Canadian Federal: 2019–20 Budget

SUMMARY

- **The 2019 Canadian Federal Budget (*Budget*) continues to project deficits in every fiscal year through 2023–24 (FY24). A declining accumulated deficit-to-GDP ratio continues to anchor fiscal planning.**
- **A reduced $14.9 bn shortfall is forecast for FY19. The projected fiscal shortfall in FY21 is $1.6 bn greater than in November, but FY22–24 balances are a cumulative $2.4 bn lower than to the prior projection.**
- **As expected, support for first-time homebuyers and workforce training represented *Budget*'s signature policy announcements, and were largely financed by this year's fiscal windfall.**
- **The Government expects to borrow $280 bn in FY20, the entirety of which will be sourced from domestic and foreign wholesale markets. Refinancing of maturing debt is projected to total $250 bn with a financial requirement of $32 bn.**
- **The updated fiscal blueprint is unlikely to alter the current Bank of Canada policy rate path.**

Budgetary outcomes have largely landed as set out in the Fall Economic Statement. A deficit of about $14.9 bn is forecast for FY19, falling to about $9.8 bn in FY24 (chart 1, p.2). The accumulated deficit-to-GDP continues a modest decline from its current 30.8% to 28.6% by FY24 (chart 2, p.2).

A largely unchanged bottom line masks important dynamics at play. Revenue growth has been exceptional at 6.7% growth this year. Despite a temporary slowdown in growth late last year, revenue receipts across the board have over-performed, both on the personal and corporate income tax fronts. Strong employment along with corporate reassessments are among factors explaining the strong growth. Expenditure growth modestly exceeded expectations growing around 5% this year. While downward revisions to nominal growth forecasts (to 3.8%, 3.4%, and 3.5 % in 2018, 2019, and 2020 respectively) create some headwind, we could have expected deficits to be trimmed by $27.8 bn cumulatively through FY24. A budget spend of $22.8 bn through FY24 will absorb this space, along with an additional $4 bn committed since the 2018 Fall Statement.

What does $22.8 bn buy? The budget aims to "*make sure all Canadians feel confident and secure about their future*". It announces dozens of new measures targeting the diversity of Canadian interests: housing support for first-time home buyers, incentives for re-training, cheaper educational financing for students, incentives for older workers to stay in the workforce, incentives for zero-emission vehicles for the environmentally conscious, to name a few.

The direct economic impact will be very modest in the near term. A small, near-term boost can be expected from one-time investments of about $3.2 bn in FY19 towards municipal infrastructure and energy efficiency projects. Investments

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Updated Fiscal Forecast
CAD bn

