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Economic and Fiscal Outlook 2014

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The mandate of the Parliamentary Budget Officer (PBO) is to provide independent analysis to Parliament on the state of the nation's finances, the government's estimates and trends in the Canadian economy; and upon request from a committee or parliamentarian, to estimate the financial cost of any proposal for matters over which Parliament has jurisdiction.

This report fulfils the September 29, 2011 Standing Committee on Finance motion that "[c]onsistent with the Parliamentary Budget Office[r] (PBO) mandate […] the PBO provide an economic and fiscal outlook to the Committee the fourth week of October and April of every calendar year and be available to appear before the Committee to discuss its finding shortly thereafter."

Economic and Fiscal Outlook 2014 provides PBO's economic and budgetary projections based on data up to and including April 8, 2014.

Prepared by: Randall Bartlett, Scott Cameron and Helen Lao*

* The authors thank Mostafa Askari, Jason Jacques, Pat Brown and Jocelyne Scrim for comments. Any errors or omissions are the responsibility of the authors.
Please contact Mostafa Askari (email: mostafa.askari@parl.gc.ca) for further information.

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Summary

Economic outlook

Compared to PBO's previous economic and fiscal projection published in the October 2013 Economic and Fiscal Outlook Update (EFOU), prospects for the Canadian economy are generally more positive, as a result of buoyant international economic growth and sustained domestic demand.

Global economy

Global economic activity and trade picked up in the second half of 2013, as final demand in advanced economies increased at a steady pace while higher inventory investment surprised on the upside. In emerging market economies, solid export growth drove economic activity, outpacing the more subdued growth in domestic demand.

The April 2014 International Monetary Fund (IMF) World Economic Outlook (WEO) indicates that global economic activity is expected to continue to improve in 2014 and 2015, with much of the strength coming from advanced economies, largely reflecting a reduction in fiscal tightening complemented by still highly accommodative monetary policy. That said, downside risks remain, with risks related to low inflation in advanced economies coming to the fore more recently.

U.S. economy

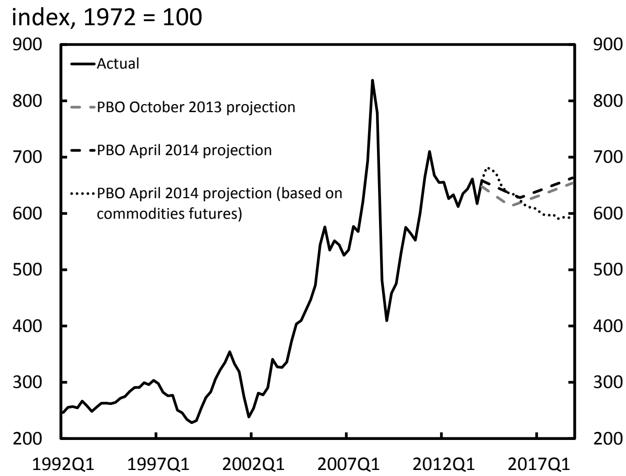
U.S. real GDP advanced by 1.9 per cent in 2013—0.3 percentage points stronger than projected by PBO in October 2013. Despite the stronger-than-expected growth, PBO has left its outlook for U.S. growth in 2014 unchanged at 2.7 per cent due to weaker-than-expected growth at the beginning of the year. Growth over the remainder of the projection is broadly unchanged.

Commodity prices

Based on the Bank of Canada's Commodity Price Index (BCPI), energy price growth in 2013 was broadly in line with the October 2013 EFOU projection, while non-energy commodity prices were modestly weaker. As a result, the PBO outlook for commodity prices is little changed from the October 2013 EFOU projection (Summary Figure 1). PBO's outlook for the BCPI remains higher over the projection than futures prices would suggest.

Summary Figure 1

Commodity Price Projection, 1992Q1 to 2018Q4



Sources: Office of the Parliamentary Budget Officer; Bank of Canada; Bloomberg.

