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Chair

Mr. James Rajotte

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● (1530)

[*English*]

The Chair (Mr. James Rajotte (Edmonton—Leduc, CPC)): I call the 44th meeting of the Standing Committee on Finance to order.

Thank you all for being here.

Pursuant to Standing Order 108(2), the orders of the day are a study of the government's economic update and fiscal projections.

We have four organizations represented here this afternoon. From the Library of Parliament, we have Mr. Kevin Page, the Parliamentary Budget Officer; Mr. Mostafa Askari, assistant parliamentary budget officer; Mr. Sahir Khan, assistant parliamentary budget officer; and Mr. Chris Matier, senior advisor, economic and fiscal analysis.

The second organization we have is the C.D. Howe Institute, and Mr. Finn Poschmann. From TD Bank Financial Group, we have Mr. Derek Burleton. From our fourth organization, Scotiabank Group, we have Ms. Mary Webb, senior economist and manager.

Thank you all for being with us here this afternoon. You each have up to 10 minutes for an opening statement.

We will start with Mr. Page, please.

Mr. Kevin Page (Parliamentary Budget Officer, Library of Parliament): Thank you.

Good afternoon, Mr. Chair, vice-chairs, and members of the committee.

Thank you for inviting me and my colleagues to speak to you about Canada's economic and fiscal outlook.

These are challenging times for budget makers across the world. The level of economic uncertainty remains high. The pace of economic recovery has slowed for many G-8 countries at a time when economies are still operating well below their potential. The slowdown in growth is also taking place at the same time as governments are considering the end of fiscal stimulus programs and the implementation of austerity measures to reduce budgetary deficits.

There are significant policy trade-offs and risks. Policy makers need to steer a policy course between short-term support for a fragile economic recovery, on the one hand, and the avoidance of a buildup of public debt that will burden future generations on the other. There are also structural problems—low productivity growth, aging demographics, and fiscal imbalances—that will require structural solutions.

[*Translation*]

In this context, policy and budget makers in Canada need to place a premium on fiscal transparency and analysis to support policy debate leading up to the 2011 Budget.

Today, my office released a paper updating our five-year fiscal projections. We have updated our analysis of the cyclical and structural components of the projected federal budgetary deficits. We have provided a new quantitative assessment of the uncertainty and risks around these projections.

A few weeks ago, we made available analysis that looked at international and Canadian experiences with fiscal rules (i.e., legislative and/or strong political commitments to budgetary constraint).

We made the case that parliamentarians may wish to commence debate on the next generation of fiscal rules in Canada. It highlighted the need for this discussion to include a long-term perspective on Canada's fiscal challenges; to look at all levels of government in a fiscal federalism context; to account for risk and uncertainty; and to separate the cyclical from structural aspects to Canada's budgetary balance outlook.

In the weeks ahead, PBO will release analysis on the impact of fiscal stimulus in Canada with a focus on the Infrastructure Stimulus Fund. The goals of this work are: to estimate the short-run economic impacts; to track budget implementation; and to draw some preliminary lessons to aid future policy deliberations.

Next spring, PBO will release an updated fiscal sustainability report. The report will examine the fiscal actions required to maintain a steady debt to GDP ratio in Canada, not just from a federal perspective, but from a total government perspective.

● (1535)

[*English*]

I wish to highlight some messages and observations from the report we released today regarding our economic and fiscal situation and outlook.

Canadian economic activity still remains well below its level of full capacity—potential GDP. Given the average private sector forecast and PBO's estimate of potential GDP, the output gap is projected to narrow gradually over the medium term, and the economy will reach its potential by the end of 2016.

While real GDP has almost recouped all the losses from the first quarter of 2008 to the second quarter of 2009, Canadian economic activity still remains well below PBO's estimate of potential GDP of about 2.9 percentage points. Labour market indicators also suggest that there is a significant amount of excess capacity.

While the level of employment has returned to its pre-recession peak, it is important to recognize that total hours worked remain below their pre-recession level and 1.8% below their trend. This low level partly reflects the fact that recent employment gains have been disproportionately in part-time work. The unemployment rate remained at 8% in the third quarter of 2010, well above estimates of the natural rate of unemployment.

The Department of Finance's September survey of private sector forecasters indicates that the outlook for nominal GDP over the medium term—the broadest measure of the government's tax base—is little changed from the forecast on which Budget 2010 was based. However, private sector forecasters have revised down significantly their outlook for interest rates, with both short- and long-term rates approximately 80 basis points lower each year on average over the 2011 to 2014 period.

The near-term outlook for the unemployment rate has been revised down somewhat, although private sector forecasters now expect a slightly higher rate of unemployment in the medium term.

PBO projects a budgetary deficit of $40 billion—2.5% of GDP—in 2010-11, declining to $11 billion—0.5% of GDP—in 2015-16. This results in a projected cumulative increase in federal debt of $200.5 billion to $658.1 billion by 2015-16, or about 32.4% of GDP, when combined with budgetary deficits realized in 2008-09 and 2009-10.

The projected reduction in the budgetary deficit over the medium term largely reflects a cyclical improvement in the economy. PBO estimates that the government's structural deficit will decline only gradually to $10.2 billion in 2015-16, or 0.5% of potential income.

Notwithstanding the extent to which Canada's fiscal plan has been thrown off course since the recent global recession, Canadian fiscal balances and debt levels are in a relatively better position than those of many of our competitors. The magnitudes of Canada's structural deficits over the medium term are significantly smaller than the structural deficits observed in the 1980s and 1990s. From this relative perspective, it is fair to say that Canada's fiscal challenges appear less severe and more manageable.

The fact that Canada has relatively better balances does not mean, however, we have a fiscal structure that is sustainable. Assessing fiscal sustainability requires looking beyond projections of budget deficits and debt over a medium-term horizon to take into account the economic and fiscal implications of the population aging.

In our 2010 fiscal sustainability report, PBO calculated a federal fiscal gap of 1% to 2% of GDP, depending on differing assumptions. This suggests that sizable and sustained fiscal actions are required to maintain a steady debt-to-GDP ratio over the longer term.

Parliamentarians need to be aware that the cost of fiscal action increases substantially the longer actions are delayed.

The PBO fiscal projections, as well as those in the government's update, are based on the results of Finance Canada's survey of economic forecasts produced by private sector organizations. Both PBO and Finance Canada translate the average private sector economic forecast into a fiscal projection based on their own assumptions.

PBO projects budgetary deficits that are moderately larger on average than those presented in PBO's March report and the government's update, owing primarily to higher operating expenditures.

Given the lack of detail regarding the government's expenses subject to the operating freeze, PBO has assumed that these expenses will grow in line with population growth and inflation—equal to 3.2% on average—over the 2010-11 to 2015-16 period. This assumption is significantly lower than both nominal GDP growth over the same period—about 4.9%—and the 6.4% average growth observed in the five years preceding the government's economic action plan.

● (1540)

[*Translation*]

In PBO's judgment, the balance of risk to the current economic outlook is heavily weighted to the downside. These downside risks include both external and domestic risks, each of which could have a substantial negative impact on economic growth in the near and medium term.

External risks relate to the U.S. outlook; the recent appreciation of the Canadian dollar and ongoing global currency tensions; and sovereign debt concerns.

Over recent quarters real GDP growth in the U.S. has slowed, employment growth has remained weak and the unemployment rate has remained well above 9%. In PBO's view the balance of risks to the U.S. outlook are clearly to the downside, which could have an important impact on the Canadian economy.

[*English*]

Currency tensions among countries have escalated in recent months, prompting discussions of competitive devaluations and tariff barriers. This could pose a downside risk to the global economic outlook. A second currency risk relates to the strong rebound in the Canadian dollar, which, since the first quarter of 2009, has outpaced a movement in commodity prices, thereby restraining growth.

While sovereign debt concerns have receded somewhat in recent months, as noted in the Bank of Canada's October 2010 monetary policy report, credit spreads remain elevated for some European countries, and a negative shock would risk triggering renewed strains in global financial markets, resulting in higher-risk premiums that would put upward pressure on global interest rates.

Domestic risks relate primarily to the high level of household debt in Canada. Household debt has continued its upward trend, reaching 147% of personal disposable income in 2009, putting households in a vulnerable position. The high level of debt of Canadian households will likely constrain growth and consumption and housing investment over the projection horizon.

The PBO report released today provides new analysis for Canada on the quantification of uncertainty and risk around economic and fiscal projections. The purpose is to enrich the analysis of the planning environment facing parliamentarians to elevate the debate away from relatively small differences in the medium-term balanced budget projections to a richer assessment of the uncertainty that incorporates the historical track record of private sector economic forecasts and PBO judgment for risk. While the government's fall update introduces a risk adjustment in its projection, in our view it is small and does not adequately reflect the magnitude of the downside risks to the economic outlook.

On a status quo basis, according to PBO estimates, the likelihood that the budget will be in a balanced or surplus position over the period 2010-11 to 2013-14 is effectively nil. There is an 85% chance of probability the budget will be in deficit in 2015-16, and there's an 88% chance that the budgetary balance of 2015-16 is lower than the $2.6 billion surplus projected in the government's economic and fiscal update. In this environment, parliamentarians may wish to debate the appropriate fiscal adjustments for uncertainty and risk, in addition to the appropriate medium-term and long-term fiscal objectives with respect to budget balances and fiscal sustainability.

In closing, PBO recommends the government consider making available their analysis on cyclically adjusted budget balances, on longer-term fiscal sustainability, and a detailed assessment of uncertainty and risk so that parliamentarians and Canadians will have access to the same level of analysis that's provided in many other countries. PBO also recommends that the government provide additional transparency related to the status of the fiscal framework for money set aside for new and proposed programs and the departmental strategies to freeze operational expenditures.

Thank you for the opportunity to speak to you today. We'd be happy to take questions after others speak.

● (1545)

[*Translation*]

Thank you very much.

[*English*]

The Chair: Thank you very much, Mr. Page.

We'll now hear from Mr. Poschmann, please.

Mr. Finn Poschmann (Vice-President, Research, C.D. Howe Institute): Thank you, Mr. Chairman and members of the committee.

Good afternoon. It's great to be back with this committee. It's a very, very friendly place to be—sometimes, anyway.

I'd like everyone to recall, as always, that while I am vice-president for research at the C.D. Howe Institute, I'm speaking on my on behalf and not that of my members and board of directors, who may not agree very much with the things I say.

To move on, I'd like to emphasize a few of the points raised by Mr. Page, including some points of agreement and some points of emphasis, and then to extend them a little bit in a policy direction.