	FY19 FES*	FY19 Rev.	FY20 Rev.	FY24** Fcst.
Personal Income Tax (PIT)	161.9	162.8	170.4	189.2
Corporate Income Tax (CIT)	49.5	52.0	46.3	50.1
Other Tax Revenue	65.7	68.1	69.0	73.0
Total Tax Revenue	**277.1**	**282.9**	**285.7**	**312.3**
Employ. Insurance (EI) Premiums	22.0	21.4	22.0	24.0
Other Revenue	29.8	27.9	28.7	32.5
Total Revenue	**328.9**	**332.2**	**338.8**	**373.6**
Elderly Benefits	53.4	53.3	56.2	65.1
Employ. Insurance (EI) Benefits	20.1	18.8	19.9	23.3
Children's Benefits	23.9	23.9	24.3	25.4
Major Transfers to Persons	**97.5**	**96.0**	**100.4**	**113.8**
Transfers to Other Levels of Gov't	73.8	76.0	76.9	83.8
Direct Program Spending	149.0	151.5	152.1	156.2
Total Program Spending	**320.2**	**323.5**	**329.4**	**353.9**
Debt Service	23.8	23.6	26.2	30.8
Total Expenditure	**344.1**	**347.1**	**355.6**	**384.7**
Adjustment for Risk	3.0	0.0	3.0	3.0
Budget Balance	**-18.1**	**-14.9**	**-19.8**	**-14.1**
Accumulated Deficit	**687.7**	**685.6**	**705.4**	**744.6**
Annual Change, %				
Personal Income Tax (PIT)	*5.4*	*6.0*	*4.7*	*4.3*
Corporate Income Tax (CIT)	*3.5*	*8.8*	*-11.0*	*3.3*
Total Tax Revenue	*5.3*	*7.5*	*1.0*	*3.7*
EI Premiums	*4.1*	*1.2*	*2.8*	*3.6*
Total Revenue	***4.9***	*5.9*	***2.0***	***3.9***
Elderly Benefits	*5.4*	*5.2*	*5.4*	*5.9*
Employ. Insurance (EI) Benefits	*2.0*	*5.2*	*5.9*	*5.7*
Children's Benefits	*2.0*	*2.0*	*1.7*	*1.8*
Major Transfers to Persons	***4.0***	*2.4*	***4.6***	***4.9***
Transfers to Other Levels of Gov't	*4.7*	*7.8*	*1.2*	*3.5*
Direct Program Spending	*1.8*	*3.5*	*0.4*	*1.2*
Total Program Spending	***3.1***	*4.1*	***1.8***	***2.9***
Total Expenditure	***3.5***	*4.4*	***2.4***	***3.1***
Memo Items, %				
Tax Revenue / GDP	12.7	12.4	12.4	12.4
Total Revenue / GDP	14.9	14.7	14.7	14.8
Total Program Spending / GDP	14.6	14.3	14.3	14.0
Budget Balance / GDP	-0.7	-0.9	-0.9	-0.6
Accumulated Deficit / GDP	30.8	30.7	30.7	29.6
Net Debt / GDP	34.7	34.5	34.5	33.3
Debt Service / Revenue	8.3	9.2	9.2	9.9

* Fall Economic Statement 2018 projection. ** Average annual growth for FY21–24. Sources: Finance Canada; Statistics Canada; nominal GDP forecasts: Scotiabank Economics.

in education and training can provide a boost over the medium term, but will provide little relief to businesses aiming to fill jobs today and do little to tap the biggest labour force gap—female participation. Similarly, modest new investments in R&D, as well as the elimination of the income threshold for small business Scientific Research & Experimental Development (SR&ED), will take time to translate into growth. Meanwhile, the majority of new spending targets social and reconciliation objectives.

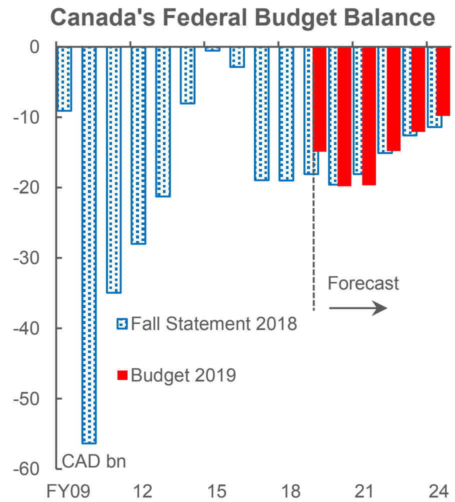
Similarly, the impact of the new housing measures will likely be marginal at best. One of the key concerns in advance of *Budget* was that affordability measures for first-time buyers might stoke housing demand, thereby pushing home values higher and exacerbating the current predicament. The First Time Homebuyers Incentive (FTHBI) affects only buyers who have already qualified for an insured mortgage and is unlikely to have this effect. However, modest increases in RRSP withdrawals for down payments will likely offer only marginal support for buyers who seek to enter, for instance, the Vancouver market, where average home sales prices regular exceed $1 mn. We support continued efforts to boost housing supply.

Banking the savings could have accelerated the reduction of Canada's federal debt. At this mature phase of the economic cycle, we should be cognisant of risks ahead and the tools available should they materialize. Government policies are still largely supportive—with a lot of money still working its way through the system including in the infrastructure and innovation space—so modest additional stimulus was not necessary. We are not on the brink of a recession. Paying down the debt burden now would keep our powder dry for such a future event.

