital that all provinces take part.

Reducing private sector wage pressures will also help to lower costs, improve our competitive position and help reduce both inflation and interest rates. This will lead to more growth, new jobs and higher incomes.

Other management and efficiency initiatives

A number of other actions are being taken to streamline operations and encourage efficiency. The Department of National Revenue will take steps to improve the collection of tax revenues. Changes will also be introduced to permit the recovery from tax refunds of debts owing to the government. New cost-recovery measures will be implemented in the areas of transportation services and border crossings.

Privatization and Crown corporations

Since 1984, the government has privatized or dissolved more than 20 Crown corporations. Action will proceed to privatize Petro-Canada, Telesat Canada and CN Exploration. The Canada Oil and Gas Lands Administration will be disbanded and its responsibilities transferred to other departments. Petro-Canada International Assistance Corporation will be dissolved.

The use of Special Operating Agencies will be extended to improve efficiency and cut costs. Organizations or functions to be converted to this status include the Canadian Grain Commission, Race Track Supervision, and the Intellectual Property Directorate of Consumer and Corporate Affairs.

The functions of the Office of Privatization and Regulatory Affairs will be redeployed to other departments. Ongoing and future privatizations will be managed by the Department of Finance under the responsibility of the Minister of State (Finance and Privatization).

Legislating spending limits

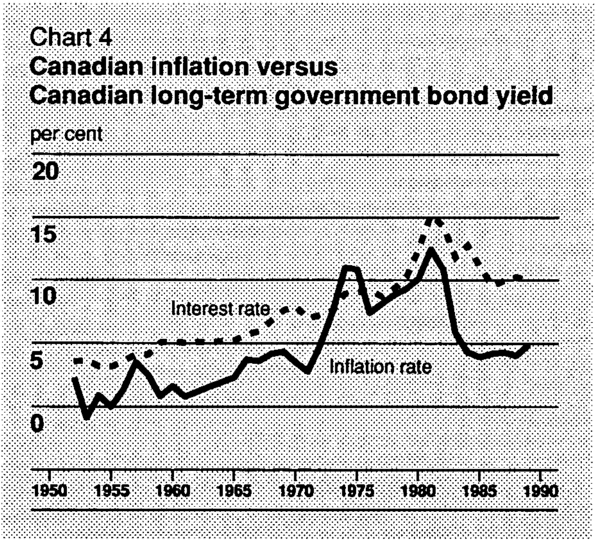
To provide Canadians further assurance that future program spending will be managed tightly, expenditure limits on program spending will be imposed by legislation for the next five years.

Setting these limits in law will ensure that this budget's program spending track will be met. This law will bring a significant change to the way government manages its expenditures. The government will consult on the precise form this important legislation should take.

Targeting GST revenues to reduce the deficit

To address public concerns that revenues from the Goods and Services Tax might be used to finance new spending instead of to reduce the deficit, a further safeguard will be provided.

All GST revenues will be allocated solely to the effort to bring the public debt under control. This will be done through legislation to establish the Debt Servicing and Reduction Fund into which all GST revenues will flow, as well as privatization revenues and contributions from individuals and businesses.



Establishing national inflation targets

The government and the Bank of Canada have made a clear commitment to achieving price stability in order to promote stable growth, equity and prosperity in Canada. To help achieve this, the **Plan for Economic Recovery** establishes intermediate inflation targets to serve as key steps on the way to price stability. The government is committed to lowering inflation gradually to 2 per cent by 1995.

Revenue measures

Financing unemployment insurance

To prevent debt problems from building up in the unemployment insurance fund, steps will be taken to ensure the fund remains self-financing. The unemployment insurance premium rate will rise by 55 cents per $100 of insurable earnings to $2.80 for employees. For employers, the rate will increase to $3.92. These measures will take effect July 1, 1991. The after-tax cost of the increase for employees with the maximum insurable earnings will be $2.70 per week.

Increased tobacco taxes

To raise additional revenues and help discourage younger Canadians from smoking, the excise tax on cigarettes is increased by three cents per cigarette. The excise tax on other tobacco products is increased proportionately. This measure, which complements the government's national strategy to reduce tobacco use, is expected to result in 100,000 fewer teenage smokers.