First, you will have heard from economists for a very long time, and will continue to hear, a story about uncertainty. Economic output forecasts are always uncertain. They're especially uncertain in current times. This is an issue for budget-makers right now, because despite that degree of uncertainty, the fiscal prudence contained in the budget and the economic outlook averages only about $1 billion annually over the six-year horizon. That's about half a percentage point of revenue, or not very much. It's lower than the historical contingency reserve and lower than the economic prudence amounts of about $4 billion annually. That was about 2% of budget revenues looking back to previous years.

The point about this is that arguably it's not enough in a volatile economic environment, where fiscal projections are going to be prone to errors—and potentially big errors. That's one of the reasons it's plausible, as Mr. Page said, to look to the out-years of the planning horizon and to suspect that positive or balanced budgets may not be the most likely outcome.

So there are reasons to have some doubt, just based on volatility, about the economic forecast and the uncertainty about the forecast.

There are a few risks, some of which Mr. Page pointed out, but I'll add some others. One is that the outlook assumes a pretty low long-term financing rate for the federal government. The $2 billion to $3 billion in savings in annual debt services owing to low interest rates could come true. No one is expecting interest rates to go up very quickly right now—absolutely not—but there certainly is a risk. In bond markets, we'll be looking at higher interest rates down the road, and potentially not very far down the road.

What else are we assuming collectively among the private forecasters or from a federal perspective? We're assuming that unemployment comes down fairly quickly and that the labour market performs strongly. Again, that may well happen, but it's hardly baked in.

The other assumption in the outlook that takes us to roughly zero balance by 2014-2016 is that there will be no major new spending initiatives over the next five budgets. Again, that could be true, but it's a bit of a crash diet. It's going to take a lot of discipline to stay on it. It's great if the federal government is able to do so from a planning perspective and a fiscal perspective, but it will take a lot of willpower. That's what budget-making does, just like any diet does. So that's important, too.

Another observation is that notwithstanding these risks, the outlook for the federal government is relatively strong or positive compared with the provincial governments, where we have some major cost drivers. Mr. Page referred to the demographic pressures on health expenditures, in particular from an aging society—a story that we're very familiar with. Most of these costs are going to be centred on the provinces, where a lot of the socially driven or demographically driven spending occurs.

So those are some significant risks in the overall government budget-making process, which are going to put pressure on the federal government, obviously, particularly because of health care and looking to 2014 and beyond for it, when the current agreement for health transfers needs to be renewed. We have a more or less steady as you go, fairly quick growth rate built into health spending in the outlook right now. That's going to be an issue that will have to be dealt with by 2014. It's going to mean that the questions about fiscal imbalance will be back on the table not very long from now. Those are some familiar issues.

In particular, from a tax-raising or revenue-raising point of view, there's a question about who's going to raise the revenue to finance these growing expenditures on health. Will it be the federal government or will it be the provincial governments? For the most part, the federal government and the provincial governments occupy the same tax basis. That means that when you're talking about corporation income taxes, personal income taxes, sales or consumption taxes, the federal and provincial governments share all of those things.

So there will have to be, or perhaps there ought to be, some trade-offs as far as tax room goes in the next few years, in order that the revenue-raising ability will reside or be held by the level of government that has to conduct the spending that's funded by those taxes.

● (1550)

After alerting or pointing out to this committee some of these risks and emerging issues, I did want to make a few closing recommendations.

One, notwithstanding some of the spending risks, we, or I, don't see that much of a risk on the revenue side necessarily for the federal government. We don't see a reason to shy away from the government's planned path on corporation income tax relief. If you think about economic growth in the long run and the way corporation income taxes work, in the long run, tax relief from where we are, at 18% federally, is likely to have a positive net impact on government balances. In other words, a one percentage point drop in the current 18% federal corporation income tax rate in 2010, in the long run, is going to have a positive impact on federal revenues—not in the short term necessarily, but certainly in the long run. That's just the way corporate taxes work, because of the incentives for investment and growth and the way that corporations tend to respond to investment incentives.

The same corporation income tax reduction is potentially good for the provinces because of the growth in the tax base. Economic growth also drives provincial income growth. So there are positive externalities there as well; the provinces do well when the federal government drops its corporation income tax rate. But this is part of a plan that's essentially baked into the outlook right now, and I think it would make sense to stick with that plan.

I'd like to look back to the balance between the federal government and the provinces and to what some of us were saying a years ago about the balance between the taxing authority, corporation income tax room for the federal government, and also personal income tax room and sales tax room.

If you look back to 2005, I co-wrote, with Mr. Stephen Tapp, a paper that recommended that the federal government drop its personal income tax rate, drop the GST rate by two percentage points, and leave room for the provincial governments to raise their consumption taxes in order to fund the health spending that was necessarily part of their programs. We're part of the way there. We have seen the federal government drop 2% off its GST rate. It's important, though, that any tax room the provinces take up be smart tax room—in other words, not economically damaging tax room. That's why the conversion in Ontario and B.C., as well as Quebec and three of the eastern provinces, going back to 1997, to a harmonized sales tax system is good. There you have a smart tax system on which the provinces can put more weight. So we've created room for the provinces to do more of their funding through the HST and to fund more of their own health expenditures, and there is less pressure on the federal government to finance provincial spending through federal taxation.

So we need to start talking more about the balance between taxation and transfers from the federal government to the provinces and how the provinces set their own tax rates and finance their own spending needs.

With that, Mr. Chairman and committee, thank you.

I cede the floor.

The Chair: Thank you very much, Mr. Poschmann.

We'll now hear from Mr. Burleton, please.

Mr. Derek Burleton (Deputy Chief Economist, TD Bank Financial Group): Thank you very much, Mr. Chairman. It's a pleasure to be here.

We heard from the Office of the Parliamentary Budget Officer today, who gave us their take on the fiscal outlook for the next five years. We did send around—and hopefully you did get a copy—our fiscal table, our view, and I'll touch on that in just a second. If you don't have it, I'll qualitatively describe it.

But I do want to jump a little bit further into this issue of a wider-than-usual dispersion in private sector forecasts. I think it's very important, and it obviously reflects an extremely unusual period that we're in. I would argue that this is going to remain the case over the foreseeable future. There are two reasons why. Obviously, we're coming off a very difficult financial crisis. We're hearing central bankers around the world using the expression “greater than usual uncertainty”, but it's also this notion, in my view—and this is shared by many—that the so-called period of great moderation is behind us.

We went through a period in the nineties and through much of the 2000s where the view was that if you kept inflation low and stable, economic cycles would be less extreme than they were in the eighties and before. Some argued that there was also a little bit of luck. In the end, I think recent developments do show us that luck was at play. Part of the problem with some of these developments is that they did encourage more risk taking. The period of great moderation is behind us, so I think we can expect bigger economic cycles than we've seen in the last 15 years or so, and also in financial markets.

Just to look at the forecasts—I looked at Consensus Economics' numbers—in the range of forecasts we are looking at between 1% and something over 3% in U.S. growth next year. The Canadian dollar will be ranging between 87¢ and $1.15 through next year. For Canadian economic growth, there's a little bit less of a difference, less than 2% and more than 3%, less than the U.S. The fact of the matter is we are confronting as forecasters very difficult issues, both from a cyclical perspective and from a structural perspective.

In terms of the cycle, we talk about the external risks. In the U.S., of course, as I mentioned, all this quantitative easing...will it be effective? It's very difficult to ascertain at the moment. But I also am concerned about some of the domestic issues, some of the imbalances that we've seen develop—household indebtedness. As forecasters we're trying to assess how these imbalances will play out when interest rates are extremely low, and we expect that will remain the case in the near term. These imbalances could get worse. In my view, there's an upside risk in the near-term forecast. In the longer term, though, it could be a big downside risk. I'm just giving you a sense that these are very significant issues.

From a longer-term perspective, we're seeing economists split in two camps. You get some who think we're very much dealing with the status quo of a 3% trend growth rate, or slightly less, and others, in the camp that I'm in, who think growth is likely to be closer to 2% on a longer-term basis.

Dealing with the demographics, productivity is something that obviously is a huge driver of those medium- to long-term views. But when you think about it, most of us are a little reticent to start building in an acceleration of productivity growth. We just haven't seen it. Yet, if we were to give a list of things governments had to do 15 years ago to improve productivity, a lot of those things have been done—mostly recently, the HST, in both Ontario and B.C.—and yet we haven't seen that acceleration. Maybe it's not long enough. Maybe it's a lag.

So even though in my forecasts I don't build it in, what I'm trying to indicate here is that there are some upside risks as well to the longer-term view.

I'm assuming you did receive that forecast. If you haven't, our view is somewhere in between the Parliamentary Budget Officer's and the fiscal update. We are more negative on the longer-term projections for the economy, building in some of these downside risks on demographics. In the short term—and as Kevin Page just mentioned—in terms of some of these issues with consumer spending, I think consumers will be hard pressed to grow their spending at anything more than a very modest clip on a three-to-five-year basis, so I've built that in. I've taken our economic projections. I've left the program spending track unchanged from the budget update. I just assume that the governments are able to meet that.

Interest rate projections are built off our interest rate forecasts. We don't have a very big increase in interest rates, but very much a gradual increase to something close to what we feel is more normal. Obviously there are risks around that projection three to five years out. We have a deficit in 2015-16 of about $5 billion, which is about an $8 billion weaker projection than in the budget update, again reflecting our weaker forecasts.

● (1555)

Certainly this is not a big share of GDP—0.2%. I would argue, five years out, that it's actually not that dramatically different from the private sector. Again, there's uncertainty of how you take these projections and build your revenues off them. We've assumed a very similar track as that in the budget update in terms of GDP to revenues. That's our view of where we're headed.

To bring it to a close, one thing we need to come to grips with in future budget plans is dealing with this wider than usual dispersion. When I look around the country, I look at what other governments do. I like the B.C. model. They have a group of forecasters who meet annually. In the budget they provide about a three- or four-page text box that describes the range of private sector projections. It gives a fair amount of detail in there: who's high, who's low, and all the groups. Even in their observations they talk about how these projections unfold and the difference there. They ask us what probability we would assign to each outcome. So if my base case is this, what probability do I assign to it. They take that into account in their budget plans. I must say I would put a lower probability on this than I would have, say, three years ago. I would put maybe 50% on this outcome, this base case, whereas maybe a few years ago I would have put 60% to 70%. Again, I think looking at the broader range, as well as what my fellow speakers have commented on, more analysis on the budget would be helpful, looking at what these forecasts mean in terms of potential budget impacts.

I will stop there.

Thank you.

● (1600)

The Chair: Thank you very much for your presentation.

Ms. Webb, please.

Ms. Mary Webb (Senior Economist and Manager, Scotiabank Group): Thank you, Mr. Chair, for the invitation to speak today.