The government is no doubt betting on a boost to confidence with this budget. The stage is set for a rebound in growth: trade uncertainty has dissipated, business sentiment is decent, job creation remains robust, oil prices are recovering, and housing markets are stabilizing. Government policies remain accommodative including recently introduced corporate tax measures in the Fall Economic Statement and a temporary pause in the Bank of Canada's interest rate tightening cycle. But we are still waiting to see this translate into accelerated business investment. The government is likely be banking on a mildly simulative budget to bridge that gap, and importantly, to be in power when it happens.

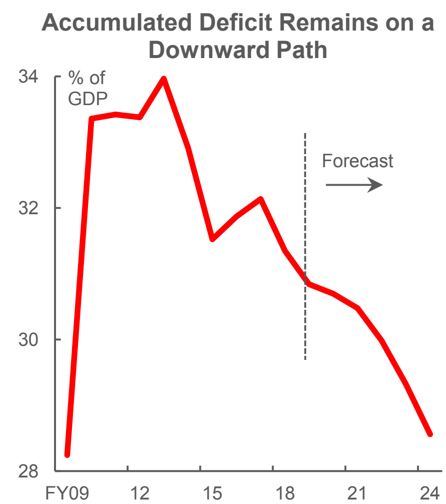
Longer-term fiscal pressures loom on the horizon. This budget commits to a national pharmacare plan with the establishment of the Canadian Drug Agency, which will come with a steep price tag in the order of $20 bn per year. We can expect green finance to be another steep initiative debated over the summer. While Canada's federal debt levels are sustainable, especially relative to peers, few provinces are in a position to shoulder significant new costs despite ongoing consolidation efforts. Addressing these longer-term challenges will require a significant boost to Canada's growth potential. This budget defers these difficult debates.

Chart 1



Source: Scotiabank Economics, Finance Canada.

Chart 2



Source: Scotiabank Economics, Finance Canada.

BUDGET HIGHLIGHTS AND POLICY DETAILS

Measures designed to improve housing affordability and availability were a key plank of the Government's fiscal blueprint, and aim to support first-time homebuyers and spur new construction. They come with a modest price tag of $885 mn over five years, with costs forecast to rise steadily from FY20 to FY24.

Under the FTHBI, first-time buyers with a minimum down payment already secured can apply to finance a portion of their home purchase through a shared equity mortgage with the CMHC. The FTHBI reduces the amount of an insured mortgage—by 10% of the home purchase price for newly constructed homes or by 5% for existing structures—for first-time home buyers with household incomes under $120,000 per year. Participants' insured mortgage and the Incentive amount cannot exceed four times the participants' annual household incomes. The RRSP withdrawal amount for down payments by first-time homebuyers was also increased from $25,000 to $35,000.

For new construction, the Rental Construction Financing Initiative, which offers low-cost loans for the construction of new rental housing for modest-income Canadians, will be extended to FY28, with costs of $385 mn over FY20–24. The Government will also allocate $250 mn during the planning horizon towards a new Housing Supply Challenge to explore new avenues to enhance housing supply; details of the program will come this summer. An Expert Panel on the Future of Housing Supply and Affordability will also be launched, alongside actions to enhance real estate tax compliance.

With respect to training and skills development, Budget outlines FY20–24 investments of $4.6 bn. The new Canada Training Benefit offers a non-taxable benefit of $250 per year for tuition and training fees for those who take time off work. Individuals who earn between $10,000 and $150,000 per annum will be eligible, with lifetime benefits capped at $5,000. An expansion of the current Employment Insurance program, which comes with an FY20–24 price tag of $1.2 bn, will allow for up to four weeks of income support. *Budget* also lowers interest rates on Canada Student Loans and Canada Apprentice Loans and offers supports for youth employment, which include outlays of $631.2 mn over FY20–24 for new post-secondary student work placements in Canada.

On infrastructure, *Budget* provides a one-time transfer of $2.2 bn in FY19 through the federal Gas Tax Fund to address municipalities' and First Nations communities' short-term infrastructure priorities.