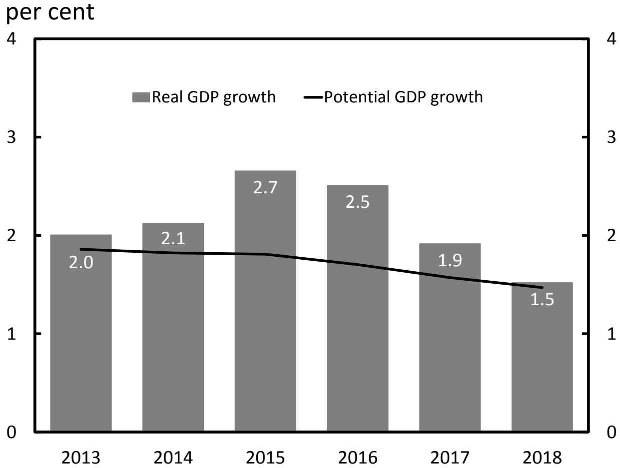
Canadian economy

Real GDP growth of 2.0 per cent in 2013 was 0.4 percentage points stronger than projected in the October 2013 EFOU. PBO projects real GDP growth in Canada to accelerate to 2.1 per cent in 2014 and remain above its potential growth rate until 2018. This solid growth is the result of higher domestic and external demand, partly offset by government spending restraint acting as a drag on economic activity and job creation going forward (Summary Figure 2).

Summary Figure 2

Real GDP and Potential GDP Growth

per cent



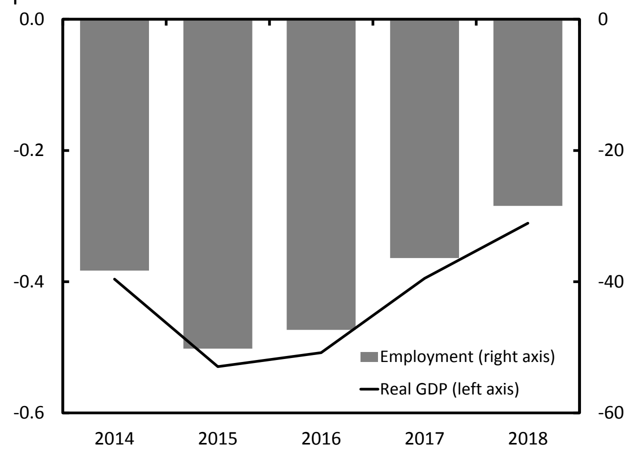
Sources: Office of the Parliamentary Budget Officer; Statistics Canada.

PBO's outlook incorporates Budget 2014 measures, including stimulative measures (i.e., "actions to support jobs and growth") and savings measures (i.e., spending reductions and revenue increases). When these measures are combined with the spending, savings, and revenue measures, as well as revisions to spending levels introduced beginning in Budget 2012, the level of real GDP is projected to be 0.5 per cent lower in 2016 than would have been the case in the absence of these measures (Summary Figure 3). Further, this economic impact translates into about 46,000 fewer jobs being created by 2016.

Summary Figure 3

Economic Impacts of Budget Measures since Budget 2012

per cent of real GDP thousands



Source: Office of the Parliamentary Budget Officer.

Note: The estimated impacts on real GDP and employment do not include changes to employment insurance premiums or take into account offsetting impacts from changes to interest and exchange rates. Impacts are expressed relative to PBO's current projection of real GDP.

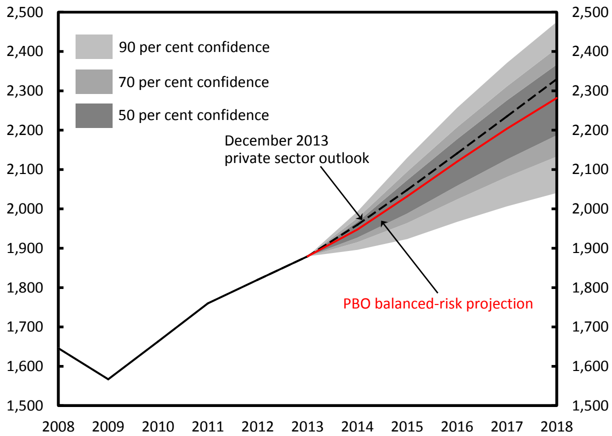
PBO uses its outlook to highlight what it believes are the key risks to the private sector economic outlook on which the Government's fiscal projections are based.

Based on its projection of nominal GDP, PBO judges that the downside risk to the private sector outlook for nominal GDP is broadly in line with the Government's $20 billion annual adjustment for risk (Summary Figure 4).