I'd like to echo the theme of uncertainty, and also the volatility that we think will continue in both foreign exchange rates and financial markets. We had such a strong initial rebound for Canada that this slowdown is only beginning to be appreciated. In fact, what we're looking for, after 3% real growth this year, is somewhere around 2.25% next year, with the U.S. being about a 0.25% below Canada's growth. It means that in terms of nominal GDP growth we may in fact be hard-pressed to reach 4% to 4.5%, and far less likely to reach 5%.

Canada, as a small economy, has a number of strengths, and I would point to our resource wealth and the strength of our corporate sector balance sheets, which is substantially stronger than in prior repair periods. But we also have significant adjustments, particularly in central Canada, and of course in Ontario, where we have seen industries, such as forest products and the motor vehicles sector, permanently downsized. So there is restructuring going on that we have to do in a world that's now dominated by growth that's fuelled by the emerging economies.

In terms of the U.S., I completely endorse the views of my colleagues. This is an economy that is under substantial duress. We are quite uncertain about the outcome of the second quantitative easing, not only in terms of the boost that it may or may not provide to real growth and job creation, but also in terms of the U.S. dollar and, eventually, the mid-term path for inflation. Our concern there as well is that the longer you delay a comprehensive fiscal repair plan, the steeper the fiscal correction will eventually be.

I think the shadow of protectionism, be it competitive currency devaluation or other means, will be hanging over us for a number of years going forward. At the same time, there is a race right now to sign advantageous bilateral trade deals so that our whole global trade framework is in the process of shifting.

Finally, Canada really benefited not only from our own domestic stimulus, but from the synchronized monetary and fiscal stimulus around the world. We're now facing a period of several years in which you have nations with different recovery paths in terms of pace and type, and you also have a simultaneous withdrawal of the fiscal stimulus and fiscal repair. We haven't had the type of fiscal repair among the developed nations on that scale simultaneously, so there is considerable uncertainty about how those interact with each other and play out.

On the domestic front, we quite strongly believe—because of our belief that the U.S. dollar will continue to soften—that the Canadian dollar will move sustainably to parity by the second half of 2011, and probably trade through parity as we look to 2012 and 2013. Our industry has learned to cope with a 95¢ U.S. dollar, but they haven't learned to cope with a dollar that might be at $1.05.

The volume of our exports in the second quarter of 2010 was about 86% of the prior peak in the second quarter of 2007. Our imports, by the way, were 99% at that peak.

We also have a concern about Canadian households having to slow their credit growth and their spending. When you look at one metric, the debt-to-income, it's at record levels. It's actually now approaching the level in the U.S., which has come down. And Canadians, because of a series of unexpected circumstances as we came out of the recession, had every incentive to borrow. If we're right, that means we face a cooler housing market and also a much more cautious Canadian consumer as provinces and the federal government try to repair their balance sheets.

There is a comparison that comes to mind, that the Parliamentary Budget Officer made: if you look at the latter half of the 1990s, from 1997 to 2000, that was a period of robust economic expansion that actually facilitated the fiscal repair progress by provinces and the federal government. The real growth was 4.4%, nominal GDP growth was 6.5%, you had a dollar that was still very weak, and you had interest rates that had declined through the 1990s. It was simply a very fortuitous period to finish that repair process. I don't think the next few years are going to be nearly as kind.

● (1605)

So we welcomed the fact that in the fall update the government had built in at least some uncertainty and the fact that their nominal GDP growth could well be less than the private sector average.

I think a scenario worth looking at is our concern that you could have several years where that happens. But instead of averaging some 2.7% real growth from 2011 through 2015, the average might be significantly below 2.5%, say 2.25%. In fact the GDP deflator is less than 2%.

That's why we're coming out with a nominal GDP that, like the TD, is some $50 billion less by the final year of the update.

Thinking about that, and therefore thinking about the path the federal government has laid out, we've always viewed fiscal 15 as being a balance, looking toward the fact that you couldn't have drastic fiscal repair because of the fragility of Canada's recovery, but also the U.S. recovery and the global recovery and the fact that one needs to move to take advantage of the window of low interest rates.

So it looks to me as though you have a process year by year of adjusting the fiscal reduction plan. Thus there is an extended period of quite significant program spending restraint that does contrast very much with the five years up to fiscal 2008 and would have a fraction of what we had. So as we potentially adjust on the program spending restraint annually, what comes to mind are the principles the U.K. brought forward. Now the U.K. is undertaking a far, far more severe austerity program, but they kept returning to the principles of equity and reform, ensuring that a strong base was laid for longer-term growth.

With respect to the last principle, we would endorse that you stay the track on the corporate tax reduction cuts that are planned. Both the provinces and the federal government will benefit from that in the longer term in terms of their revenues, as has been pointed out, and that type of measure—we are a small, open economy—will open us more to trade and foreign investment, which are extremely important.

Thank you.

The Chair: Thank you very much for your presentation.

We'll start questions from members. Mr. Brison, for a seven-minute round.

● (1610)

Hon. Scott Brison (Kings—Hants, Lib.): Thank you very much to each of you for your presentations today.

Mr. Page, in your report you confirm that Canada now has a structural deficit. How will reducing the corporate tax rate by a further three points affect our deficit targets and our return to balanced books?

Mr. Kevin Page: In our projections we've built in the reductions in corporate taxes for the next few years, so it's part of our projections for both the structural deficit and our overall budget balance.

Hon. Scott Brison: If we were not to pursue those corporate tax cuts, would we return to a balanced budget faster?

Mr. Kevin Page: I think the rough estimation is out there, and the rules of thumb as well from the Department of Finance, that for every point reduction in the corporate statutory rate, you're talking about something in the neighbourhood of $1.5 billion to $2 billion, depending on the level of corporate income.

So yes, if you are talking about three points, you could be talking upwards of $5 billion to $6 billion.

In Canada we're talking about the economy getting back to its potential in 2016 and a structural deficit of about $11 billion. It wouldn't quite close the gap, but it would help.

Hon. Scott Brison: In your report you say “the Government's current fiscal structure is not sustainable over the long term”.

Mr. Poschmann referred to the demographic shift, aging population, productivity issues, higher health care costs as we enter negotiations on the health transfers.

Is there a risk these further corporate tax cuts will not be sustainable? Is there a risk they will be need to be reversed in order to pay or eliminate the deficit within the next five years?

Mr. Kevin Page: We think the current fiscal structure for Canada is not sustainable when you look to the long term. So we will have to change the current fiscal structure to make it sustainable.

In work we did earlier in the year, sir, for our fiscal sustainability report, when we projected forward and looked at those issues of trend productivity, growth rate, and what's happening to labour input, depending on what your assumptions are for the transfers, which Mr. Poschmann has raised, you're looking at a fiscal gap for Canada of between one and two percentage points of GDP.

What I mean, sir, is that to maintain a stable debt-to-GDP ratio of roughly 33% and to build in, forward looking, for the next 75 years, the aging and the demographics, you'd have to take fiscal action in the neighbourhood of one to two percentage points of GDP.

When you're talking about 2015-16, you're talking about a $2 trillion economy. Every point of GDP is roughly $20 billion, and that has to be sustained, sir, to eliminate that fiscal gap. That's a calculation other countries regularly do, and in fact are legislated to do.

Hon. Scott Brison: In your report you also say that the PBO requested details regarding how the government intends to achieve its planned operating budget freeze over the projection period. However, the government has indicated that this information is a cabinet confidence and will not be released to the public.

You're an officer of Parliament. We're parliamentarians, and ultimately, Parliament holds the purse strings of government. That's been the role of Parliament in terms of accountability. Can you explain to this committee why you believe the government is not providing you with the specific information you requested, and as such is not providing Parliament with the information you requested?

Mr. Kevin Page: What we requested were basically five-year plan reference levels for departments, with the appropriate breakdowns—operational, capital, transfers, and so on—so that we could actually improve our expenditure forecasting process.

Also, we wanted that information so that we could kind of undertake an analysis for parliamentarians on whether there is fiscal risk or service-level risk from a sustained operational freeze.

We've asked for the five-year reference levels on a couple of occasions. The operations and estimates committee has also put forward a motion asking for that information so that we can undertake that analysis.

Hon. Scott Brison: Earlier last month, this committee passed four motions requesting that Finance Canada provide us with projected costs for the F-35 fighter jets, the corporate tax cuts, and the Conservatives' crime legislation. Do you believe the department's response to these motions was adequate for us to fully evaluate them?

Mr. Kevin Page: Well, we've been asked to provide financial analysis around the F-35. We're undertaking that analysis. We hope to have a report to parliamentarians before Christmas. In response, I would say that I still think there are a number of questions about the costs, and there is some uncertainty with respect to the F-35.

On the other issues mentioned, such as the report on the G-8 and G-20, we did some work for parliamentarians in advance.

It's true that we have not seen even in the 2010 budget or in the fiscal update what adjustments were actually made in the fiscal framework for those expenditures. I think there's uncertainty. But I think at this point the work is now really over to the Auditor General to kind of look at the receipts. I'm not sure how much more value-added we could provide on that.

On corporate tax rates, we could do some work to look at what the rough costs were. We don't have a great corporate tax model. We could work with Statistics Canada. We've done these sorts of estimates before. We could do crude estimates. I think Finance already put out roughly what those estimates would be, I think in the 2000 statement, when they made the reductions in corporate income tax. So there's some information out there.

What was the fourth one?

● (1615)

The Chair: You have 30 seconds.

Mr. Kevin Page: Oh, yes, it was on the crime bills. I'm sorry, sir.

We're still waiting for information on the crime bills. We had no luck when we did our costing of the Truth in Sentencing Act, in terms of getting information.

Hon. Scott Brison: You had no luck. Do you mean they didn't give you...?

Mr. Kevin Page: We had no information, sir.

Hon. Scott Brison: But you requested information.

Mr. Kevin Page: We did request information. We requested, actually, context so that we could understand how they were doing their costing. We were not able to have—

Hon. Scott Brison: When did you ask for that information?

Mr. Kevin Page: Well, when we did the work on the Truth in Sentencing Act, the work started in the late fall of 2009, and as you know, we tabled the report in June.

Hon. Scott Brison: So you've been waiting since the fall of 2009 for the information on the costing of some of this legislation.

Mr. Kevin Page: Well, sir, on the Truth in Sentencing Act, the old Bill C-25, that is the case. There are a number of other bills. We haven't received any information on the other bills.

The Chair: Okay. Thank you.

Thank you, Mr. Brison.

Monsieur Paillé, *s'il vous plaît*.

[*Translation*]

Mr. Daniel Paillé (Hochelaga, BQ): Thank you, Mr. Chair.

I am a bit uncomfortable discussing the report from Mr. Page and his colleagues, and mixing it with “salespeople” from two chartered banks and the presentation of an individual, because the forecasters have led us into sort of a stratospheric projection, in my opinion. Everyone knows that projections are to forecasters like a lamppost is to a drunk; they provide support, not light.

