

**OFFICE OF
THE PARLIAMENTARY BUDGET OFFICER**



**BUREAU DU
DIRECTEUR PARLEMENTAIRE DU BUDGET**

IMF Article IV Meeting

February 25, 2009



Outline

1) Economic and Fiscal Outlook

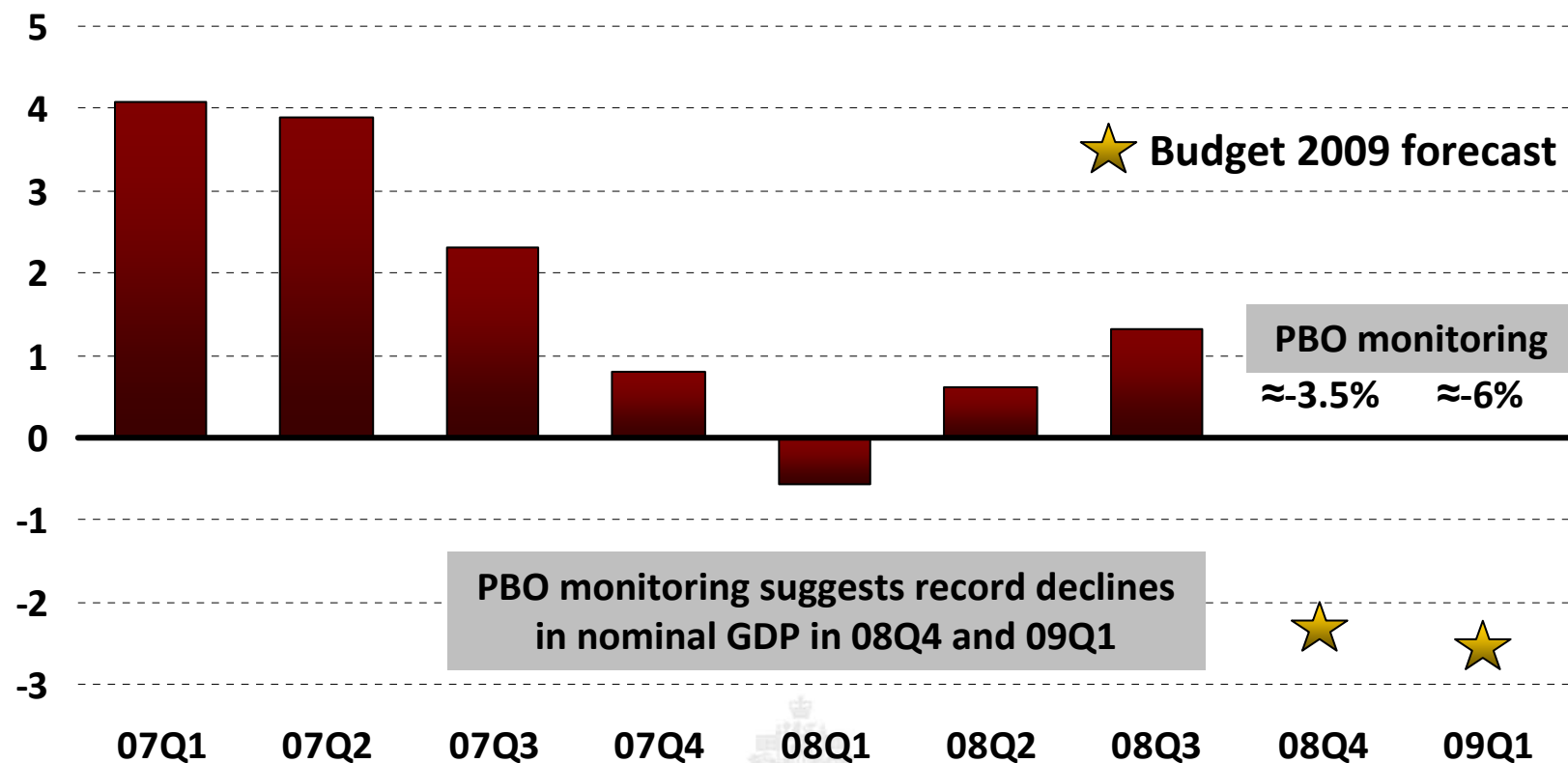
2) Fiscal Stimulus

3) Budget Practices

PBO expects weaker near-term performance compared to Budget 2009

Canadian Real GDP Growth

per cent, period to period at annual rates



Source: Budget 2009, Office of the PBO

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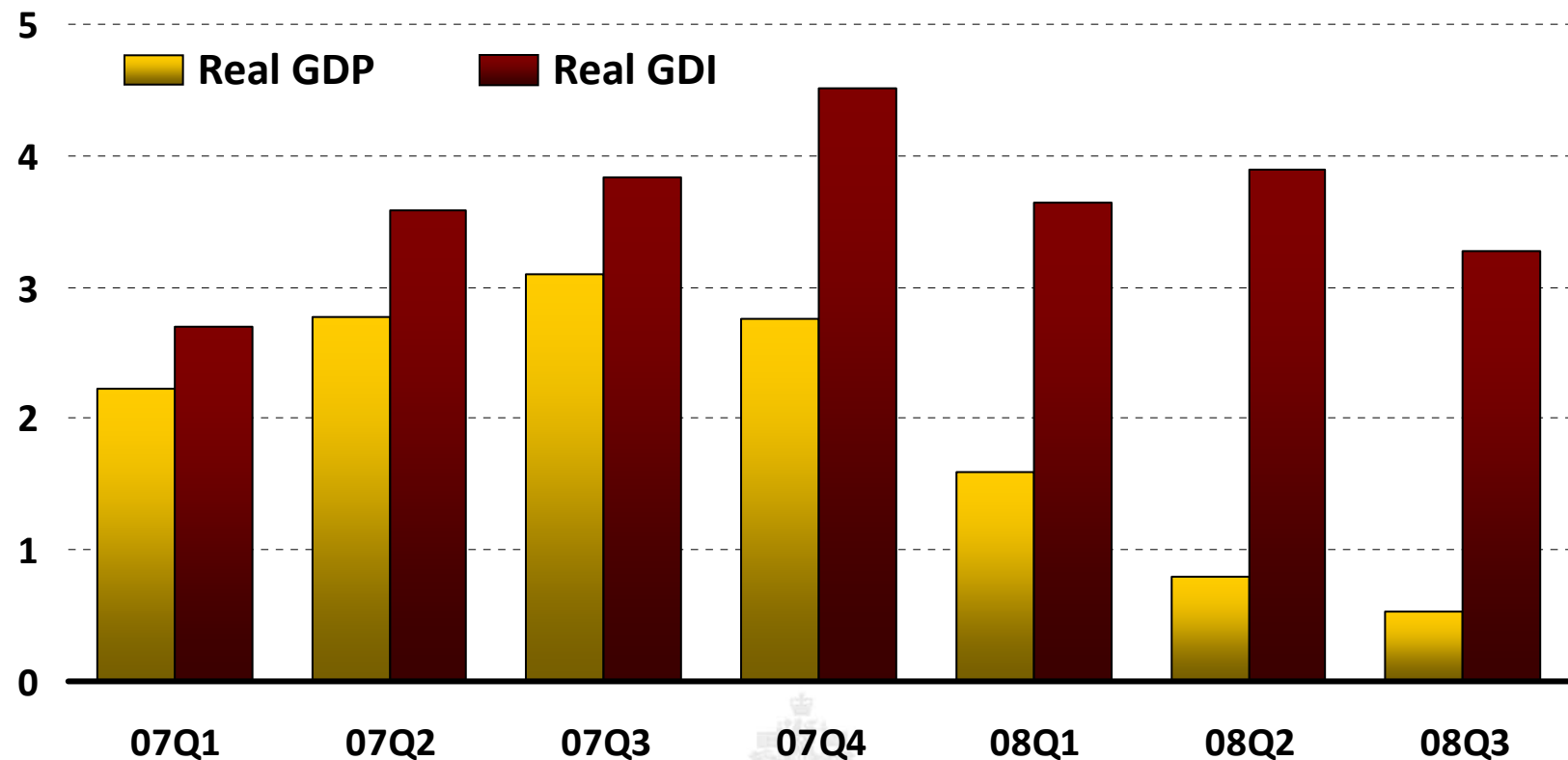


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Terms of trade gains cushioned GDP slowdown but commodity price reversal means much slower income growth ahead