Summary Figure 4

Nominal GDP Projections

billions of dollars



Sources: Office of the Parliamentary Budget Officer; Finance Canada; Statistics Canada.

Fiscal Outlook

Prospects for budgetary surpluses are higher over the outlook than in EFOU 2013 due to a combination of an improved economic outlook and measures in Budget 2014, in particular further planned restraint in Direct Program Expenses (DPE).

PBO estimates that the budgetary balance will be $11.6 billion (0.6 per cent of GDP) in deficit in 2013-14. PBO projects the budget will reach a surplus of $7.8 billion (0.4 per cent of GDP) in 2015-16 and maintain an average surplus of $8.6 billion (0.4 per cent of GDP) over the remainder of the outlook (Summary Table 1). A budgetary surplus could be achieved in 2014-15 (one-year earlier than the government's target) if PIT revenues rebound at a higher rate than expected, or if departments underspend (lapse) at the same rate as fiscal years 2009-10 to 2012-13 (over 8 per cent of appropriations).

Summary Table 1

Statement of operations

billions of dollars

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Budgetary revenues	268.3	280.0	297.1	310.4	320.3	332.5
Program expenses	251.0	250.7	258.7	267.8	276.0	284.5
Public debt charges	28.9	29.8	30.5	33.4	36.8	38.9
Budgetary balance	-11.6	-0.5	7.8	9.1	7.5	9.1
Federal debt	614.0	614.5	606.7	597.6	590.1	580.9
Per cent of GDP						
Budgetary revenues	14.3	14.4	14.6	14.6	14.5	14.6
Program expenses	13.4	12.9	12.7	12.6	12.5	12.5
Public debt charges	1.5	1.5	1.5	1.6	1.7	1.7
Budgetary balance	-0.6	0.0	0.4	0.4	0.3	0.4
Federal debt	32.7	31.6	29.9	28.2	26.8	25.5

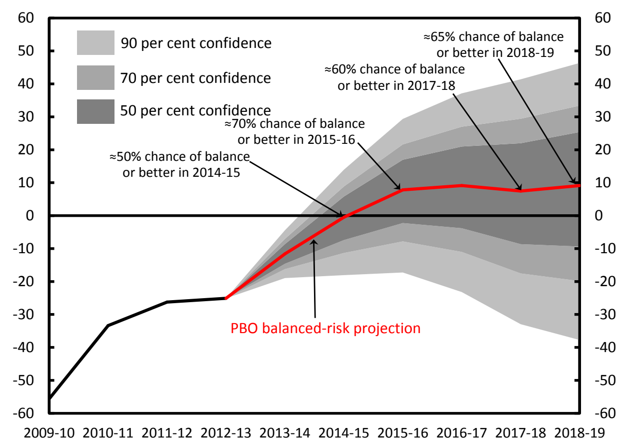
Source: Office of the Parliamentary Budget Officer.

PBO estimates that the likelihood of realizing a budgetary balance or better is approximately 50 per cent in 2014-15, and more than 60 per cent in 2015-16 and beyond (Summary Figure 5).

Summary Figure 5

Budgetary Balance Outcomes Given Economic Uncertainty

billions of dollars



Sources: Office of the Parliamentary Budget Officer; Finance Canada.

While PBO projects budgetary surpluses over the medium-term, these are primarily attributable to the economy growing faster than trend (i.e. cyclical factors), rather than revenues from tax policy being fundamentally higher than projected expenses (i.e. structural factors). PBO's estimate of the underlying structural balance suggests there is limited room to implement new policies which reduce tax revenues or increase spending without re-introducing structural deficits (Summary Table 2).

Summary Table 2

Structural and Cyclical Balance Estimates

billions of dollars

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Budgetary balance	-11.6	-0.5	7.8	9.1	7.5	9.1
Structural balance	-4.5	4.8	8.9	5.7	2.0	3.1
Cyclical balance	-7.1	-5.3	-1.1	3.4	5.5	6.0

Source: Office of the Parliamentary Budget Officer.