In the long-term, we will all be dead. Ladies and gentlemen, I also think that the projection I can make is that you are mistaken. In four or five years, we will for sure come back here and say that the figures from TD, Mr. Poschmann or the Scotiabank Group were all wrong. But that's irrelevant here. I would like to come back to Mr. Page because he represents parliamentarians and that's why we are trying to work with him.

You are actually missing information. This is very important to me because you are saying that the government manages its revenue by following its very Conservative fiscal policy and, as a result, is keeping the corporate tax cuts. Economists tell us that it will be profitable in the long term. Of course they do!

Meanwhile, the government shows us—and history tends to repeat itself—its inability to be in control of its expenditures. In addition, it does not give you access to information and that worries me.

You are saying that your assumption of growth has to be 3.2%. That's very brave of you. Not everything is wrong in your comments. There are some interesting things. But I have some questions. Since we are all dipping into the same fiscal pot, that shows us that the fiscal imbalance has never been resolved in Canada. Both levels of government are picking the same taxpayers' pockets. The current risk is in the health agreement the minister wants to resume, saying that, in the next few years, he will base it on the consumer loans index rather than the needs of the workforce. That makes no sense.

Although you have little or no information, don't you get the impression that this government is pushing the snow over to the next-door neighbour, except that the snow will not melt and the provincial governments will be facing huge imbalances that will become unmanageable?

● (1620)

Mr. Kevin Page: In my opinion, we need analyses to examine not only the fiscal sustainability of the federal government but also of the provincial governments.

In our first report on the 2010 fiscal sustainability, we have only examined the federal government. As I said earlier, in our next report, coming out perhaps in February or March, we are determined to examine the government in a consolidated manner, meaning all levels of government.

As Mr. Poschmann said, important issues have to be addressed, including the growth rate in health transfers. In the current fiscal framework, there is a 6% assumption per year; that's a big chunk of our budget, as Mr. Burleton pointed out when we talked about the 2% GDP growth rate.

So we should talk about this. Meanwhile, it is important that our office and, perhaps, the Department of Finance conduct appropriate analyses to examine the fiscal sustainability of all levels of government.

Mr. Daniel Paillé: We represent ridings. So, in terms of the needs of the public, we can say that the growth rate will be two, two and a half, two and three-quarters, two and seven-eighths. The trend is what is important, but it won't be the same everywhere. The economic growth in Alberta won't be the same as in Quebec. So don't you get the impression that it would be a lot better if the government freed some space, handing over tax points and entire taxes? It is not enough if it just gives half or keeps three quarters. It should give the Quebec government and the other provincial governments the means to assume their responsibilities.

Mr. Kevin Page: Yes, I agree; the situation can change. But perhaps the most important thing is having clear analyses to determine the assumptions for the federal and provincial governments. And if it is possible to do the proper analyses on the fiscal sustainability of each province, what are the assumptions?

So, it is not only a question of making a projection; the assumption is really crucial.

Mr. Daniel Paillé: As to statistics, don't you feel that the government or the Department of Finance is trying to prevent you from getting the right data? In the longer term, with the chopped-off census, the data will no longer be reliable.

Mr. Kevin Page: We are concerned about the level of transparency of issues related to operational expenditures and direct program spending. As to the Department of Finance and its officials, I have no doubt that they are quite capable of carrying out the proper analyses.

Mr. Daniel Paillé: Of course. I agree with you, they are good people.

The Chair: Thank you, Mr. Paillé.

Mr. Menzies.

[*English*]

Mr. Ted Menzies (Macleod, CPC): Thank you, Mr. Chair.

Thank you to all of our witnesses.

Thank you again, Mr. Page, for bringing your very capable staff with you. We tend to focus our questions on you, so please share the wealth.

I have a very serious question for you. In your opening statement you say there's an 85% chance of probability that the budget will be in deficit in 2015-16 and an 88% chance the budgetary balance in 2015-16 will be lower than $2.6 billion.

I don't watch a lot of television, but there's one cute ad: what are the chances of me being abducted by aliens?

I'm just kidding, of course, but when you put that down in your opening statement, I thought we had to follow up with that.

My sense is, Mr. Page, that you're very close to what our economic fall update actually was. The only difference would be program spending, our track on program spending to yours. We share your fervour, if you will, to make sure we get back to balanced budgets, and we appreciate that comment. But if your projections adopted the same expense track as ours, we would be quite close. I'd be interested in your comments on that.

The one thing I did want to pick up on is that you're recommending the Department of Finance use its own economic forecast in our budget planning process, rather than using these individuals, the 15 private sector advisors, if you will, that we use. This is what we've done since 1994.

In the last budget there was a spread of $100 billion in projected GDP. We're down to a $50 billion spread. So volatility is very important when we're looking at those kinds of spreads.

This forecasting process—gathering information, if you will—was recommended by Ernst & Young in 1994. O'Neill Strategic Economics reaffirmed the method in 2005, and the method has actually been supported by the IMF. What are your reasons for suggesting this should be done only within the Department of Finance and that we shouldn't be speaking to the experts outside the department?

● (1625)

Mr. Kevin Page: Thank you.

Sir, we don't have a model that we could use to see what the probability is that you would be abducted by aliens.

Voices: Oh, oh!

Mr. Ted Menzies: Can you work on that?

Mr. Kevin Page: I'd like to just pick up seriously on three of the points you made: one on the area of risk, one on the closeness of our projections vis-à-vis the Department of Finance, and the third one around the issue of independent forecasts.

Actually, I think the one that's probably most important is the issue of risk and how we deal with that—putting aside the issue of the model for whether or not we'll be abducted by aliens. It's important to know—and I think Mr. Paillé raised this issue as well—that economists aren't mystics. There was a quote in the paper today from Mr. Galbraith, saying that economists do forecasts not because they know, but because they're asked to.

Mr. Ted Menzies: I think they get paid to. Hopefully they get paid for it too.

Mr. Kevin Page: No, sir, I didn't mean it in that context.

I think why the PBO does these forecasts for you and why we do reconciliations and all the analysis around it is so that you can have a rich planning environment, so that you can debate the policy and priorities, short term, medium term, and long term. That's why we do these forecasts, and there are always doubts.

When we do these fan charts that look at probabilities and distributions—it's something that is being done in different parts of the world, such as in the U.S., in the U.K. now, and central banks do it around inflation—basically what we're doing, sir, is we're looking back. What's been the track record of private sector forecasts on the average forecast? We have sixteen years of information. We have four surveys a year. What's our track record to predict, one, two, three, four, five years out? We want you to know that, sir, because this is part of the richness of the environment you're dealing with. That's just our ability to forecast. We're being honest in that sense.

Then I think you should ask us what our judgment is on the risk. How are you dealing with the issues of a potentially weak U.S. economy? People have talked about that here today. Currency risks—people have talked about that here today in the context of QE2, quantitative easing 2, etc. Issues of sovereign credit risk, issues of household debt.... How are you adjusting that distribution of probability of outcomes? That's all we're doing there. So we're trying to give you a rich environment.

To put a number on where the deficit's going to be in 2015-16, as I think Derek said here today...the difference between $5 billion, $10 billion, or $15 billion in a $2 trillion economy is not really the issue. In putting the point of view, he's debating what should be the policy of priorities.

Again, we don't have a model to predict whether or not we'll be abducted by aliens, but it is important to understand the risk that is out there and our ability to track these things and project forward.

Number two, you're quite right, sir, that there's very little difference between the Finance numbers. If you just look at the budgetary balance, in fact, if you break it out and look at revenues and expenditures over the five-year track, on the revenue side it's negligible. On the spending side you highlighted the big differences in operating spending. There are some differences on public debt charges. But all told, if you add it up over five years, you're probably talking about a little more than $30 billion, cumulative in terms of debt, so it's not a big difference.

Again, for us that's not the most important issue. You want to understand the risks that surround those numbers. We want you to understand whether it is cyclical or whether it is structural. Do we have a fiscal structure that's sustainable? So when we make these points, sir, we need more analysis. It's only in that context that you can debate those issues.

In terms of independent forecasts, I made that comment—somebody asked me the question. This should be the policy. I'm not the Minister of Finance. He has a very tough job. I'm not a deputy. But I think there's a certain rigour—and I think these folks know—when you do an independent forecast. When you break out the economy, what's happening in this quarter or that quarter? You do the medium term. It is helpful to do that. There's something lost when you lose that rigour. We don't want to lose what we do. We work with the average private sector forecast. We want to keep that. It's fine for the Department of Finance, if they wanted to have their own view. I think PBO should have its own view eventually some day, too, in terms of the economy, and come to these sorts of meetings and basically deconstruct that view for you.

● (1630)

The Chair: Thank you, Mr. Menzies.

Mr. Ted Menzies: Thanks, Chair.

[*Translation*]

The Chair: Mr. Mulcair, you have the floor.

Mr. Thomas Mulcair (Outremont, NDP): Thank you very much, Mr. Chair.

I will first go to Ms. Webb since I was taken aback by her earlier comment. She said:

[*English*]

“Our industry has learned to cope with a 95¢ U.S. dollar....”

[*Translation*]

If I may, I would like to read her a quote from Statistics Canada dated August 16, 2007:

> The Canadian economy doesn't have “Dutch Disease”...the Dutch case involved the discovery of a new resource, while Canada's recent trend stems from the integration of emerging nations...

In 2009, just two years later, Statistics Canada did a 180-degree turn. In a document called “Trends in Manufacturing Employment , Statistics Canada said the following:

> ...employment in manufacturing experienced a clear downward trend with successive annual losses of at least 3% from 2005 to 2008.

So, two years later, their analysis was completely different:

> In these four years, more than one in seven manufacturing jobs were lost.
>
> These losses resulted in the rapid erosion of the share of manufacturing jobs in the economy...

We are even told that 322,000 jobs disappeared in Canada during that period.

[*English*]

Is that how our industry learned to cope, by losing 322,000 jobs? Is that your analysis? Is that the Scotiabank's official position on this, that this was coping, losing 322,000 jobs?

Ms. Mary Webb: First of all, it's my opinion, not the Bank of Nova Scotia's.

Mr. Thomas Mulcair: Okay, I'm going to stop you right there. Thank you. If we're listening to your opinion and not the Bank of Nova Scotia's, I'm going straight to Mr. Page.

It's the same thing with Mr. Poschmann. I'm not here to listen to people's personal opinions; I'm here to listen to an institution. If you're not here representing your institution, thank you for your time.

[*Translation*]

Mr. Page, you have already said that the situation we are facing right now is a result of choices made. In previous reports, you said that the government was making choices that would lead to that outcome. You spoke for instance of corporate tax reductions which by definition only benefit the more profitable companies, since a forestry or manufacturing company that was struggling and not turning a profit obviously would not be paying income tax and so could not benefit from a tax reduction.