Real GDP and GDI Growth

per cent, year-over-year



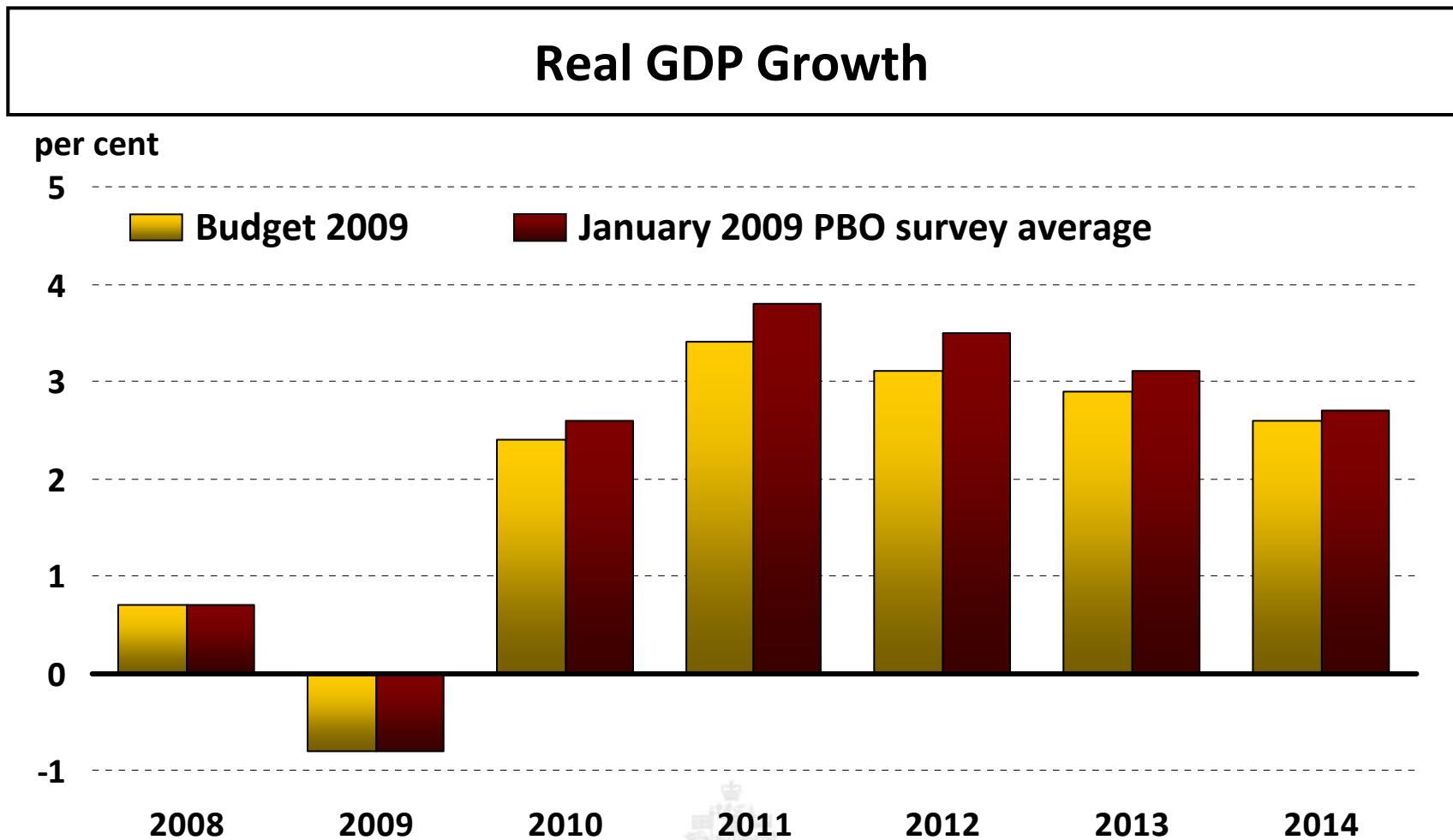
Source: Office of the PBO

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PBO survey average has slightly stronger rebound than Budget 2009 forecast



Source: Budget 2009, Office of the PBO

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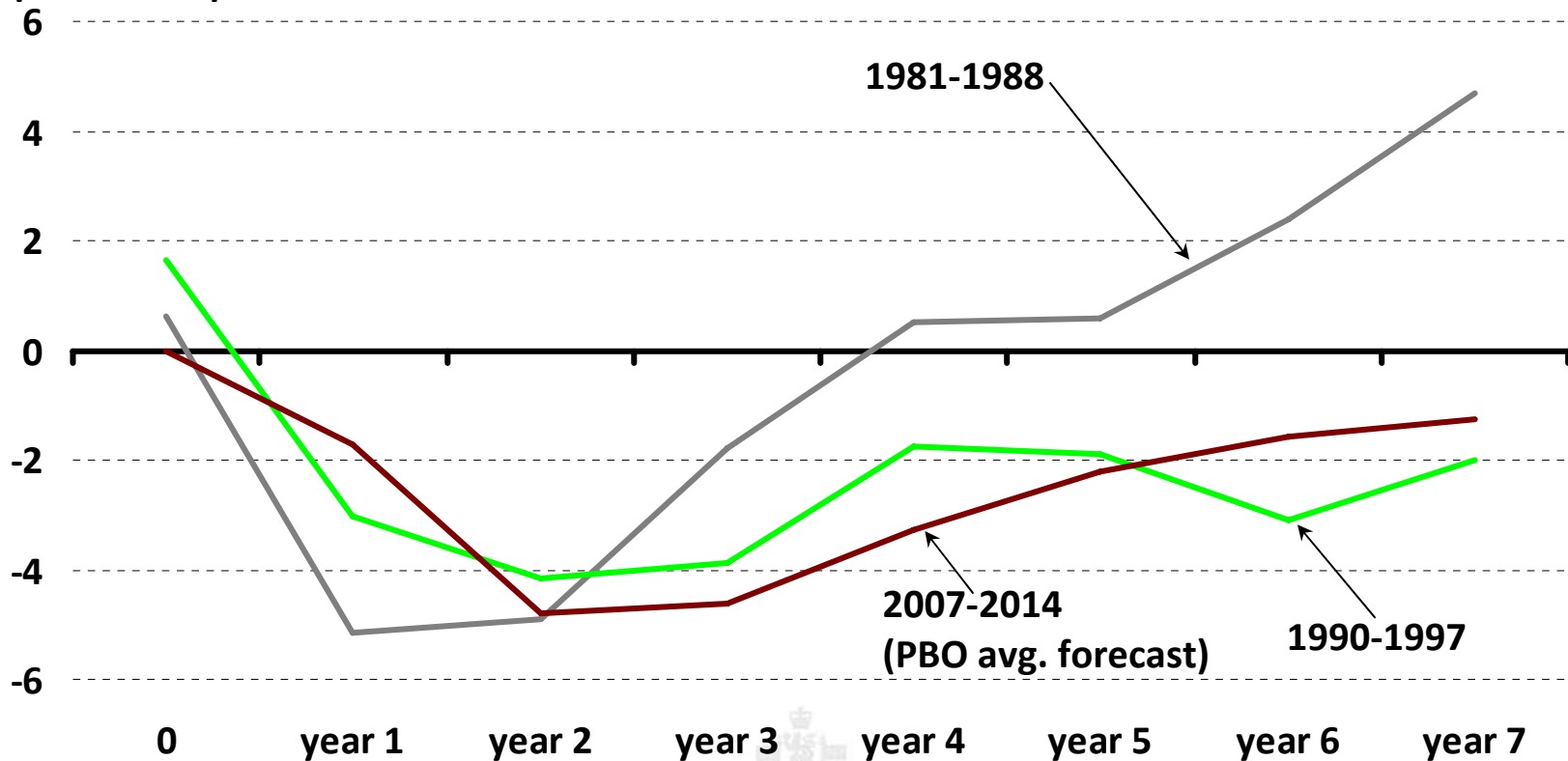


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The projected downturn is expected to be at least as severe as past two recessions

Output Gap in Previous Recessions

per cent of potential GDP*



Source: Department of Finance Canada, Office of the PBO

* Annual potential GDP growth of 2.4% assumed over 2008-2014

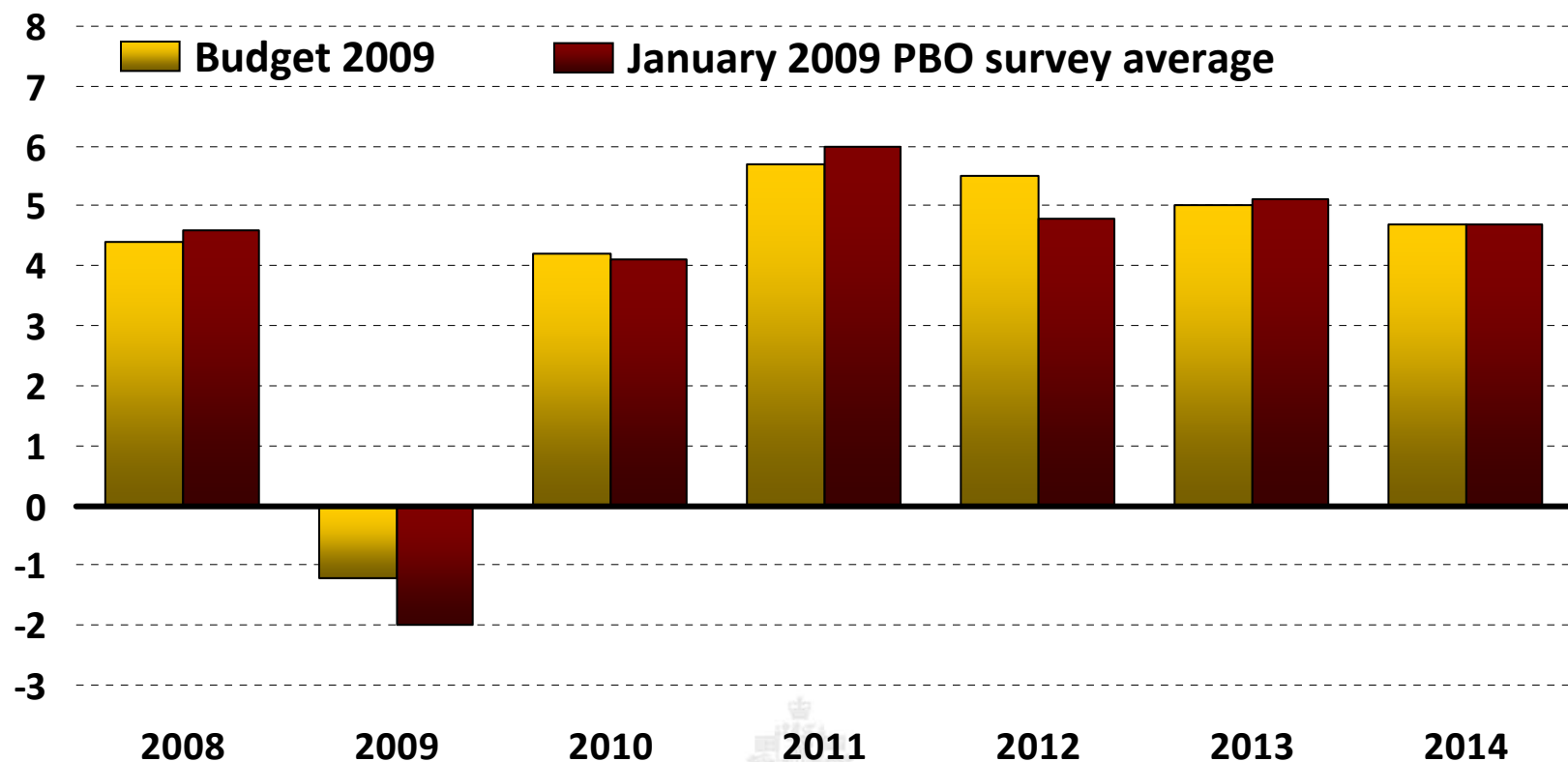


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PBO survey average outlook for nominal growth is weaker in the near term...