Measures to assist disabled Canadians

Since 1984, the government has taken major steps to promote equal opportunities for Canadians with disabilities. The Prime Minister has appointed a Minister responsible for the Status of Disabled Persons; the *Employment Equity Act*

Disabled Persons; the *Employment Equity Act* has been passed; fairer, more generous tax assistance has been put in place.

A number of steps are being taken to further assist disabled Canadians.

- The disability tax credit will be increased from $575 to $700 as of the 1991 taxation year.
- The definition of expenses eligible for the medical expense tax credit will be broadened and will include the cost of part-time attendants in the home.
- Costs paid by employers to modify their premises for disabled persons will become fully deductible in the year they are incurred.
- Benefits provided by employers to disabled persons to enable or assist them to work will no longer be taxable.

THE PROSPERITY CHALLENGE

Strengthening Canada's ability to compete in a tough, rapidly changing economic world is essential to ensure prosperity. Greater productivity will improve our competitiveness. It is the key to our future earning power.

The government will launch a national effort to build a new partnership for prosperity that draws fully on the ideas and efforts of Canadians. A discussion paper will be released in the spring to help focus debate toward the building of a broader consensus on problems and solutions.

The government proposes to encourage greater investment in shares of Canadian companies by changing the tax treatment of pension funds to eliminate the existing bias in favour of debt investments. Proposals will be discussed with interested parties.

FEDERAL-PROVINCIAL FISCAL ARRANGEMENTS

Transfers to provinces are too large to exempt from expenditure restraint. Nevertheless, major transfer programs for provinces will continue to grow at a rate greater than all other federal program spending.

Medicare

Concerns have been expressed that limiting growth of transfers under Established Programs Financing will limit the ability of the federal government to continue enforcing national medicare principles under the *Canada Health Act*. Legislation will be introduced to ensure that the government continues to have the means to enforce national medicare principles. The principles of the *Canada Health Act* will not be compromised.

Reform of the major transfer programs

Working with the provinces, the federal government will consider reforms to the major transfer programs to ensure the system provides for the sharing of the opportunities and benefits of Confederation; supports a more efficient and competitive Canada; and maintains the principles and standards that are the basis of Canadian citizenship while respecting provincial flexibility.

The government will seek the views of Canadians on these important issues.

Federal-provincial tax collection agreements

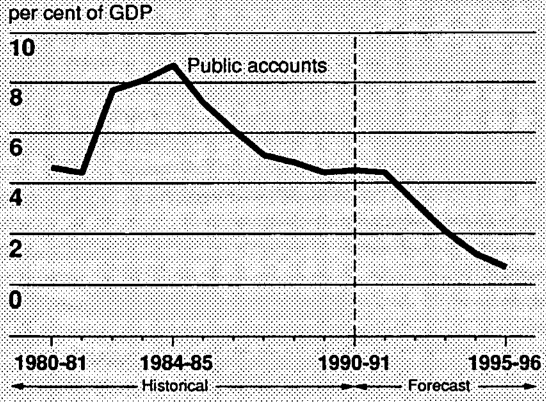
In response to provincial concerns that federal-provincial tax collection agreements do not provide enough flexibility to meet provincial priorities, the government will explore reforms in a discussion paper to be released for consultation in the spring.

ECONOMIC OUTLOOK

The components of the **Plan for Economic Recovery** reinforce each other. Lower deficits and less government borrowing will mean more favourable conditions for lower inflation and interest rates. This in turn will help to reduce the deficit by spurring stronger growth and reducing the interest costs of carrying the public debt.

The economic recovery will begin in the second half of this year and accelerate next year. Inflation and interest rates will decline. Economic growth will gain momentum and real personal disposable income will grow steadily in the medium term. Employment growth will also begin in the second half of this year and will strengthen in the years ahead.

Chart 5
The deficit
1980-81 to 1995-96



"I believe that this budget will help us regain some of the key elements that brought us strong growth in the past – low inflation, responsible financial management and a desire to work together to succeed.

"The realization of this can rekindle our pride and give us a solid basis for hope and confidence in the future – hope that is important at this time in our history. For a strong economy will strengthen our national unity... and faith in our national unity will reinforce our economic strength."

The Honourable Michael H. Wilson
February 26, 1991