I would like to hear your point of view on the program expenditures mentioned here in the presentations of some of your colleagues who say that they expect program expenditures to be set at a certain level. Will the government's choice to maintain or not maintain program expenditures have a determining effect on the economy? If so, how do you assess the risks involved?

As far as we are concerned, we think it very likely that the Conservatives, faced with a deficit they have themselves created, will say that the solution is to cut program expenditures radically.

And so, I would like to hear your analysis of the possible results of such a choice, and I would like you to tell us if you think that is a priority for them, since it is our turn to make a forecast.

Mr. Kevin Page: The government did make some choices. It decided to spend on certain programs, just as, for instance, it decided to amend the Criminal Code. Program expenditures are affected by government decisions. These are not decisions, in my opinion, that the Office of the Parliamentary Budget Officer can really examine.

It is important for our office to examine expenditure levels and to see whether they are reasonable, and if there is a risk—the government in fact referred to this—that operational expenditures may be frozen in order to achieve savings. That is not really a matter of choice, to our mind. On the basis of the government's choices, we analyze the figures and the rest is not really our affair.

● (1635)

Mr. Thomas Mulcair: Of course. We have always respected that and I think that you have always shown caution. You do not hazard into the minefield of commenting on political choices, that is certain. You assess for us the probable results of the choices you witness.

Another term that has been used here today is “priority”. So if the priority remains unchanged, certain results are probable. But if the priority becomes to react to an apprehended crisis that they themselves have created...

When you grant $60 billion in total tax reductions to the biggest corporations, and empty the coffers of employment insurance, which then are empty in periods of high unemployment, those are choices. That money was put there by all businesses, both those who were losing money and those who were making some. But since the priority seems to be to provide assistance to the big corporations, the most profitable ones, it is very likely—and it is our job as politicians to point this out—that the choice will be an across-the-board reduction of program expenditures, just as they granted “wall to wall” tax reductions to the most profitable companies without making job creation a priority, nor productivity. It is predictable that we are going to see “wall to wall” cuts. They don't want to know, managing this doesn't interest them.

And so I would like to know what you think, without inviting you to comment on these choices; what is the probable consequence of “wall to wall” cuts in program expenditures? The government is going to try to present this as something positive: we are reducing expenditures. But what are the possible negative impacts of such a choice on society, in your opinion?

Mr. Kevin Page: Our office has the opportunity to examine fiscal risk issues, as well as risks relating to services provided to the population. However, we need certain pieces of information to calculate these levels of risk. As I said, we don't have the necessary information to examine fiscal risk issues, the level of risk to services and the consequences for Canadians.

Mr. Thomas Mulcair: Mr. Chairman, I am going to conclude by thanking Mr. Page again for his balanced analysis, which always helps us tremendously.

Like my colleague Mr. Paillé, I am very sorry to hear once again that Mr. Page does not have all the information he needs, as he represents an institution that was of course created to assist parliamentarians but also, through us, to benefit the Canadian public. The fact that his work is always limited by the refusal to provide him with information he is entitled to have prevents us from doing our work, but more crucially, prevents the population from having access to essential information.

I thank you once again, Mr. Page, you are an extraordinary public servant.

[*English*]

The Chair: It's been raised by a couple of colleagues, and I just want to clarify for colleagues the exact motion that was unanimously agreed to.

On the motion of Massimo Pacetti, it was agreed:

> That the Committee invite Kevin Page, Parliamentary Budget Officer, and private sector economists to appear before the committee on Wednesday, November 3, 2010, for 2 hours to discuss the government's most recent economic update / fiscal projections and any other item related to the government's fiscal framework or their own revenue and expenditure projections.

I think we should always endeavour to treat all of our guests and colleagues with respect. I would say that the chair did invite people to be here today. The clerk obviously contacted people, and I don't think we had any suggestions from members as to private sector economists.

But in the future, if the committee wishes to have Mr. Page separately, please indicate that to the chair and that is exactly what the chair will do. Then the chair will have a panel with Mr. Page and a panel with the private sector economists.

I was simply, as the chair, fulfilling the wish of the motion as introduced by Mr. Pacetti and agreed to by this committee. I'd just like to point that out to members.

Mr. Mulcair, on a point of order.

Mr. Thomas Mulcair: I want to make it clear, Mr. Chair, that we have no trouble listening to people who come representing institutions and giving us the view of those institutions. There's a big difference for us, however, if I'm going to be talking to someone as a private individual or someone representing an institution.

When you present them to us as representing an institution and then the first thing we're told is they are representing no institution, and we're given their names...I just prefer to stick with the person who is here representing an institution, and that's Mr. Page.

No lack of respect meant and none intended. If there was any, my profoundest apologies to you, Mr. Chair, and to the committee.

● (1640)

The Chair: Thank you for raising that. I appreciate that.

But my understanding is, and I can be corrected, Ms. Webb does represent Scotiabank Group and my understanding is Mr. Burleton does represent TD Bank Financial Group.

Am I correct in that assumption?

Mr. Thomas Mulcair: She said just the opposite when I asked her a question. She said she was speaking privately and her views don't represent those of Scotiabank.

The Chair: Ms. Webb, can you just clarify for us?

Ms. Mary Webb: I spoke out of turn, I suppose.

When I made the comment about the 95¢ dollar, I was making reference to the fact that initially back 15 years ago, when we were talking about a dollar going to 90¢ or 92¢, there were studies that indicated that things like our motor vehicle parts could not cope with a dollar that was much over 85¢ to 86¢, and that 88¢ would be impossible. There's absolutely no question that our manufacturing sector has been hard hit and the dollar has hurt them. But it has found efficiencies and marketing niches that allow it to do that.

It's something that I've written about, and the restructuring of Ontario. So it has been my research. You are right, I do that research for Scotiabank. I probably shouldn't have replied as abruptly as I did that it was my research, but it was. But I do represent Scotiabank.

The Chair: Thank you. Thank you all.

We will now go to Mr. Szabo.

Mr. Paul Szabo (Mississauga South, Lib.): Thank you.

Mr. Page, you made some commentary on the status of the economic stimulus plan and suggested that there was a risk that a large percentage of these may not be completed by March 2011.

Do you have an update on your opinion with regard to that? Can you give us an idea of the impacts, in the worst possible case, in terms of employment numbers as well as GDP?

Mr. Kevin Page: Maybe I'll start and then ask Mr. Sahir Khan to add to my comments.

As I've noted, we will be releasing in a few weeks a study that looks at the stimulus overall from the macro-economic impact. It will also include our survey of municipalities that have received money as a result of the infrastructure stimulus fund program. It will look at output jobs and the effectiveness of program delivery. That study should be available to parliamentarians in a few weeks' time.

We've also received data, which is now a little bit aged, from Infrastructure Canada with respect to the infrastructure stimulus fund program. This is progress report data as of June 30. So we will update our estimates, sir, in terms of the number of projects that may be at risk. But again, the data is quite old and we will be preparing a study.

I will ask Mr. Khan just to update you on where that work is at.

Mr. Sahir Khan (Assistant Parliamentary Budget Officer, Expenditure and Revenue Analysis, Office of the Parliamentary Budget Officer, Library of Parliament): We're actually trying to get the report out. Usually, once we receive it from the department, we're able to produce it in about 10 days.

Mr. Paul Szabo: Okay, fair enough.

The recovery of jobs was disproportionately part-time from what we've reported so far. Does that give you any indication, or do you use that, to make some sort of an assessment of the strength of the recovery on the corporate sector?

Mr. Kevin Page: Both the corporate sector and overall.... In the announcements we have in our chart today, it talks about the total economy and it talks about total hours, average weekly hours. We have some charts that show where we're at vis-à-vis the peak in the fall of 2008 and where we would be relative to the trend.

Basically, when you look at hours, you get a sense that we're well below trend. We're well below that peak. We're still a good two percentage points below in terms of total hours. That means the labour input that's going in to maintain a strong economy right now is still relatively weak. What's behind that as well is that it supports our analysis to say that when we look at the private sector forecast, and we look at our estimates of potential output, we're talking about an output gap of probably, right now, even today, as of the second quarter, 2.9%, almost 3%, below potential, not closing until 2016. So when members here are thinking about what should be the appropriate policy actions in the budget, they should be thinking about an economy that's operating well below capacity now, closing very gradually.

Mr. Paul Szabo: Our economy is inextricably linked to the United States and everybody says there are very serious problems. What is going to happen? If we have a stronger dollar, at parity and maybe beyond parity, mostly resource-driven because of the resource part of the economy, at what point in time, over what period of time, will that begin to impact the manufacturing sector that is suffering from a higher dollar?

Mr. Kevin Page: Maybe this picks up on the point that Mr. Mulcair was making. We've seen, even in recent years, what an impact a high dollar can have on the manufacturing sector's output and net exports from the point of view of growth. It almost happens on a simultaneous basis, where you can see that movement in the U. S. economy has an impact almost simultaneously in the Canadian economy. So as we see the weakness, it's felt fairly quickly. When we saw the start of the strong appreciation of the Canadian dollar in 2007, we saw a significant weakness in our manufacturing sector.

● (1645)

Mr. Paul Szabo: Okay. To be very brief, looking out to 2015, everybody says things can change—volatility—but in the next fiscal year everybody agrees it will be a lower GDP growth, from the government's economic update.

The minister said in question period today that the plan is in the economic update. Do you understand what the government's plan is, to get their numbers, and why the GDP growth rates are so much lower in your estimates?

The Chair: You have 30 seconds.

Mr. Kevin Page: I don't know if the government has a plan actually to target a growth rate for the Canadian economy. You're right, I think the average private sector forecast shows growth of 3% this year in real GDP terms, falling to 2.5% next year. I think they have a plan, so to speak, in terms of reducing the deficit. I don't know if they have a plan to ensure that we hit a growth target next year precisely of something like 2.5%.

The Chair: Thank you.

[*Translation*]

Mr. Carrier, you have the floor.

Mr. Robert Carrier (Alfred-Pellan, BQ): Thank you.

Good afternoon, ladies and gentlemen. I'm going to be addressing my questions to Mr. Page, whom I am happy to see here again.

You are the reliable financial conscience of the government. And so it is important for us to hear your comments and to be able to obtain answers to our questions.

What interests me—my colleague raised this matter a little earlier — is that your next report take into account not only the viewpoint of the federal government, but also that of all the provincial governments.

Personally, I think that that is a good way to try to clarify some of the uncoordinated actions taken by the central government. Let us take for example the tax harmonization that has been granted to certain provinces but has not yet been settled for Quebec, although many think that that tax has been harmonized. I think that that is what Mr. Burleton was saying earlier. We see some individual dealings by a central government.