Nominal GDP Growth

per cent



Source: Budget 2009, Office of the PBO

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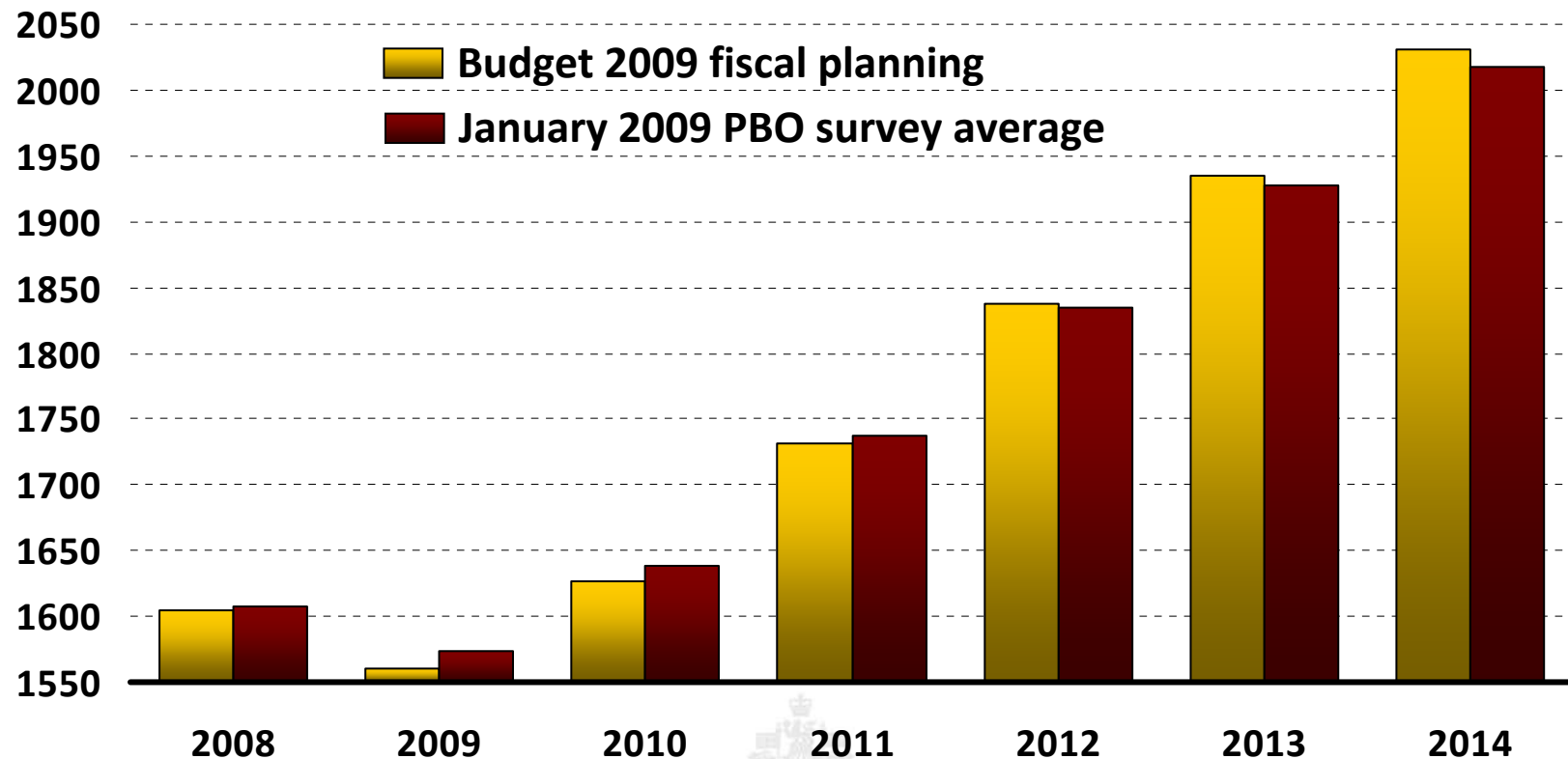


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...however Budget 2009 adjusted nominal GDP levels are very much in line with PBO survey average

Nominal GDP Outlook

\$ billions



Source: Budget 2009, Office of the PBO

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Fiscal Outlook Comparison

To put PBO and the Government's fiscal projections on a comparable basis we show outlooks excluding Budget 2009 stimulus measures and 2008 Economic and Fiscal Statement (EFS) fiscal actions:

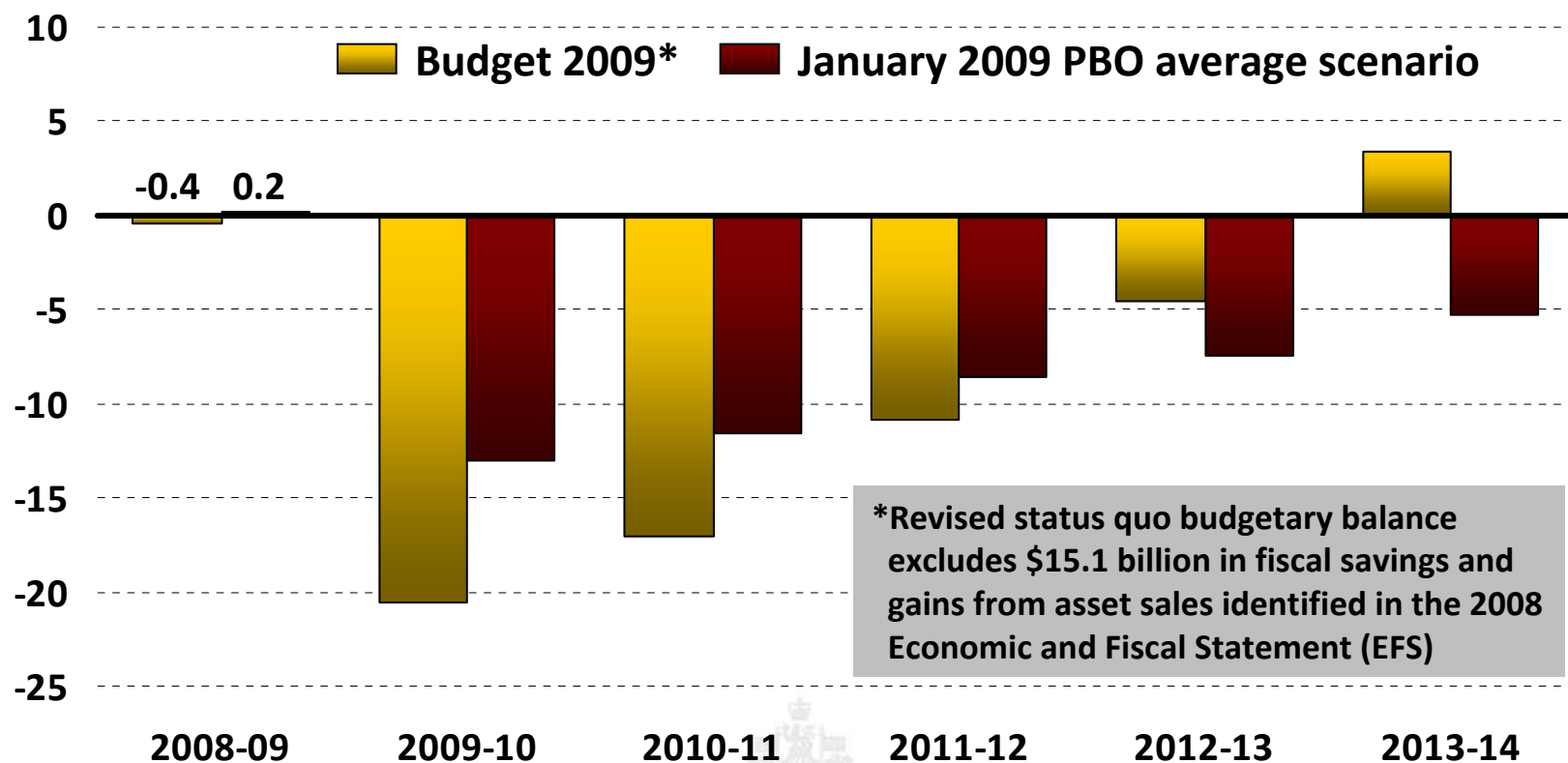
- PBO January average scenario: pre-Budget 2009 stimulus and excluding \$15.1 billion EFS fiscal actions
- Budget 2009 'revised status quo' outlook excluding \$15.1 billion in EFS fiscal actions

The Government's fiscal projections including Budget 2009 stimulus measures are shown excluding \$7.8 billion in yet-to-be-identified EFS fiscal actions

On a status quo basis Budget 2009 projects larger deficits in the near term but a more rapid return to surplus...

Status Quo Budgetary Balance

\$ billions



Source: Budget 2009, Office of the PBO

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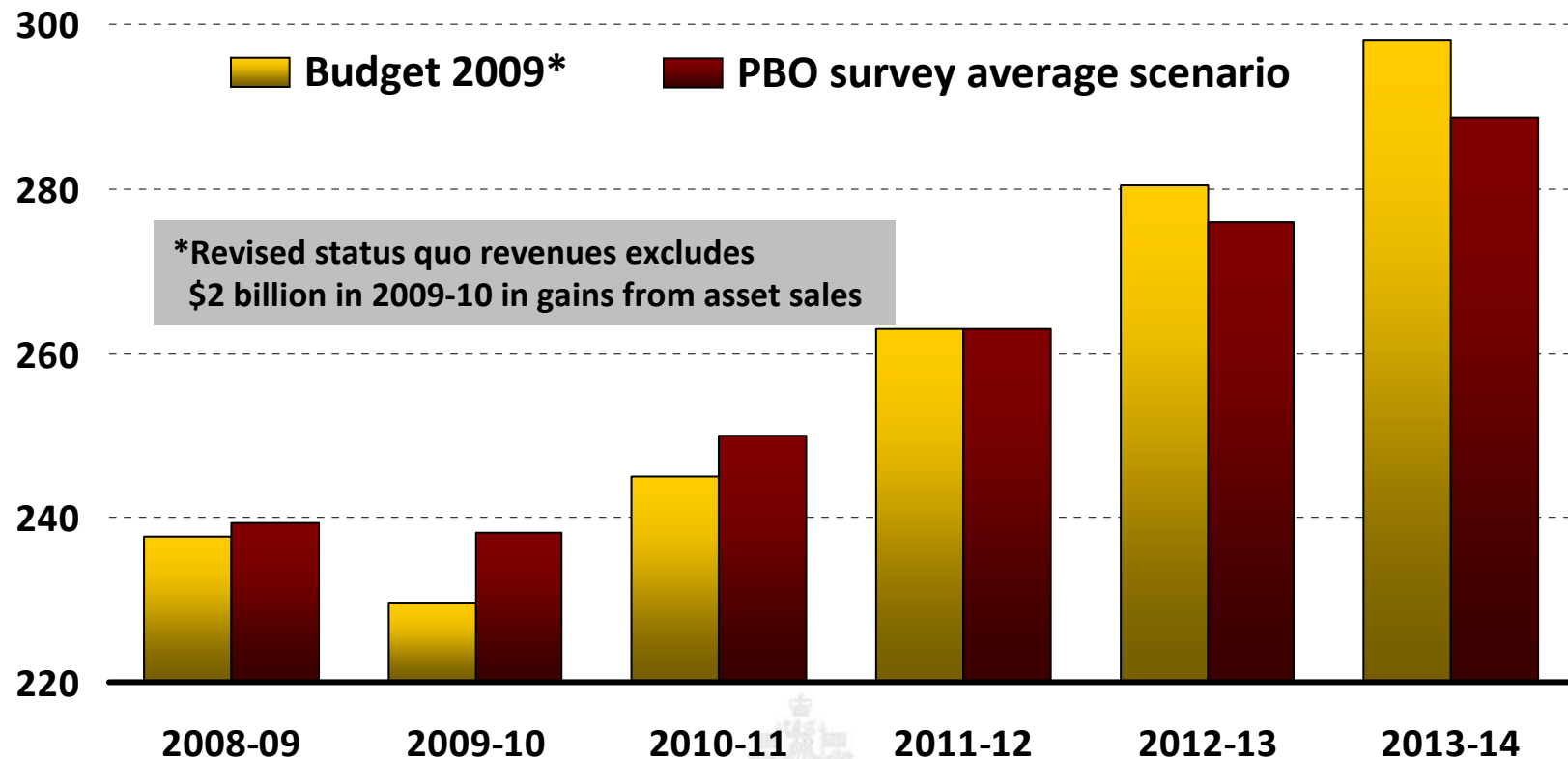


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...primarily due to stronger growth in revenues...