Risks to the outlook

Commodity prices

Commodity prices have an impact on several key economic variables, such as real GDP growth, GDP inflation, and the exchange rate. PBO's projection of the BCPI assumes that, after two years, real commodity prices will remain broadly unchanged. In contrast, the projection using energy and non-energy futures prices suggests that the BCPI will decline over the projection. Were this to be realized, the level of nominal GDP would be $26 billion below PBO's baseline projection in 2018 (Summary Table 3).

Summary Table 3

Nominal GDP Projections

billions of dollars

	2014	2015	2016	2017	2018
PBO April 2014	1,948	2,032	2,120	2,204	2,282
PBO using commodity price futures	1,953	2,034	2,116	2,187	2,256
Difference	5	2	-4	-16	-26

Sources: Office of the Parliamentary Budget Officer; Bloomberg.

Employment Insurance Revenues

As PBO discussed in EFOU 2013, the discretion granted to the Governor-in-Council for setting Employment Insurance rates introduces considerable uncertainty in the outlook for revenues. If the government were to set rates to balance premium revenues and forecast EI operating account expenditures, it could decrease the revenue outlook and the budget surplus by $2.2 billion in 2015-16 and $2.8 billion in 2016-17 (Summary Table 4).

Summary Table 4

Impact on outlook of break-even premium rates

billions of dollars

	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Budgetary balance (rate freeze)	-0.5	7.8	9.1	7.5	9.1
Budgetary balance (break-even)	-0.9	5.6	6.3	8.0	9.6
Difference	0.4	2.2	2.8	-0.5	-0.5

Source: Office of the Parliamentary Budget Officer.

Direct Program Expenses restraint

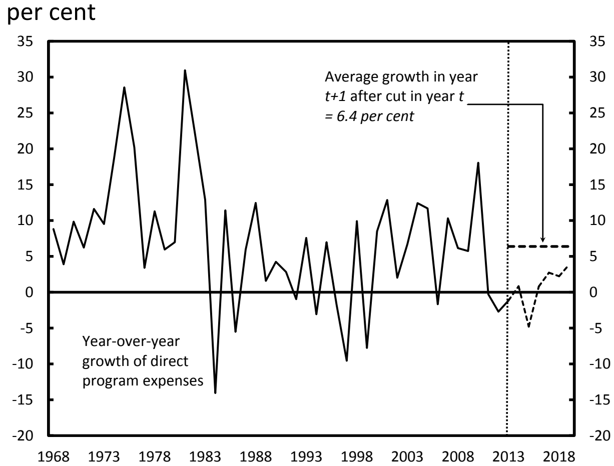
DPE will face significant pressure following the planned 2014-15 cuts. Such prolonged restraint has not been achieved in the history of the modern Public Accounts. Historically, a year of reductions is typically followed by a year of increases in DPE of around 6.4 per cent on average (Summary Figure 6). If the typical rebound from a period of DPE reductions were to occur in 2014-15 or 2015-16, it could eliminate the projected surplus in 2015-16.

PBO takes Finance Canada's projection for DPE as given, as the government has refused to release data required to assess if the current restraint is sustainable and to allow PBO to do its own projection of DPE.

Summary Figure 6

Historical and assumed DPE growth

per cent



Source: Office of the Parliamentary Budget Officer; Finance Canada.

1 External economic outlook

Global economic activity and trade picked up in the second half of 2013, as final demand in advanced economies increased at a steady pace while higher inventory investment surprised on the upside. In emerging market economies, solid export growth drove economic activity, outpacing more subdued growth in domestic demand.

As noted in the April 2014 International Monetary Fund (IMF) World Economic Outlook (WEO), global economic activity is expected to continue to improve in 2014 and 2015, with much of the strength coming from advanced economies, largely reflecting a reduction in fiscal tightening complemented by still highly accommodative monetary policy.