I'm thinking of revenue from Hydro-Québec that is not treated in the same way as revenue from Hydro One in Ontario. In Ontario, that income is not considered government revenue, contrary to the situation in Quebec. Consequently, that influences the equalization payment and the famous formula used to calculate it.

Will the approach you are proposing help to harmonize the government's actions? Would you be able to target particular approaches that are not recommendable and to suggest, rather, that there be federal policies that apply to the country as a whole?

Mr. Kevin Page: In our next report, which will be discussing the fiscal viability of federal and provincial governments, we are going to examine the tax structure of the federal government and we will be positing the hypothesis that provincial governments want to maintain that structure. We are doing calculations, we are taking into account the aging of the population and preparing hypotheses on the productivity of all of the provinces. We are calculating the tax gap for the federal government and doing other calculations for the provincial governments. We are attempting to determine whether it is possible to examine each province separately, for instance Quebec, Ontario, British Columbia, etc.

We will see what the situation is according to the results of our analysis. It is difficult to say for the moment whether that will really be possible. In my opinion, it is really important to perform such calculations, to ensure that all parliamentarians have the information and can conduct a proper debate on health and social transfer payments.

Mr. Robert Carrier: Have you ever asked the provinces whether they were interested in providing information to you? They might do a better job of that than the federal government.

● (1650)

Mr. Kevin Page: No, but as I was saying, we are performing calculations concerning the federal government. We published a study which we are going to release this year. For our team that is here today, it is difficult to do everything at once. Our purpose today is to improve the tools that allow us to assess risk and fiscal forecasts. Our next big project will be to examine fiscal viability. We are going to start tomorrow.

Mr. Robert Carrier: If I understand correctly, you have not yet asked the provinces whether they want to cooperate in the studies you are going to undertake.

Mr. Kevin Page: We are examining the type of study we need to do for all of the provinces. The fiscal viability of the provinces does not really involve a lot of calculations. In my opinion, our project is very important.

Chris may have something to add. No? Fine.

Mr. Robert Carrier: As I mentioned earlier, I hope that your work is going to bring out the inequality of the federal government's treatment of some provinces. Is that an aspect that your report is going to be touching on?

Mr. Kevin Page: Yes, but we are going to have to work with all of the experts and certainly with those from Quebec.

The Chair: Very well. Thank you.

Thank you, Mr. Carrier.

[*English*]

Mr. Wallace please, for five minutes.

Mr. Mike Wallace (Burlington, CPC): Thank you, Mr. Chairman.

I want to thank our guests for joining us this afternoon.

Mr. Page, Mr. Brison was shaking his head at everything you were saying, and I think one of the things you were saying is that we have to look at our fiscal outlook and, if we really want to get back to a balanced budget, look at cutting things. I'm looking forward to seeing what the Liberal Party brings forward in this budget process on what we're going to be cutting. I think he was, in cabinet, defending the Liberal spending scandal in the House, and I'm sure he understands the issue of cabinet confidence that you mentioned you're running into a bit of a problem with.

I have one question for you, and then I'm going to our economists who are here. I agree with you that we do have to be pretty tough going forward and we have to look at things. I'm assuming that the leadership from the budget office will be that if we're going to be making cuts to programs and so on, your office is going to be offering a reduction also, in this upcoming budget, that we can take advantage of.

Mr. Kevin Page: Sir, I've spent a whole year fighting to get my budget back. It took me two years to get my HR plan approved.

Mr. Mike Wallace: So “no” is the answer to that?

Mr. Kevin Page: If you're dissatisfied with the productivity of the PBO—

Mr. Mike Wallace: I'm not dissatisfied with anybody's productivity across the public service, but I think everyone has to pay a bit of the price and take on a bit of the burden. That's my only point.

Mr. Kevin Page: Our budget is frozen at 2.8%.

Mr. Mike Wallace: Yes, frozen, but that doesn't mean it can't go in the other direction.

That's not a threat; that's the reality.

I have two questions, and one is for my friends from the banks. You talked about household debt being a problem. My question is twofold: one, what can the federal government do to try to improve the household debt issue, from a policy perspective; and two, are the banks not responsible a bit for that? Most people, from a personal point of view, get their money from either the bank or a credit card, and I think you're involved in both. I'd be happy to have an answer on either.

Then for Mr. Poschmann, when we get a chance—hopefully we get a chance—on the personal tax rates that you talked about, is there a better way of changing that? Is it threshold changes or is it percentage changes? Or do you have an opinion?

Those are my questions.

The Chair: You have two and a half minutes left.

Mr. Burleton.

Mr. Derek Burleton: Yes, maybe I'll start.

We put out a report on household indebtedness a couple of weeks ago, and it was a fairly in-depth study. I've been shocked at the dearth of research in the area, so we undertook the study, and I think it's quite good, but perhaps I'm a bit biased.

There's a lot of focus on the debt-to-income ratio. I think whenever we look at an average statistic, we always have to ask ourselves if we are getting the full story. So the study does go into a fair amount of detail, looking at assets, debt to assets, debt to net worth, looking at a lot of the different things—debt serviceability. We look at some of the same things the Bank of Canada does.

The bottom line is that, in our view, we're not at crisis levels yet. I believe there are a lot of reasons to think that we're not in a U.S.-style predicament. We didn't get into the same risky lending during the run-up in the housing market. That said, no doubt a lot of Canadians have taken advantage of extremely low interest rates, and I don't think a lot of Canadians have factored in this notion that interest rates at some time will return to more normal levels.

So a lot of the report is more forward looking.

Under these interest rate assumptions, what kind of debt are we looking at? Frankly, I'm very concerned that mortgage rates are at historical lows and that in fact the borrowing could continue, even though we've—

● (1655)

Mr. Mike Wallace: Is there a policy that the federal government could do to start addressing that issue? The answer could be no, but I need the answer.

Mr. Derek Burleton: Well, I had to provide a bit of context there.

Mr. Mike Wallace: Well, I love your context, but I only have 10 seconds.

Mr. Derek Burleton: Okay. Anyway I was just getting to the punch line.

Right now, I think we have to be a bit careful implementing anything federally, partly because the housing market is slowing. If things do pick up, then things should be looked at. Obviously, looking at the mortgage rules is one thing—CMHC and the other mortgage insurers and the kind of mortgage rules. But I agree with you, the banks do have a responsibility. Generally, we need to dig deeper and understand the implications of these lines of credit. And I think there's an onus on the banks as well to look at whether it is a first-time buyer issue, that generally first-time buyers do use mortgage insurance, or is it tied to the lines of credit? From a bank perspective, I think there's an onus on us to dig deeper into the information and look and see.

The Chair: We're going to have to come back to the other questions in a subsequent round, unfortunately.

Mr. Pacetti, please, for five minutes.

Mr. Massimo Pacetti (Saint-Léonard—Saint-Michel, Lib.): Thank you, Mr. Chair. Thank you to the witnesses for coming.

Mr. Page, I have a quick question. I've been on this committee for the last six or seven years. I used to chair it. We used to have independent forecasters come forward, and we always had a problem in terms of getting estimates. If I can ask you a question in terms of simplifying it, or explaining your job exactly, what do you do that's different from the economic forecasters? Everybody seems to take the forecasting growth, they take a percentage of what we think that's going to be, they take a percentage of the government revenues, and we decide that government revenues are going to go up by that percentage, and that's it, the work is done, because we can't get any information on what's going to be spent. And even when we do have budgets, the budgets are not respected. But with the Liberal governments, at least, it wasn't respected and we actually underspent. With this government, they seem to be overspending, so we have the same type of problem going the opposite way.

My first question is, what is in your job, as the independent Parliamentary Budget Officer, that would be different from the economic forecasters to your right?

Mr. Kevin Page: Thank you for the question.

Our job is actually quite different. Our job resembles much more what the Department of Finance does. In fact, most of our panel here have spent many years at the Department of Finance.

What we do—and what we have been doing over the past couple of years—is start with the average private sector forecast. We take the survey from the Department of Finance and then we translate that, using models, into a fiscal forecast. We break down the revenue by the major revenue components, and we do the same for spending.

Mr. Massimo Pacetti: So the revenues, pretty well, are similar. It doesn't matter who would calculate it, whether it be economic forecasters, Finance, or anybody. It's all proportional, depending on what your growth would be. Is that correct?

Mr. Kevin Page: Well, it's important when you talk about the—

Mr. Massimo Pacetti: I'm simplifying it here.

Mr. Kevin Page: Yes. It's important to do reconciliations. What is the difference between our numbers, for example, and what is different in the Department of Finance's numbers is important—to have a sense of what those projected income shares are for the economy. What does personal income look like at the Department of Finance in its five-year projections? What does its corporate income tax look like, etc.? Then we can reconcile our numbers. But our models are actually quite similar. What we lack is the grittiness, the level of detail, particularly on the program spending side. That's where we've been pushing.

Mr. Massimo Pacetti: In the last six months, where have you not got any information in particular?

Mr. Kevin Page: I think there are two parts to the answer to that. One part is when we do our economic and fiscal projections. We've tried to get from the Department of Finance those income shares and they're—

Mr. Massimo Pacetti: That has nothing to do with policy or cabinet secrecy, correct?

Mr. Kevin Page: No. As we've said on numerous occasions, we believe that has been shared with the private sector forecasters in the past when there was a different type of relationship in doing fiscal projections. More recently we've struggled with the issue. We've been working with the committee of operations and estimates on the program spending five-year outlook requirements.

● (1700)

Mr. Massimo Pacetti: Those are all programs that have been announced.

Mr. Kevin Page: Yes. Money has been approved through the budgets. There's always a question of in-year spending with the estimates. What we really want are those five-year approved reference levels for departments broken out.

On the other side of the question there are issues of policy costing. In our small shop we've done big policy costing on Afghanistan, aboriginal educational infrastructure, and the Truth in Sentencing Act.

Mr. Massimo Pacetti: We're going through our pre-budget consultations. Witnesses are coming forward who are able to cost our proposals. Finance seems to have a hard time costing certain proposals, so there seems to be an inconsistency there.

I understand your frustration in getting information. The committee has also tried in the past to get estimates from Finance before we propose a recommendation, and we get crazy estimates. We even get crazy estimates on some of the private members' bills we've come up with, as far as the variances.

In your third paragraph you say there are also structural problems, such as low productivity, aging demographics, and fiscal imbalances. Mr. Burleton was talking about household debt. Is that what you're talking about?

Mr. Kevin Page: No. Mr. Burleton will probably want to add on the issue of household debt and how that might impair economic growth going forward. But we were referring to structural deficit. So when we look at the fiscal imbalances, like other countries we break out what is cyclical and what is structural. If you have a structural issue, that means you'll be running deficits even when the economy gets back to potential. We're saying it's not going to get back to potential until 2016.