Status Quo Revenue Outlook

\$ billions



Source: Budget 2009, Office of the PBO

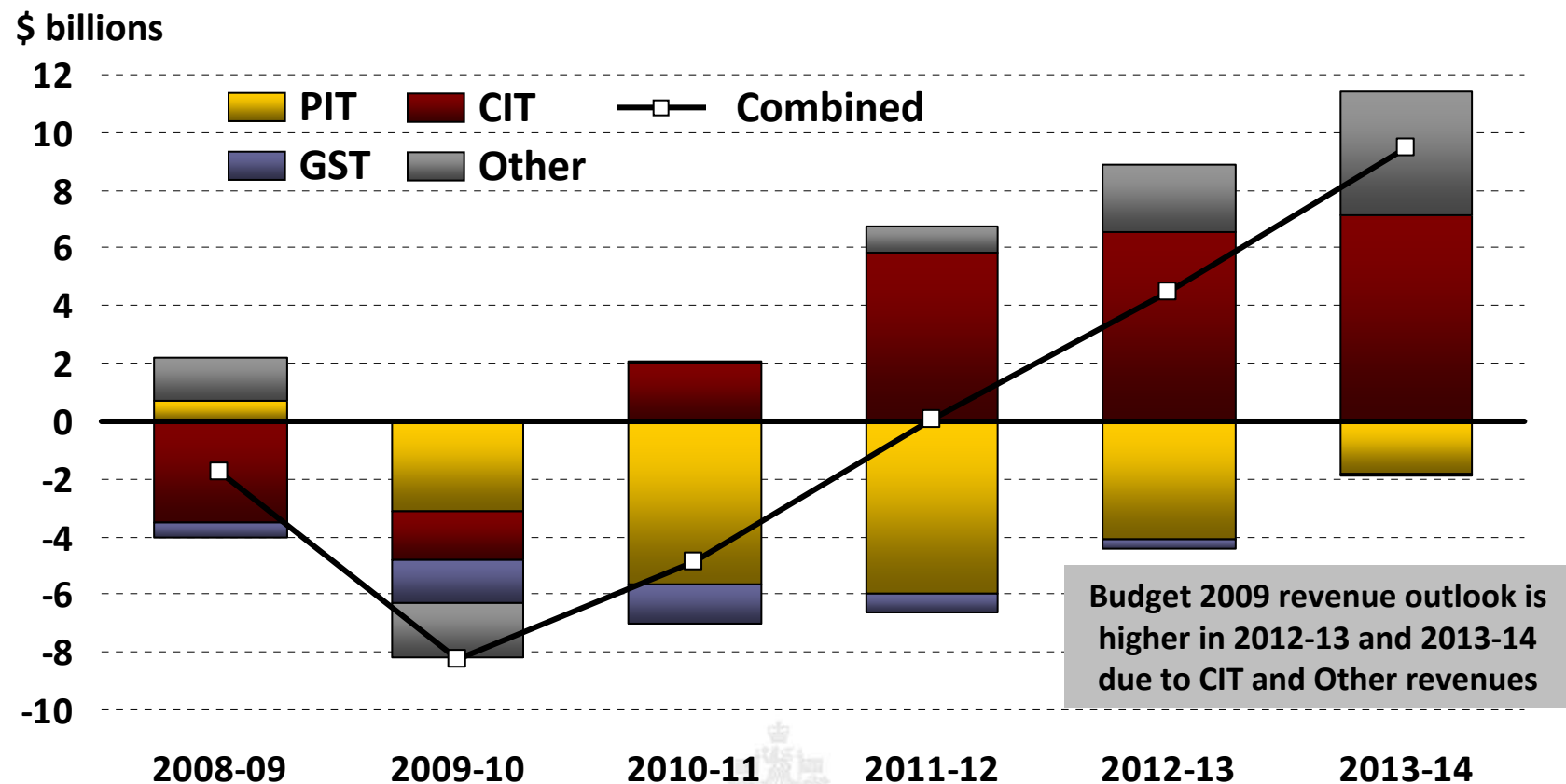
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...reflecting optimistic assumptions about corporate profits and increased EI contribution rates

Status Quo Revenue Comparison (Budget 2009 – PBO)



Source: Budget 2009, Office of the PBO

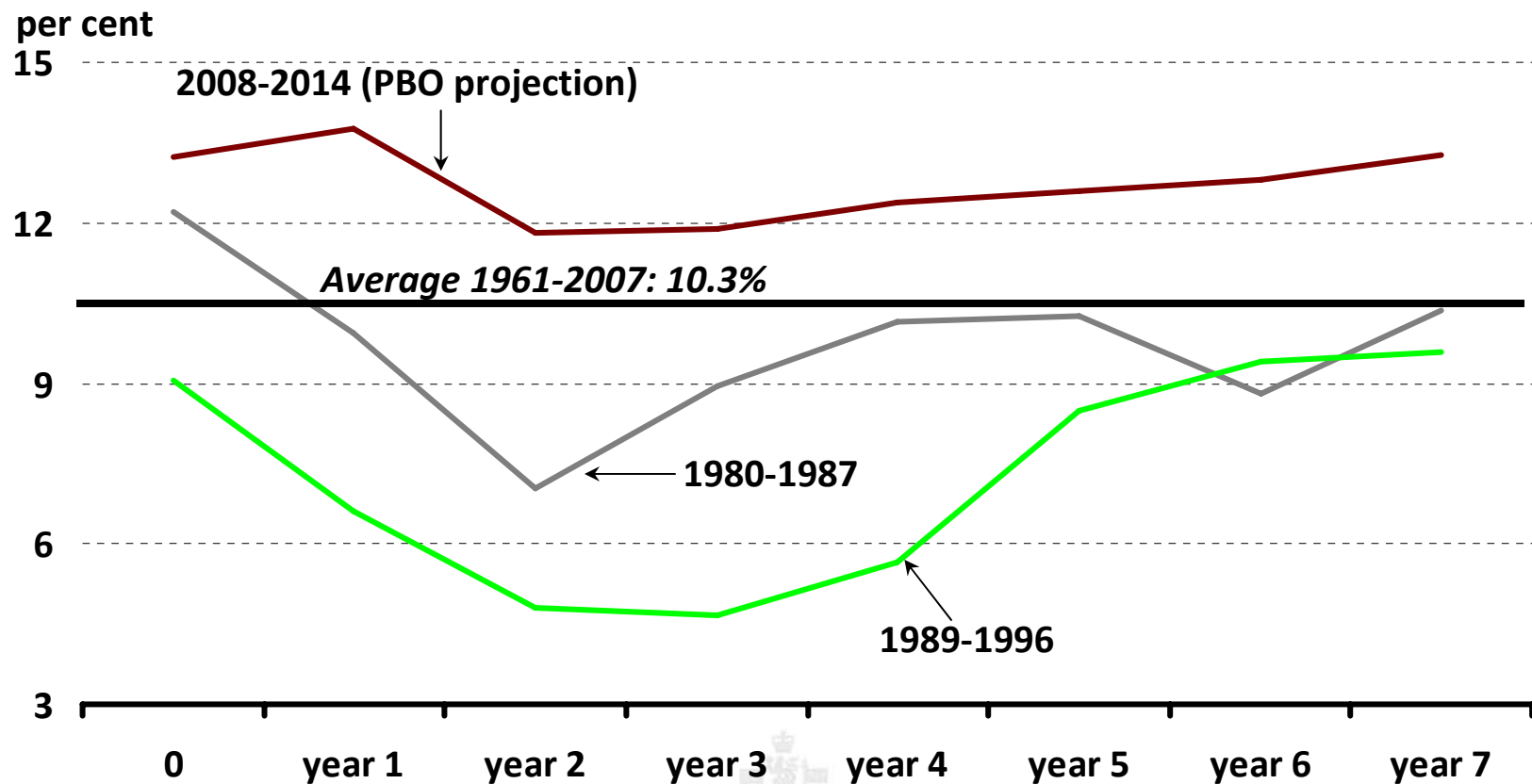
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Budget 2009 assumption about corporate profits in outer years appears to be even more optimistic than PBO