Budget defers further action on carbon pricing, but provides modest investments in energy efficiency and clean energy alternatives. A signature initiative provides about $560 mn through FY24 to support zero-emission vehicles including a purchase incentive of up to $5,000 for zero-emission vehicles, full-tax write- offs for businesses, and investments in supporting infrastructure. It also provides a one-time transfer of about $1 bn in FY2018−19 to the Federation of Canadian Municipalities to increase energy efficiency in residential and commercial buildings.

An investment of $1.7 bn will support universal high-speed internet in rural, remote and northern communities. *Budget* also provides $255 mn through FY24 to advance forest sector diversification.

Economic Assumptions
annual % change except where noted

	18	19f	20f	Average 21–23f
CANADA - Real GDP				
Finance: 2019 Budget*	1.9	1.6	1.7	1.8
2018 Fall Statement	2.0	2.0	1.6	1.8
Scotiabank Mar. 7, 2019	1.8	1.5	2.0	n.a
GDP Deflator				
Finance: 2019 Budget*	1.9	1.6	1.9	2.0
2018 Fall Statement	2.2	2.1	1.7	2.0
Scotiabank Mar. 7, 2019	1.7	0.9	2.4	n.a.
Nominal GDP				
Finance: 2019 Budget*	3.8	3.4	3.5	3.9
2018 Fall Statement	4.2	4.1	3.3	3.9
Scotiabank Mar. 7, 2019	3.6	2.4	4.6	n.a
Unemployment Rate, %				
Finance: 2019 Budget*	5.8	5.7	5.9	6.0
2018 Fall Statement	5.9	5.8	6.0	6.0
Scotiabank Mar. 7, 2019	5.8	5.8	5.9	n.a
T-Bills**, 3-month, %				
Finance: 2019 Budget*	1.4	1.9	2.2	2.4
2018 Fall Statement	1.4	2.1	2.4	2.5
Scotiabank Mar. 7, 2019	1.4	1.8	2.2	n.a
Bonds**,10-year, %				
Finance: 2019 Budget*	2.3	2.4	2.7	3.1
2018 Fall Statement	2.3	2.8	3.0	3.2
Scotiabank Mar. 7, 2019	2.1	2.0	2.4	n.a
Canadian Dollar**, US¢/C$				
Finance: 2019 Budget*	77.2	76.3	77.2	78.6
2018 Fall Statement	77.6	78.4	78.7	80.3
Scotiabank Mar. 7, 2019	78.0	76.5	80.5	n.a
U.S. - Real GDP				
Finance: 2019 Budget*	2.9	2.4	1.7	1.8
2018 Fall Statement	2.8	2.5	1.8	1.9
Scotiabank Mar. 7, 2019	2.9	2.4	1.8	n.a
WTI Oil, US$/barrel				
Finance: 2019 Budget*	66	59	60	63.0
2018 Fall Statement	67	68	65	68
Scotiabank Mar. 7, 2019	65	58	62	n.a

*Updated for historical revisions, retroactive change in Government's discount rate methodology for unfunded pension benefit obligations
**Annual averages. Sources: Finance Canada, Statistics Canada, BEA, Bloomberg, Scotiabank Economics.

Oil and gas sector challenges were acknowledged in *Budget*. The Government emphasized a need for more transportation capacity but noted the alleviation of the light-heavy oil price differential following the Alberta government's production curtailment policy and the resumption of normal US refinery operations. It will provide $100 mn beyond that already announced over four years, starting in FY20, to the Strategic Innovation Fund to support the transition to green technology, as well as $100 mn over FY20–22 for economic diversification programming in Western Canada.

To encourage scale-up among innovative firms, the Government will phase out the taxable income threshold below which small and medium-sized businesses are eligible for a refundable tax credit equal to 35% of scientific research and experimental development expenditures. The threshold for taxable capital will remain in place.