Mr. Massimo Pacetti: So that would be part of your fiscal imbalance?

Mr. Kevin Page: Right.

The Chair: Thank you, Mr. Pacetti.

We'll go to Ms. Brown, please.

Ms. Lois Brown (Newmarket—Aurora, CPC): Thank you, Mr. Chair.

Thank you very much for your presentations today.

I'm a visitor to this committee, so thank you for allowing me to speak.

Contrary to other people on this committee, I am very interested in hearing from our economists.

Mr. Poschmann, my question goes first to you. But maybe our banks can also comment, because they are probably providing credit.

I was reading the public accounts books that were released the other day. Some people say I should get a life, but as a person who has studied economics, I have an interest in them.

What was notable to me in the first few pages was a pie chart showing that government receives 47% of its income from income tax and 13% from corporate income tax. We're talking about lowering corporate income tax to create more jobs in our economy—to create well-paying jobs in our economy. What impact will that have on income tax generation for the government? What will happen if we don't make those corporate tax cuts? Tim Hortons recently returned to Canada because of corporate tax reductions. What allure will this have for other companies to invest here?

Mr. Finn Poschmann: If I may, I'd like to take that question, Mr. Chairman.

Thank you for the question, Honourable Member.

I work for a non-partisan, non-profit public policy research shop, and accordingly we publish on a wide range of issues, sometimes publishing opposing views by scholars who write for us. Last week, for instance, we published a two-part report, one part of which said the Bank of Canada should publish its forecast of the interest rate, looking out a few years. The other part explained that the Bank of Canada should not publish its forecast interest rate, looking down a few years. There are valid views on both sides of that issue. There usually are on economic issues.

On the question of tax rates, though, the work published by the institute, including my own, has been pretty consistent, in that creating a low-tax environment—one that's favourable for investment, favourable for growth, favourable for attracting jobs—is necessarily going to produce a good outcome for Canadians of all incomes. That's what a low-rate tax system is all about: having the base as broad as you can have it, having it as simple as you can have it, and taxing different businesses across sectors in very similar ways.

Likewise, if you're looking at how one might treat personal income taxes, right now, because we income-test family benefits based on family income levels, families can face fairly high effective tax rates quite low on the income scale. In other words, they might have incomes that are between $40,000 and $70,000 a year as a family. If they have children, they're going to be losing their benefits over that range, and that can expose them to fairly high effective tax rates. Those are problems for households, and we think it's generally wrong that when families go out and earn an extra dollar of income, they're sharply penalized through loss of benefits for earning that income. That's a question of what's good for incomes, what's good for families, and likewise what's good for growth.

So we've been pretty consistent in saying that a low tax rate is something that's good for investment, good for businesses, and good for households.

● (1705)

Ms. Lois Brown: Mr. Burleton.

The Chair: You have about one minute, Mr. Burleton.

Mr. Derek Burleton: Certainly, we're supportive of creating a tax advantage in this country, I think. One of the challenges Canada has is it's a smaller market than the United States and a lot of other big countries around the world. To the extent that we can create an improved environment, it's certainly going to help deal with some of this productivity challenge down the road. Obviously, as economists, we've moved away from this notion that just getting the debt down and getting taxes down does everything. But the cost of investment is still a very important element.

With the moves in place, both federally and provincially over the next couple of years, we're going to do just that. Our marginal effective tax rates on investment will be about half that, on average, in the United States, and that's a pretty attractive lure, particularly with a high Canadian dollar. In our forecast, the Canadian dollar does go up higher, so that's going to be an added impediment.

Thank you.

The Chair: Thank you.

We'll go to Mr. Pacetti, please.

Mr. Massimo Pacetti: Thank you, Mr. Chair.

Mr. Page, just to continue with what you were saying with your fiscal imbalances, I think you were answering a question and you said there's risk associated with some of these items, or they're cyclical and structural.

Mr. Kevin Page: They're structural in nature. As members of the panel talked about here today, Canada's productivity performance has been very weak in the past 10 years: multi-factor productivity, negative; labour productivity, very weak growth in the past 10 years on an annual basis. We mentioned in that list as well aging demographics; it's structural in nature. The working-age population right now is growing at a little over 1% per year, and over the next 15 years it'll drop to less than half. That's going to have a huge impact on labour input in this country and potential output on revenues, even on spending pressures, as we get older.

Then there's the issue, sir, of fiscal imbalance. We say we have a small structural deficit in this country right now, about 1% declining to half a percentage point over the next five years. It's small in the sense of what we experienced in the late 1990s, early 1980s, which was upwards of five or six percentage points in terms of structural deficit; small compared to what other countries are experiencing right now. But structural deficit, as you look long term, will actually grow due to aging demographics.

Mr. Massimo Pacetti: How do we factor that into the government numbers? Is that based on revenue coming down, or is there some type of contingency required in our expenses?

Mr. Kevin Page: When you look at the fiscal balance track, whether you look at the PBO numbers or the government's numbers, you could take the balance track in our case, sir—you were talking about a $40 billion deficit estimate for 2010-11 falling to $11 billion in 2015-16. We can break out what we think is deemed to be cyclical and what is deemed to be structural. What we're saying, roughly, is we're in the neighbourhood right now—

Mr. Massimo Pacetti: Who can break that out?

Mr. Kevin Page: We do the analysis, sir, and we know the Department of Finance analyses because we all worked for many years at the Department of Finance.

Mr. Massimo Pacetti: But you can't tell where their breakdown is versus your breakdown.

Mr. Kevin Page: Well, sir, they're not providing estimates right now on what's cyclical and what's structural. They're not providing calculations on fiscal sustainability, and we think they could do that.

Mr. Massimo Pacetti: Mr. Burleton, could I ask you quickly, when you have your numbers on your sheet here, $45 billion for 2010-11, are you separating between structural and cyclical?

Mr. Derek Burleton: Yes, we're taking into account both structural and cyclical components. The cycle—

Mr. Massimo Pacetti: Do you make public your—

Mr. Derek Burleton: No, we haven't broken it down in this analysis. In the near term the cycle dominates, but stretching out, say, beyond 2013-14, the structural influences are more important.

Mr. Massimo Pacetti: Okay, and that's what you were talking about as well with the household debt—

Mr. Derek Burleton: Yes, in our view, the household debt is consistent with only very modest consumer spending growth, and we have that factored into our more—

● (1710)

Mr. Massimo Pacetti: In demographics and everything, and that would be in your structural estimates. But would that be made public when you actually publicize your calculations?

Mr. Derek Burleton: Our view on structural growth, sort of five to ten years out, is something around 2%, and consumer spending would be about 2%.

Mr. Massimo Pacetti: Finance should be able to make those available to the Parliamentary Budget Officer, in your opinion. Is that correct—

Mr. Derek Burleton: I've always thought more information—

Mr. Massimo Pacetti: —unless they have something to hide?

Okay.

Mr. Page, again in your opening statement you said Canadian economic activity still remains well below its level of capacity. How did you come up with a statement like that? Who decides what "below" is? How do you compare it?

Mr. Kevin Page: The Department of Finance does produce estimates of Canada's potential output level and its growth rate. They do it historically. They are not publishing this information on a projected basis. We published a paper early this year, led by Mostafa Askari and Chris Matier, that shows how we calculate potential output, what are our assumptions. From that we calculate, just to link to the other conversation, what is the output gap. We use the private sector forecast to see where the economy is projected to be vis-à-vis this potential. We estimate what that output gap is.

Mr. Massimo Pacetti: Which report would that be in?

Mr. Kevin Page: All the reports are available on our website.

Mr. Massimo Pacetti: No, but the one with below its level of full capacity. I don't remember seeing that one.

Mr. Kevin Page: We could probably find out before the end of the meeting, sir, and we'll tell you which specific report, which month it was published. It would be an April timeframe.

Mr. Massimo Pacetti: Is it comparable to what other countries are doing?

Mr. Kevin Page: Yes, most countries, and even the Department of Finance, but they do it on a historical basis to calculate these estimates for their countries.

Mr. Massimo Pacetti: That's it.

The Chair: Thank you, Mr. Pacetti.

I'll go to Mr. Généreux, but I'm going to take a Conservative round. I'm going to allow Ms. Webb to answer.

Every time we go down the line you're always cut off, so I'll give you about 30 seconds to let you respond.

Ms. Mary Webb: Thank you very much.

My reference to the households was not in terms of this being a situation anywhere akin to what's happened to the U.S. Our whole banking and mortgage system is entirely different and has a much more solid underpinning. It was more that as we look out over the next five years, why would our growth be in the 2% range and not 2.5% to 3%? It would be much better, as governments try to balance their books, if it were at 3% and if we were closing the output gap more quickly.

The answer is that with the surge in consumer borrowing immediately after the recession, they've used up some of the spending room that might have otherwise been available down the road. This is important for your committee, simply because as we look forward, we're relying an awful lot on export growth and business investment to power the economy in terms of private sector demand and as the public sector pulls back.

The Chair: Thank you.

[*Translation*]

Mr. Généreux, you have four minutes.

Mr. Bernard Généreux (Montmagny—L'Islet—Kamouraska—Rivière-du-Loup, CPC): Thank you, Mr. Chairman.

Welcome to all of you. My question is for Ms. Webb.

According to what I understood earlier, you have studied certain issues that are of interest to me. Canada is an important exporting country. I'd like to hear what you have to say about the parity of the Canadian dollar with the American dollar and the hypothesis that we might see the Canadian dollar go higher than the American dollar. You stated earlier that you had done a study in 1997 in which it was said that Canada would not be able to function with a dollar whose value climbed from 67¢ to 88¢. What is your opinion on that? I am giving you all of my time to allow you to answer that question.

[*English*]

Ms. Mary Webb: Initially, back when the dollar started to climb, 90¢ was considered very high. A number of our industries made different representations about how difficult it would be to compete with a dollar that was over 85¢. In this particular instance, our work in Scotia economics was focused on the motor vehicle sector and its representations.

Going forward, what the dollar is also doing is a constant skim on the profit that's available, because so many of our contracts are denominated in U.S. dollars. Even outside the manufacturing sector, the dollar has a very significant impact, because if the product is denominated in U.S. dollars, of course you are receiving less.

There's a concern across all industries that as we move through parity, it's another threshold. I think Canadian business has proven to be resilient, but it is tough to be resilient in a global situation where we already have overcapacity in many industries.

● (1715)

[*Translation*]

Mr. Bernard Généreux: What exchange rate would be completely unacceptable if the Canadian dollar reaches parity with the American dollar, or perhaps goes even higher? Is there a ceiling that would be unacceptable, that businesses could not deal with?

[*English*]

Ms. Mary Webb: That's an extremely interesting question, one that we should deal with. We have not dealt with it, and it would obviously vary by industry.