Corporate Profits relative to Nominal GDP



Source: Office of the PBO

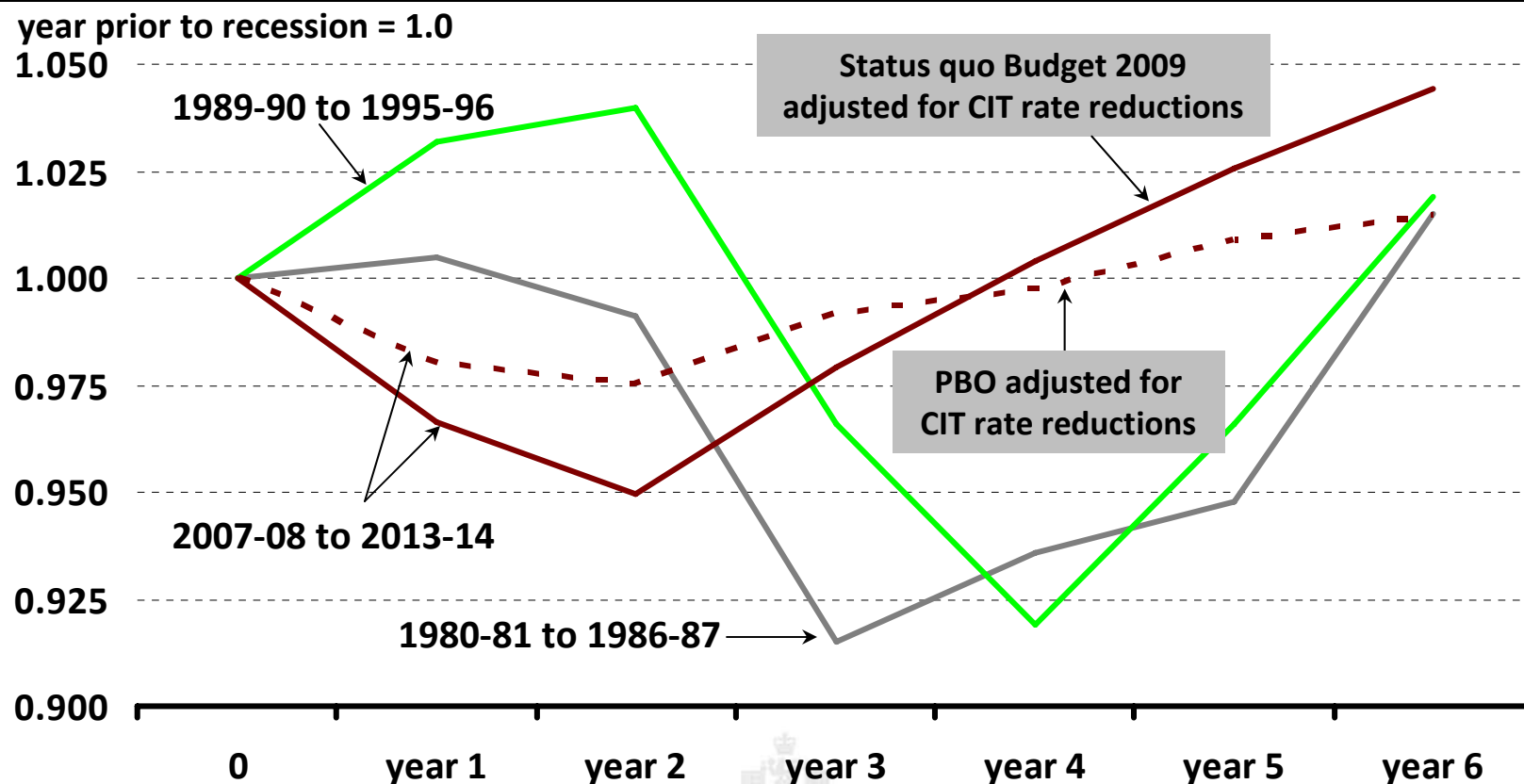
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Compared to past recessions Budget 2009 PIT and CIT revenue projections are optimistic

PIT and CIT Revenues relative to Nominal GDP



Source: Office of the PBO

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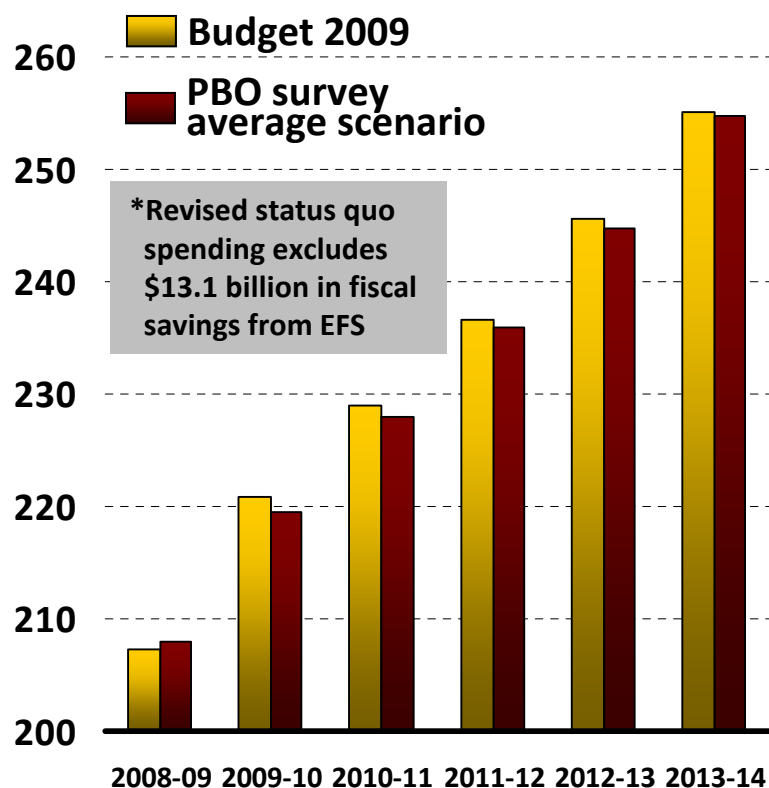


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PBO projections of program spending and public debt charges are in line with Budget 2009 projections

Status Quo Program Spending

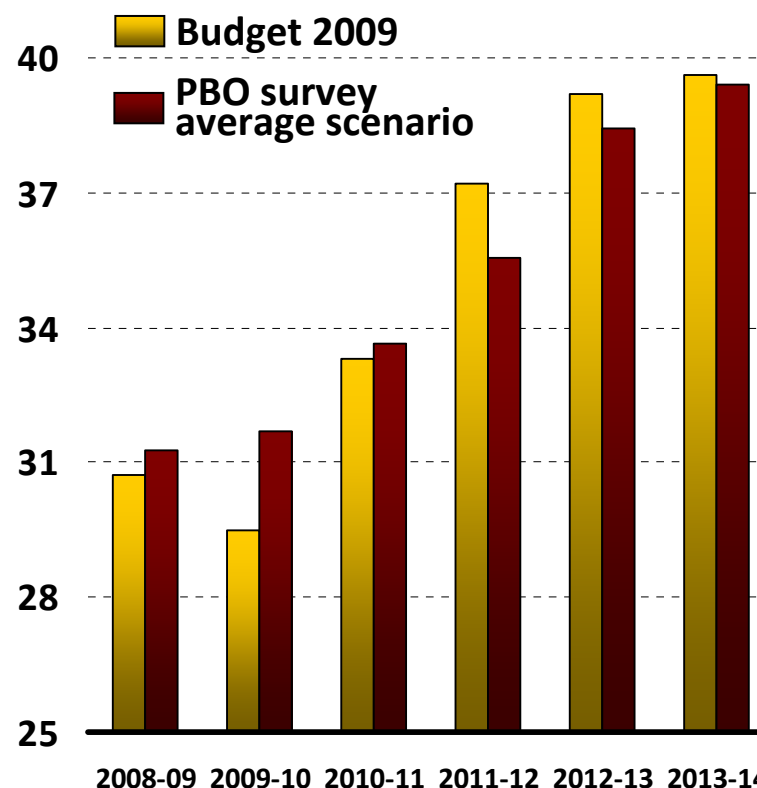
\$ billions



Source: Budget 2009, Office of the PBO

Status Quo Public Debt Charges

\$ billions



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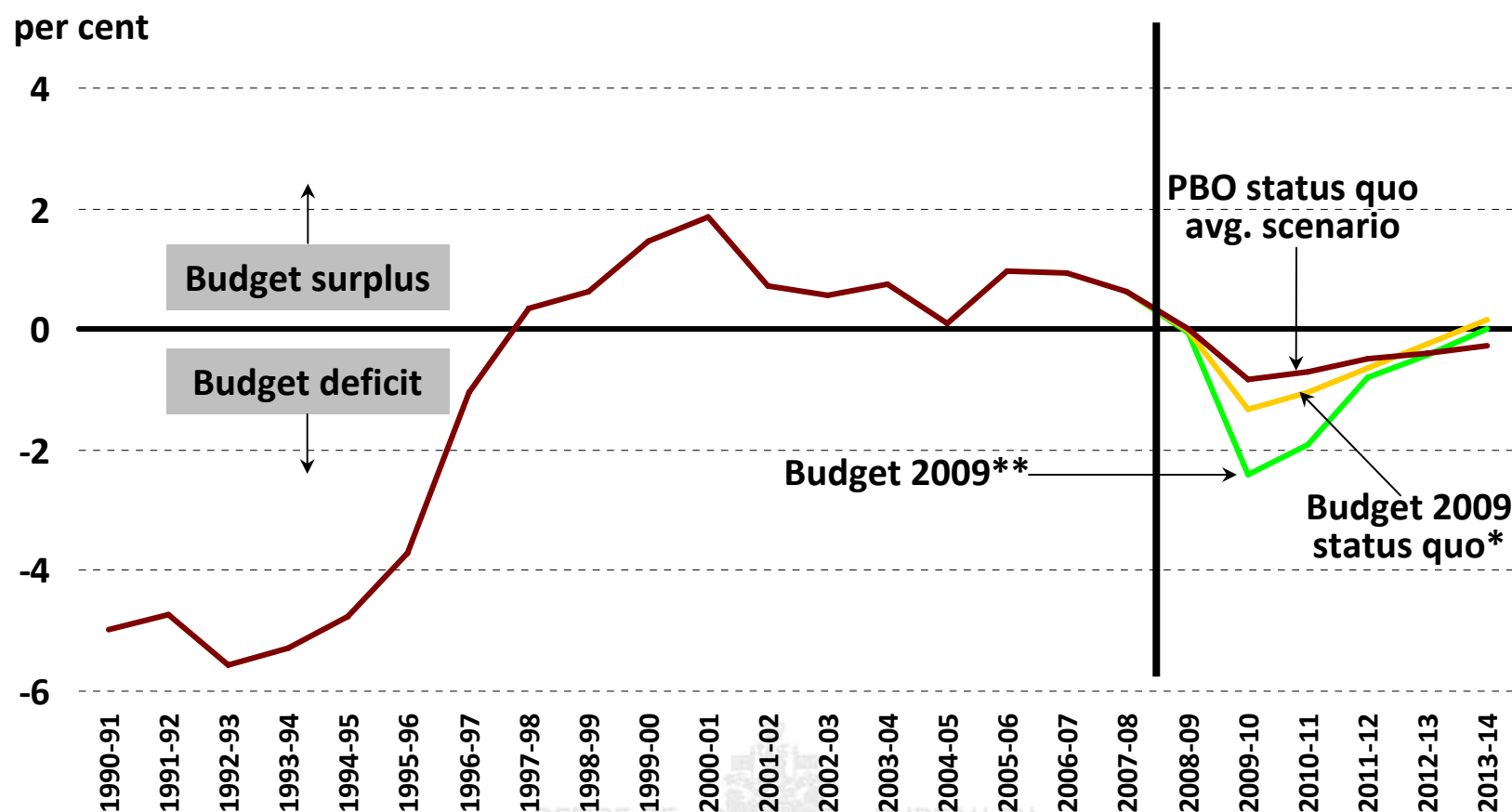
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Projected status quo budget deficits relative to the size of the economy are small and declining