Developments Since the 2018 Fall Economic Statement
CAD bn

	FY19	FY20	FY21	FY22	FY23	FY24	FY20-FY24
***Fall Statement 2018*: Deficits**	**-18.1**	**-19.6**	**-18.1**	**-15.1**	**-12.6**	**-11.4**	**-94.9**
Risk Adjustment	3.0	3.0	3.0	3.0	3.0	3.0	18.0
***Fall Statement 2018*: Deficits No Risk Adjustment**	**-15.1**	**-16.6**	**-15.1**	**-12.1**	**-9.6**	**-8.4**	**-76.9**
Economic & Fiscal Developments	5.9	4.8	4.7	3.7	4.1	4.6	27.8
Revised Deficits Before Policy Actions	**-9.2**	**-11.8**	**-10.4**	**-8.4**	**-5.5**	**-3.8**	**-49.0**
Policy Actions Since *Fall Statement 2018*	-1.4	-1.0	-0.6	-0.6	-0.2	-0.2	
Policy Actions in *2019 Budget*							
Support for Households	0.0	-0.6	-1.3	-1.8	-2.3	-2.4	-8.4
Business Investment and Infrastructure	-3.2	-0.3	-0.8	-0.8	-0.6	-0.4	-6.1
Advancing Reconciliation	-0.9	-0.7	-1.0	-1.0	-0.6	-0.6	-4.8
Social Policy Spending	-0.1	-1.7	-1.6	-0.8	-0.5	-0.6	-5.3
Other	0.0	-0.7	-0.9	1.6	0.6	1.2	1.8
Subtotal	**-4.2**	**-4.0**	**-5.7**	**-2.7**	**-3.4**	**-2.8**	**-22.8**
Total Policy Actions	**-5.6**	**-5.0**	**-6.3**	**-3.3**	**-3.6**	**-2.9**	**-26.7**
***2019 Budget:* Deficits No Risk Adjustment**	**-14.9**	**-16.8**	**-16.7**	**-11.8**	**-9.1**	**-6.8**	**-76.0**
Risk Adjustment		3.0	3.0	3.0	3.0	3.0	**15.0**
***2018 Budget:* Deficits**	**-14.9**	**-19.8**	**-19.7**	**-14.8**	**-12.1**	**-9.8**	**-91.0**

Source: Finance Canada.

Borrowing Details
CAD bn

Sources of borrowings	
Payable in Canadian currency	
Treasury bills[1]	151
Bonds[2]	119
Total payable in Canadian currency	270
Payable in foreign currencies	10
Total cash raised through borrowing activities	280
Uses of borrowings	
Refinancing needs	
Payable in Canadian currency	
Treasury bills	131
Bonds	111
Of which:	
Switch bond buybacks	1
Cash management bond buybacks	40
Retail debt	1
Total payable in Canadian currency	243
Payable in foreign currencies	7
Total refinancing needs	250
Financial source/requirement	
Budgetary balance	20
Non-budgetary transactions	
Pension and other accounts	-6
Non-financial assets	3
Loans, investments and advances	8
Of which:	
Loans to enterprise Crown corporations	7
Other	1
Other transactions[3]	8
Total non-budgetary transactions	12
Total financial source/requirement	**32**
Adjustment for risk[4]	-3
Change in other unmatured debt transactions[5]	1
Net increase or decrease (-) in cash	0
Total uses of borrowings	**280**

Notes: Numbers may not add due to rounding. A negative sign denotes a financial source.

[1] Treasury bills are rolled over, or refinanced, a number of times during the year. This results in a larger number of new issues per year than the stock of outstanding at the end of the fiscal year, which is presented in the table.

[2] Includes switch buyback issuance.

[3] Other transactions primarily comprise the conversion of accrual transactions to cash inflows and outflows for taxes and other accounts receivable, provincial and territorial tax collection agreements, amounts payable to taxpayers and other liabilities, and foreign exchange accounts.

[4] The $3 billion risk adjustment included for prudent fiscal planning purposes is removed to increase the accuracy of borrowing needs. If the risk adjustment is needed, the debt strategy can be adjusted accordingly.

[5] Includes cross-currency swap revaluation, unamortized discounts on debt issues, obligations related to capital leases and other unmatured debt.

Source: Department of Finance Canada, *Budget 2019*.