[*Translation*]

Mr. Bernard Généreux: Thank you very much.

The Chair: You have two minutes left.

[*English*]

Mr. Hiebert, if you have a question, you have two and a half minutes.

Mr. Russ Hiebert (South Surrey—White Rock—Cloverdale, CPC): Thank you.

I think it was Mr. Poschmann who said that with every 1% reduction in corporate tax rates, there's actually an increase in government revenue. Did I hear you correctly?

Mr. Finn Poschmann: The correct way to put it, Mr. Chairman and honourable members, is on a present value basis the federal government's net revenue is positive, given where the tax rate is right now, if we bring it down one percentage point. It's just a long-term assessment.

Mr. Russ Hiebert: You said “long-term”. What timeframe are we talking about here, if we reduced with the plan we have right now, with the reduction to 15% by 2012?

Mr. Finn Poschmann: If you look at the responsiveness of investment to tax rates, a reasonable timeframe to expect, given where we are and a reduction to come somewhere near to paying itself, would be in the four- to ten-year framework.

Mr. Russ Hiebert: Four to ten years. Okay. So outside the timeframe that we're looking at right now?

Mr. Finn Poschmann: Arguably. It depends on the investment response and other things that are going on in the economy. For instance, we have a lot of businesses right now sitting on fairly large treasuries. In other words, businesses have been holding back on investment for the last couple of years. Banks are sitting on a lot of reserve capital owing to the fact that they've had to build up their capital stock in the last couple of years. So there are reasons to imagine that in fact there might be quite quick investment responses, but there are a lot of things at play here.

Mr. Russ Hiebert: Okay.

I wasn't sure who said it, but somebody suggested that we apply the U.K. principles of equity reform, a strong base for the long term. Who was it?

It was you, Ms. Webb? Okay.

Could you elaborate on the application of those principles to the Canadian context? How would you see that happening?

Ms. Mary Webb: The initial reason I brought it up is that the U. K. is facing such severe austerity and yet they've made the conscious decision that for some capital projects, some of their science and research budgets, they would protect those simply because they have to maintain a longer-term growth base.

I think that's really important to consider in terms of Canada's situation. We do have more flexibility than many other developed nations right now, and therefore it's extremely important to look at the budget paths we want to take while still increasing our productive capital, whether it's physical or human capital or new technological expertise.

The Chair: Thank you.

Thank you, Mr. Hiebert.

Monsieur Mulcair.

[*Translation*]

Mr. Thomas Mulcair: Thank you, Mr. Chairman.

I would like to go back to Mr. Burleton to ask him whether, following his analyses, he believes that because of the amount of money that has been printed, once the velocity of that money starts to increase... As he said so well, currently we are not in a situation where there is such an acceleration. We have printed... you used the expression that is used in Great Britain, “quantitative easing”. Réal Caouette used to call that “printing money”.

According to the TD Bank Financial Group, once that money starts to circulate in the economy more quickly, is there a danger that inflation might go higher than the 2% target, for instance, if that acceleration begins in the United States, where trillions of dollars were printed?

[*English*]

Mr. Derek Burleton: Mr. Chair, I am concerned about what's going on in the United States. This is very uncharted territory, and I'm concerned about inflation in the medium term. In Canada, less so, because we have inflation and targeting, and we didn't get into quantitative easing. I say less so, but what happens in the U.S. bond market, for example, does tend to have an impact up here. We are very much integrated.

It is something that as a medium-term risk I would put right up there with a lot of other things. It's a concern.

● (1720)

[*Translation*]

Mr. Thomas Mulcair: Ms. Webb, after the Vietnam war, the only way of reimbursing that debt that had become too unwieldy was to resort to inflation. Once the value of currency changes, reimbursement takes place more quickly, but the value is changing.

Will there be any other way to reimburse these thousands of billion dollars—trillions in English, billions in French—than through high inflation? I have met several economists who are afraid of that. However, whenever we meet with Mr. Carney, he tries to be reassuring.

As your colleague from the TD bank pointed out, our economy is intimately linked to the American market whether we like it or not. Do you have any fears concerning medium-term inflation, like Mr. Burleton?

[*English*]

Ms. Mary Webb: My sentiments echo Mr. Burleton's. In the U.S. right now, there's also an issue of the velocity of money. It's actually fallen so low that as they've put more money into the system, it doesn't seem to have much impact. It's almost like the “pushing on a string” type of analogy.

Then there's the concern that once you do get the velocity, and that assumes a number of financial institutional changes, as well as consumer and business sentiment, then all of a sudden you could have a jump in that velocity. That's when it becomes an issue.

But the U.S. Federal Reserve has published a number of good papers that have indicated when they see the pre-signs of that happening, they can drain the money quickly. One appreciates their arguments. Again, we are in uncharted territory, so whether they can actually respond quickly and substantively enough remains an issue. Our situation in Canada is so different that I don't see it, except in terms of Canada's tight linkages to the U.S.

In terms of a strategy to deal with debt, high inflation is very punitive for those on fixed incomes—all the reasons we've tried to stay to the 2% target. I think the Bank of Canada has been very clear on that.

[*Translation*]

Mr. Thomas Mulcair: There's also another way of looking at things, Mr. Chairman. Some people have no fixed assets. At least homeowners will see the value of their property increase. But tenants will only see their rents increase, without having any assets that will increase in value.

Mr. Page, would you be so kind as to share your opinion on that?

[*English*]

Mr. Kevin Page: I would echo what's already been said. My reading of what Mr. Bernanke, the Federal Reserve chairman, is doing in the United States—and his concerns are primarily unemployment and deflation—is that it's very much focused on the short term. I think you could probably also see that equity prices have responded to his basic.... We've seen some bolster in equity prices recently connected to his statement that they're going to put more money into the system.

I think there is a concern, though, that as you take on this quantitative easing you add so much extra liquidity in the system. Where is it going to go? Is it going to stay in the United States? Is it going to go to the higher interest rates? We've seen interest rates rise in India and Australia very recently. You've got all these carry trades going on.

Is the money going to actually stay there to have an impact on asset prices in the States? It's hard to say. But I'm sure central bankers are worried everywhere in the world. When you keep these interest rates as low as they are right now, you're going to face bubbles down the road. They must be worried about that.

[*Translation*]

Mr. Thomas Mulcair: Thank you very much.

Thank you, Mr. Chairman.

[*English*]

The Chair: Thank you. *Merci*.

We'll now go to Mr. Szabo, please.

Mr. Paul Szabo: Mr. Page, if the federal government downloads dollars to the provinces, how would that impact the federal situation? Would it be a dollar-for-dollar benefit to the government in terms of dealing with its structural deficit?

Mr. Kevin Page: Basically, we reduce our federal transfers from where they are right now so the expenditure burden or the federalism imbalance is shifted towards the provinces.

On a federal basis, I think we would be reducing our structural imbalance, and we would be increasing on the provincial basis, which raises the point of why it's so important to look at this from a consolidated point of view.

Mr. Paul Szabo: Exactly.

What have you assumed with regard to the new health accord?

Mr. Kevin Page: For the medium term, we've taken the government's assumptions beyond 2014. There's the 6% growth rate for the Canada health transfer and the 3% growth rate for the Canada social transfer—equalization. We've basically taken the government's numbers. But when we do our fiscal sustainability calculations, we do scenarios.

Mr. Paul Szabo: On the new EI commission—the premiums go in, the benefits are paid out—it's operating at a significant deficit right now. You assume that any deficit they have is rolled into the projections. Initially I think there was a 15¢ increase in EI in the budget in the economic update. We're now down to a 5¢ increase. Even with a 5¢ increase in EI premiums, do you have any idea of the number of jobs that will cost?

● (1725)

Mr. Kevin Page: We have a rule of thumb on the fiscal cost, but we don't have a rule of thumb on the jobs.

Mr. Paul Szabo: Do we have an idea how many jobs will be created with a reduction in the corporate tax?

Mr. Kevin Page: Sir, we don't have numbers like that.

To pick up on the point that Mr. Poschmann raised, a number of international studies look at different tax regimes and the mix. They look at the impact of changing a bracket versus a rate across personal, corporate, and excise taxes, etc.

Mr. Paul Szabo: What's the biggest adverse risk to the federal government with its projections?

Mr. Kevin Page: There are a number of risks. If I only get to highlight one, we need to look to the long term. We need to look at aging demographics. We need to look beyond 2015-16 and take an account of aging demographics to really get at the issue of fiscal sustainability. Otherwise I don't think we'll be doing parliamentarians and Canadians justice.

The Chair: Thank you, Mr. Szabo.

We have two minutes, if you want time, Mr. Brison.

Hon. Scott Brison: On gross debt, when we compare Canada's debt as a percentage of GDP to other countries, we often compare our debt to unitary states where other levels of government do not carry the levels of debt we're seeing in Canadian provincial governments. It's a particularly germane question, given the timing. We're entering a period of negotiation with the provinces on health transfers, and a demographic shift is going to impose on us significant productivity challenges and increases in health and social costs.

We have an 82% gross debt as a percent of GDP; the U.S. is at 83% gross debt as a percent of GDP. Our gross debt as a percent of GDP is higher than that of the U.K., France, and Germany.

What should we be doing on the federal side to prepare for these negotiations and bring the federal government into a surplus? How concerned are you about the gross debt issue?

The Chair: We have 45 seconds, Mr. Brison, so who would you like to respond?

Hon. Scott Brison: I'd be interested in hearing from some of the bank economists on the gross debt issue.

The Chair: Ms. Webb.

Ms. Mary Webb: That's definitely the reason for moving toward balance as quickly as possible without interrupting the economic momentum. But while it is serious—and serious in terms of the accumulated deficits that the provinces have racked up that also need to be addressed—in our country net debt makes a lot of sense. There are things such as our Canada Pension Plan, where we have a fully funded national social security framework that continues to grow. That's a huge wedge, and there aren't many countries that have the same type of wedge.

So while I appreciate your concern, there are a few offsetting factors that are critical.

The Chair: Thank you.

Monsieur Paillé, *s'il vous plaît*.

[*Translation*]

Mr. Daniel Paillé: Thank you, Mr. Chairman. I know it is getting late, and so I want to thank our witnesses.

However, since I am by training an economic forecaster—you may say that it has been a long time since I practised that profession —I am used to assessing risks and probability and I can guarantee you that there is no probability at all that aliens are going to abduct Mike Wallace. They don't want him. I'm sure of that.

As he did not understand my remark, others may repeat it for him. I would like to adjourn this meeting on this humorous note that will be translated for Mr. Wallace in due course.

[*English*]

The Chair: Okay.

On that note, I want to thank all of our witnesses for being here this afternoon. Thank you for your presentations and your responses to our questions.

The meeting is adjourned.

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