Budget Balance-to-GDP Ratio



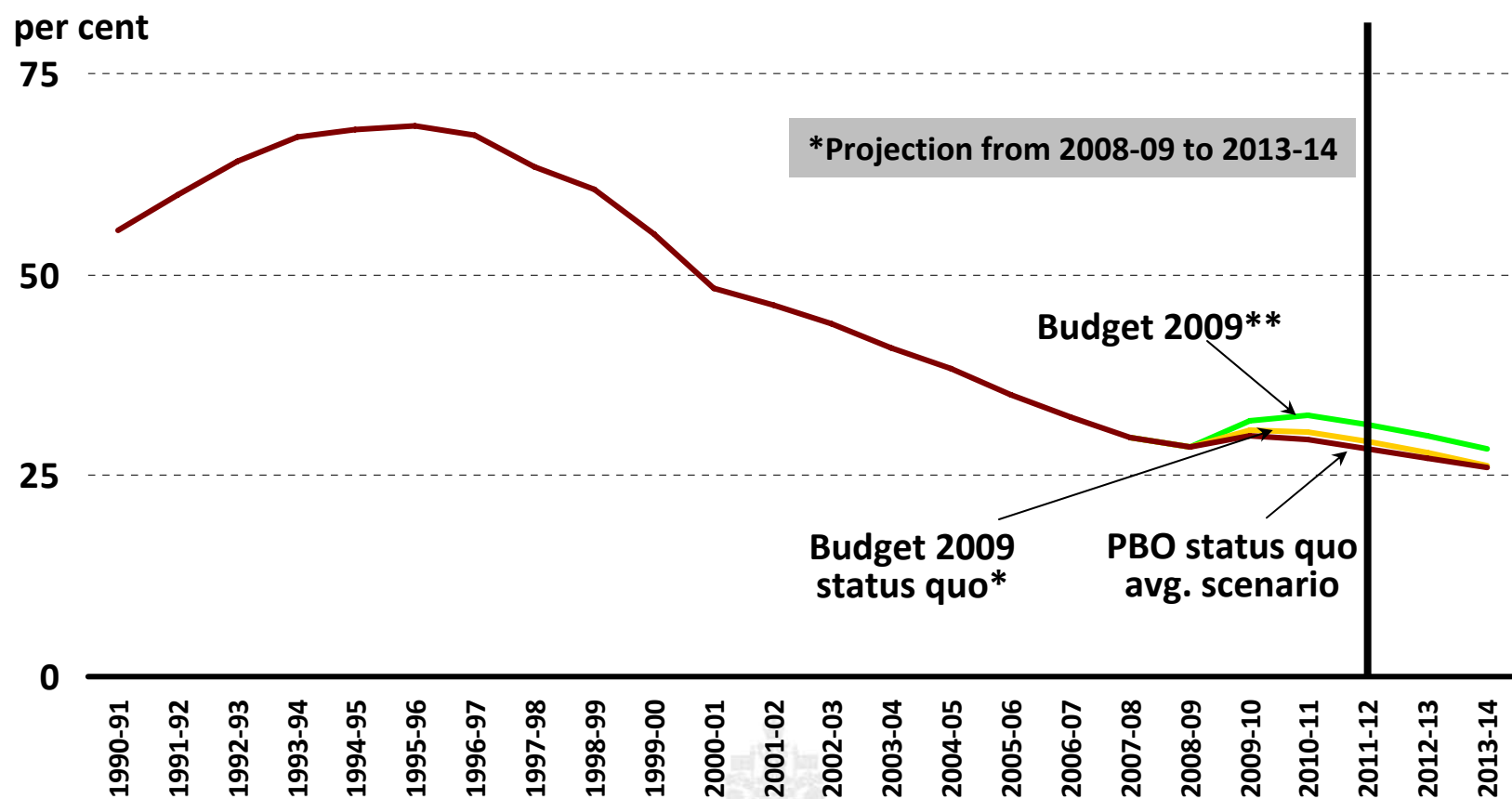
Source: Budget 2009, Office of the PBO

*excludes \$15.1 billion in fiscal savings and gains from asset sales

**excludes \$7.8 billion in yet-to-be-determined fiscal savings and gains from asset sales

Although the 25% debt-to-GDP target is not achieved by 2011-12 the debt ratio is projected to resume its downward trajectory

Debt-to-GDP Ratio and 25% Target by 2011-12



Source: Budget 2009, Office of the PBO

*excludes \$15.1 billion in fiscal savings and gains from asset sales

**excludes \$7.8 billion in yet-to-be-determined fiscal savings and gains from asset sales



Risks to the PBO January Average Scenario

Weaker-than-expected real and nominal GDP in 2008Q4 and 2009Q1

More protracted downturn through 2010 and 2011

Less pronounced improvement in commodity prices

Lower revenues due to shifts in tax bases



Fiscal Stimulus

Automatic Stabilizers

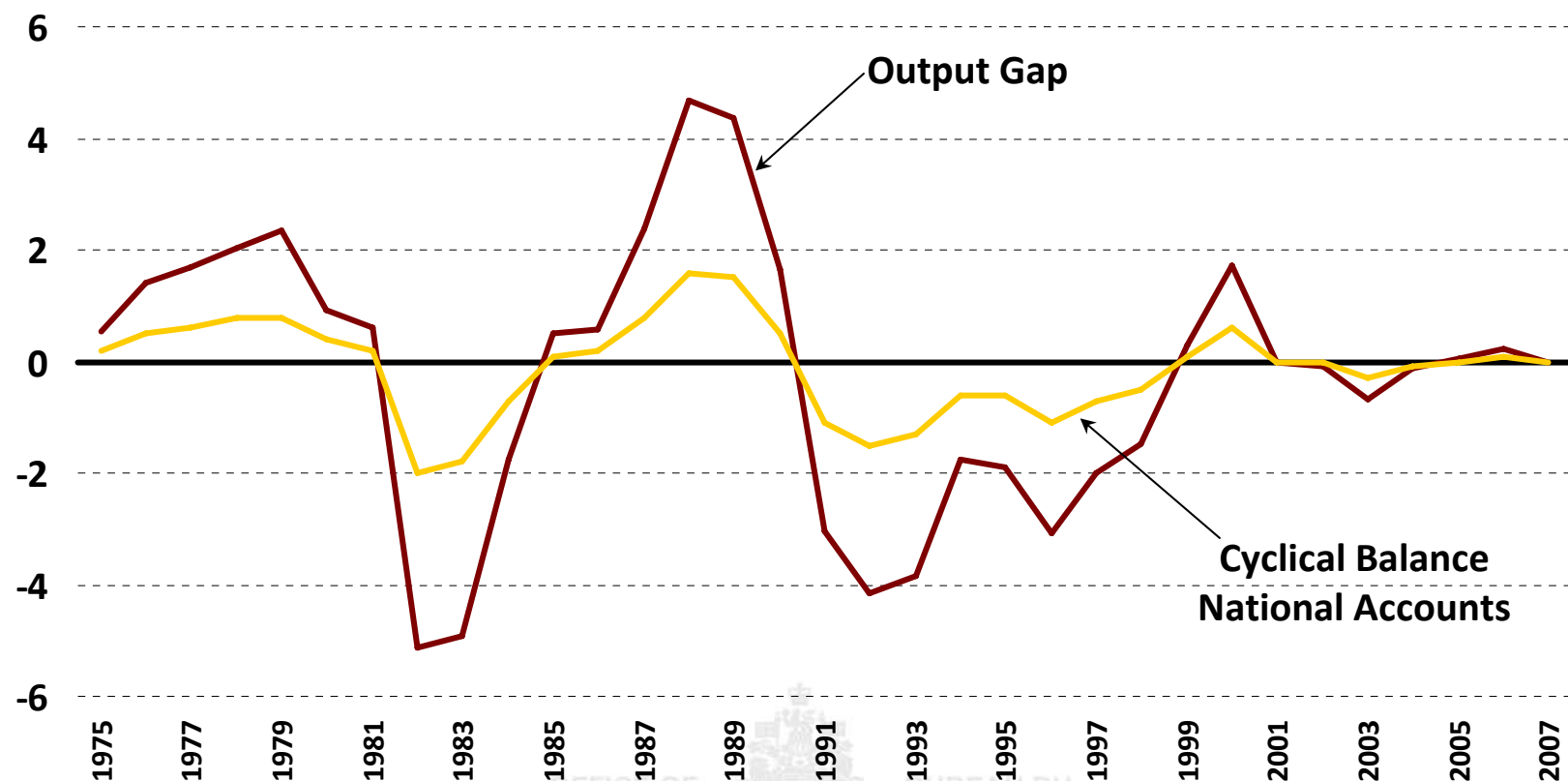
Discretionary Measures

Economic Impacts

Automatic stabilizers have supported the economy in previous recessions

Output Gap and Cyclical Budget Balance

per cent of potential GDP



Source: Department of Finance Canada

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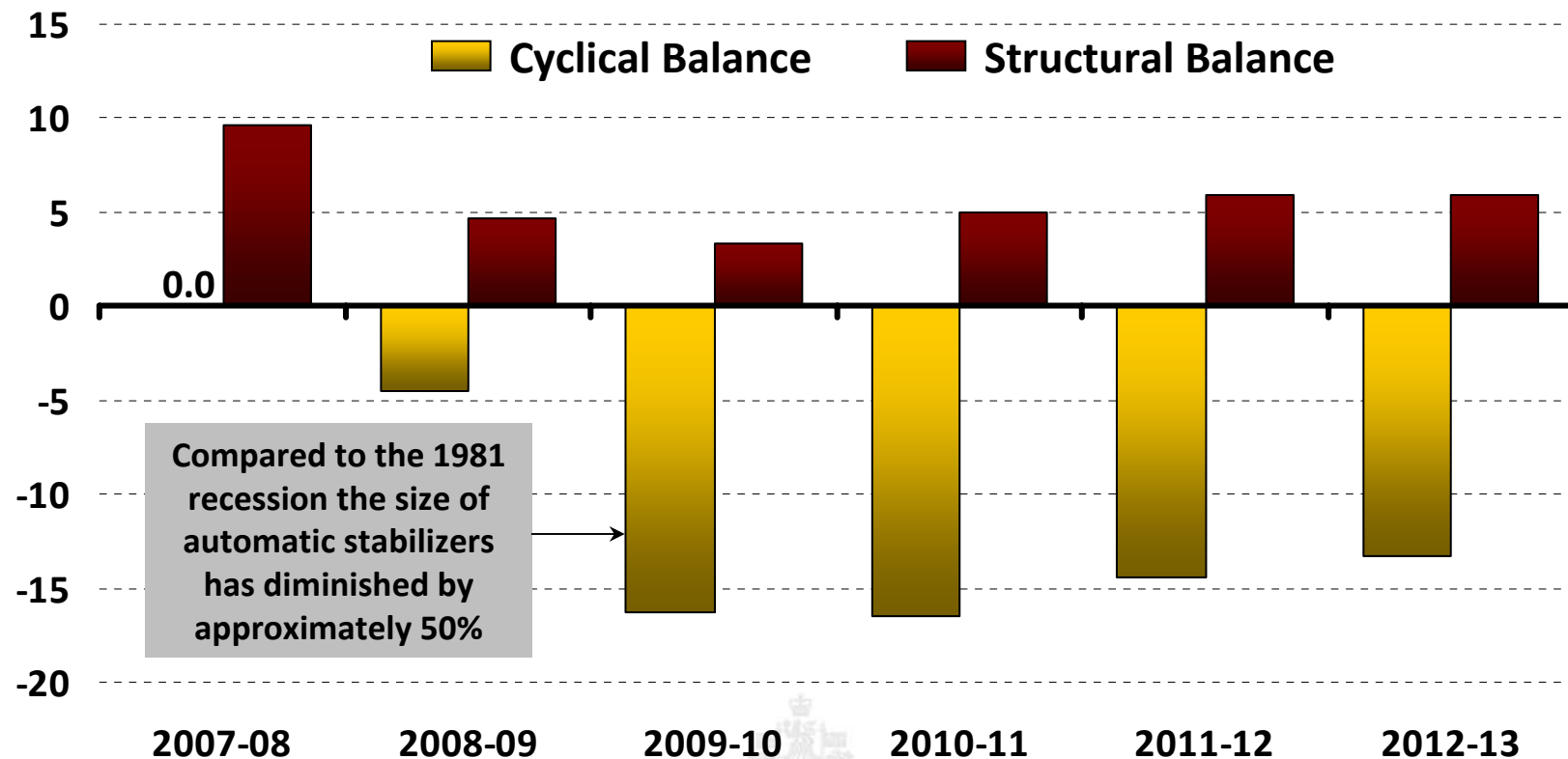


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PBO estimates that a small structural surplus exists but that the budget is less sensitive to the economic cycle

Status Quo PBO Structural and Cyclical Budget Balances

\$ billions



Source: Office of the PBO

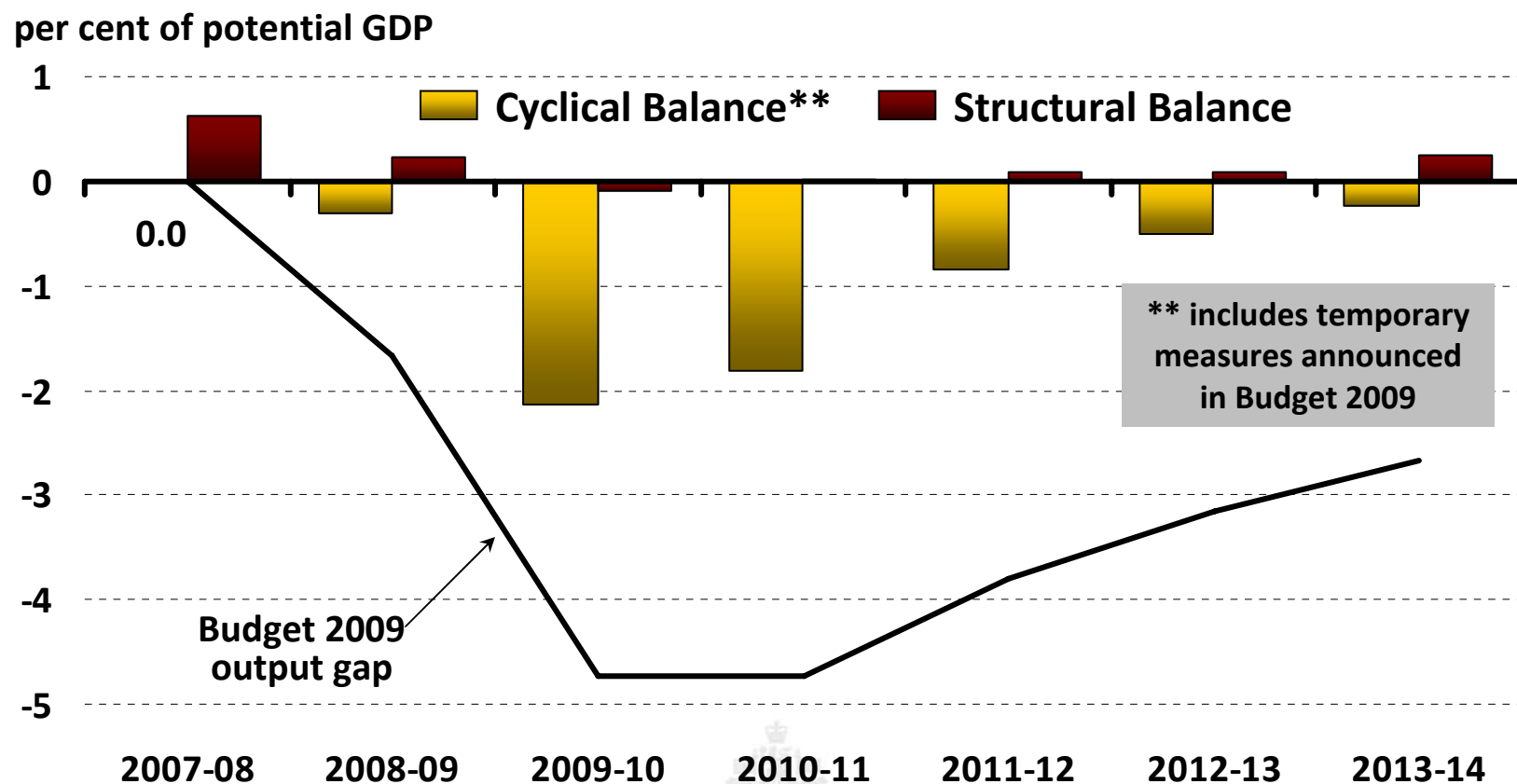
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After accounting for Budget 2009 measures the cyclical balance is providing as much near-term support as in the 1981 recession

Budget 2009* Structural and Cyclical Budget Balances



Source: Department of Finance Canada, Office of the PBO

* excluding \$7.8 billion in yet-to-be-determined fiscal savings and gains from asset sales



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Budget 2009 Discretionary Fiscal Policy Response

1) Timely

- *\$7.3 billion in federal infrastructure planned for 2009 may not get out the door on time*

2) Targeted

- *Most of the budget measures have an average multiplier greater than 1.0*

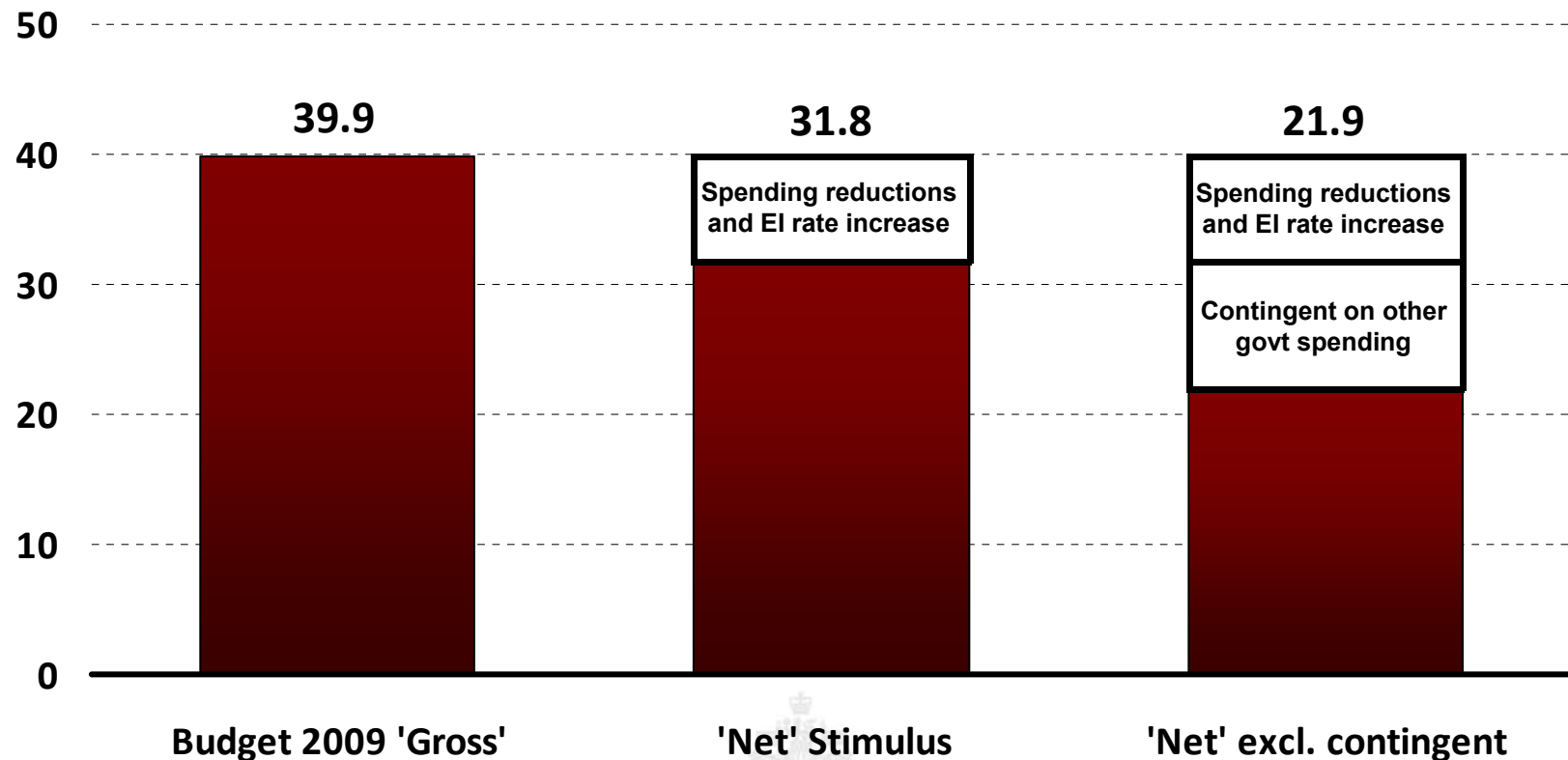
3) Temporary

- *\$5.5 billion in permanent PIT and CIT measures;
\$1.7 billion in spending on training and other measures
could become permanent*

Budget 2009 estimate of the size of the federal stimulus is overstated

Estimates of Federal Fiscal Stimulus 2009-10 to 2010-11

\$ billions



Source: Budget 2009, Office of the PBO

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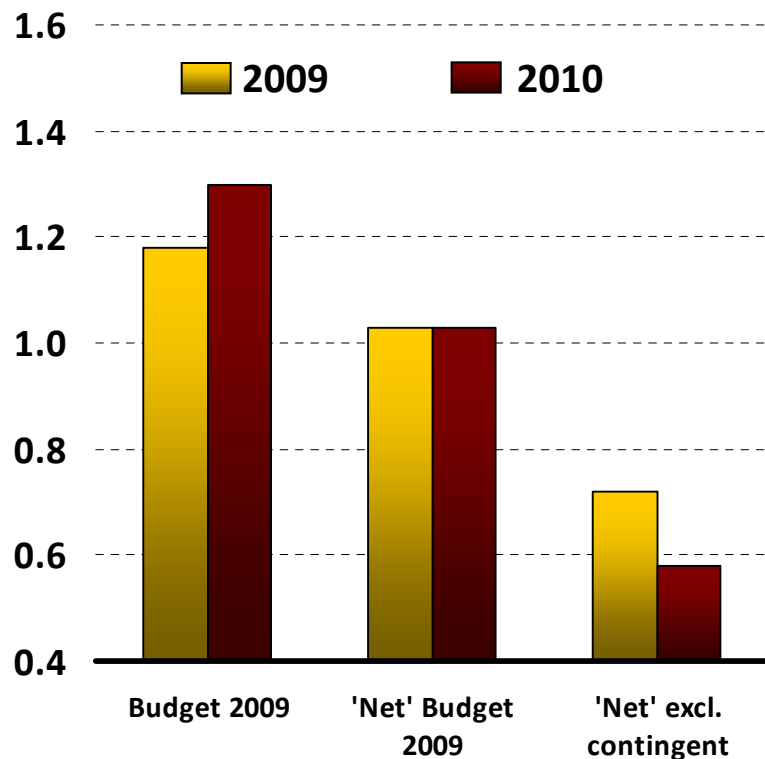


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As a result the expected economic impacts of the stimulus may be overestimated

Impact on Real GDP of Federal Stimulus

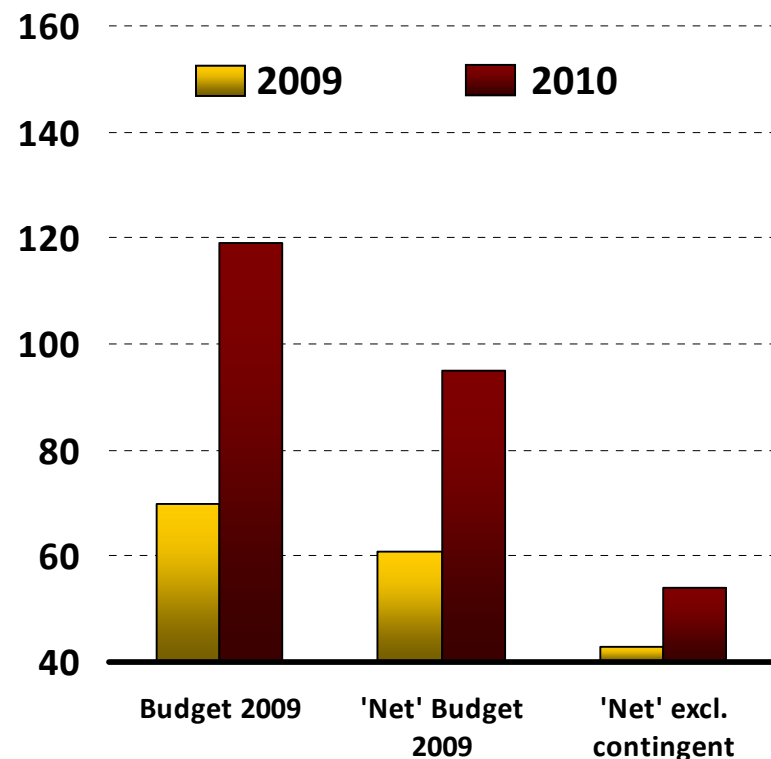
per cent difference



Source: Budget 2009, Office of the PBO

Impact on Employment of Federal Stimulus

thousands of jobs



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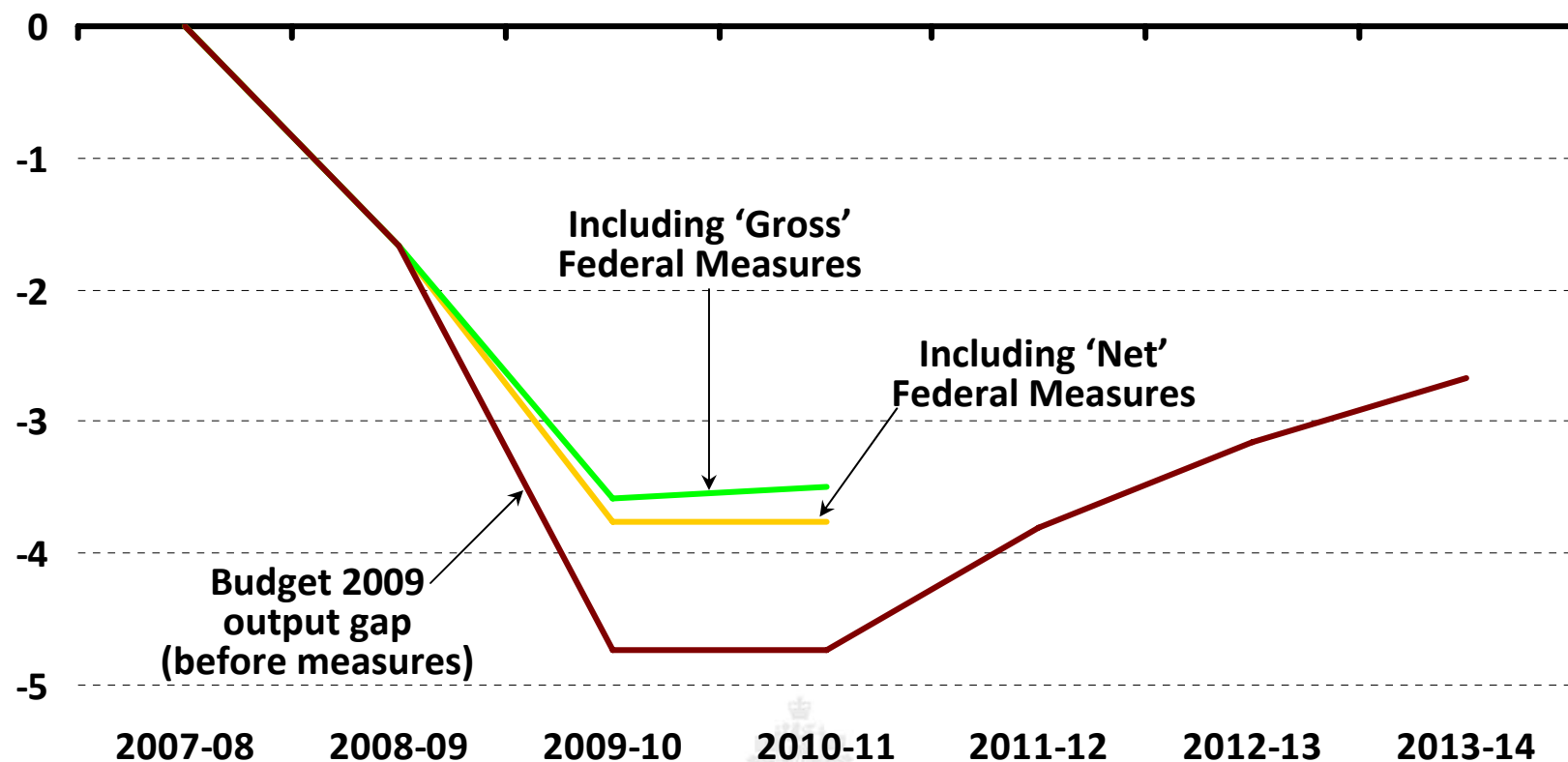
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Budget 2009 measures will help cushion the impact of the downturn but the economy will remain well below its potential

Impact of Budget 2009 Federal Stimulus on the Output Gap

per cent of potential GDP



Source: Budget 2009, Office of the PBO

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Budget Practices

Budget Transparency

Fiscal Policy Governance

Budget 2009 Implementation



Budget Transparency

- There is considerable scope for the Government of Canada to improve the transparency of its budget plans
- The Government “could enhance the understanding of budgetary forecasts by providing more information on the assumptions and methods underlying the translation of the macroeconomic outlook into fiscal projections” -- *IMF Working Paper, 2005*
- There is a “need for Finance to provide a detailed breakdown of the linkages between the (external) economic and (internal) National Accounts fiscal forecasts and of the reconciliation of the National Accounts to the Public Accounts fiscal projections” -- *2005 Review of Canadian Federal Fiscal Forecasting, Tim O’Neill*



Governance

- The PBO supports the IMF's call for broader reforms to fiscal policy governance which would bolster the impact of fiscal stimulus measures
- While the Government of Canada – as recommended by the IMF – has already established a sort of 'fiscal watchdog' by creating the PBO, the PBO's independence and operational model need to be clarified and adequately financed
- Compared to other countries' budget offices, Canada's PBO is relatively small in terms of the size of its staff and budget



Budget 2009 Implementation and Oversight

- Increased scrutiny of Budget 2009 stimulus measures paves the way for improved budgetary reporting and oversight practices
- PBO is contributing to this scrutiny by suggesting some key elements for the Government's proposed quarterly reports and by proposing a framework to assist Parliamentary oversight and track budget implementation
- The central goal of the proposed quarterly reporting framework — whatever specific shape it ultimately takes — should be to provide Parliament with accurate, timely, and easily understood information on recent economic and fiscal developments and prospects as well as the implementation and effectiveness of budget measures
- PBO's work in this area is a work in progress and will evolve based on feedback received