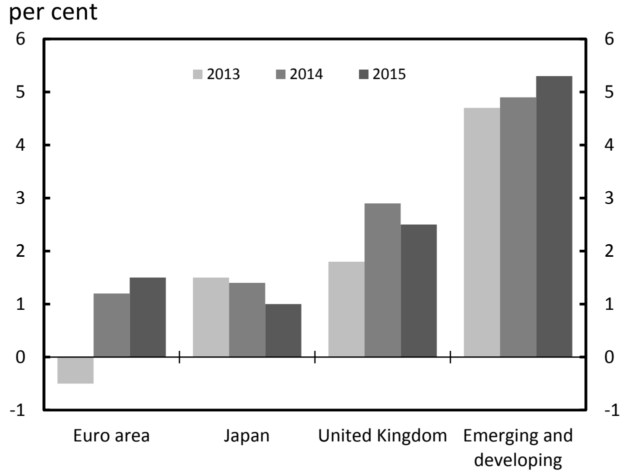
More specifically, while growth in the euro area is expected to strengthen, the recovery remains uneven as high debt (both public and private) and financial fragmentation put downward pressure on domestic demand in weaker peripheral countries (Figure 1-1). In the United Kingdom, economic activity has been buoyed by easier credit conditions and increased confidence spurring a rebound in household spending, although business investment and exports remain sluggish. In Japan, while some underlying growth drivers are expected to strengthen, notably private investment and exports, activity overall is projected to slow moderately in 2014 and 2015 in response to a tightening fiscal policy stance.

In emerging market and developing economies, growth is expected to increase in 2014 and 2015 from its modest pace in 2013, as many emerging market and developing economies benefit from stronger external demand in advanced economies. However, in many emerging market and developing economies, domestic demand has remained subdued, reflecting to varying degrees, tighter financial conditions and policy stances since mid-2013.

Figure 1-1

IMF Real GDP Growth Projections

per cent



Source: IMF April 2014 World Economic Outlook.

According to the IMF, downside risks to the global economy remain. In advanced economies, these include the reestablishment of normal monetary policy conditions, unfinished financial sector reforms, corporate debt overhang (particularly in some euro area economies), high government debt and related fiscal and financial risks. These are complemented by increased risks to activity associated with very low inflation, as longer-term inflation expectations risk drifting down further, possibly leading to deflation, the result of which would be higher real interest rates and weaker demand and output. In emerging market economies, increased financial market and capital flow volatility remain, particularly in light of the rapid normalization of monetary policy in the U.S. as the tapering of asset purchases continues through 2014. Finally, new geopolitical risks, particularly in Ukraine, have contributed additional uncertainty to the global economic outlook.

1.1 U.S. outlook

Despite the headwinds in 2013 created by fiscal drag in the U.S. stemming from the continued impact of sequestration and the U.S. government shutdown in the fall of 2013, growth in the second half of 2013 was much stronger than expected in October 2013. Specifically, growth in the third and fourth quarters of 2013 was 4.1 and 2.6 per cent, respectively, at annualized rates. As a result, for 2013 overall, U.S. real GDP advanced by 1.9 per cent – 0.3 percentage points stronger than projected by PBO in its October 2013 Economic and Fiscal Outlook Update (EFOU).

More recent indicators, however, suggest that the U.S. economy may grow at a more modest pace in the early part of 2014. Specifically, the housing market has begun to show some signs of cooling recently, with housing starts remaining below November 2013 levels and existing home sales falling in seven of the last eight months. Meanwhile, real personal consumption expenditures on goods have remained subdued recently, largely due to lower expenditures on durable goods. Nominal manufacturing shipments, wholesale trade, and retail sales have also been modest in recent months.

Looking to the labour market, the U.S. unemployment rate remains near post-recession lows. This can largely be attributed to a decline in the participation rate, which has only recently begun to rebound from the lowest levels observed since 1978, as employment growth has only just kept up with population growth (thereby maintaining the employment rate near its recessionary trough).[1]

Despite the stronger-than-expected growth in the second half of 2013 pushing into 2014, PBO has left its outlook for U.S. growth in 2014 unchanged at 2.7 per cent due to weaker-than-expected growth at the beginning of the year (Table 1-1). Meanwhile, growth over the remainder of the projection is broadly unchanged. This projection is similar to that of the Congressional Budget Office and private-sector economists.

Table 1-1

U.S. Real GDP Growth Projection

per cent

	2013	2014	2015	2016	2017	2018
October 2013 EFOU	1.6	2.7	3.4	3.6	3.3	2.6
April 2014 EFO	1.9	2.7	3.5	3.6	3.1	2.5

Sources: Office of the Parliamentary Budget Officer; Bureau of Economic Analysis.
Note: The 2013 value in the April 2014 EFO is the actual value.

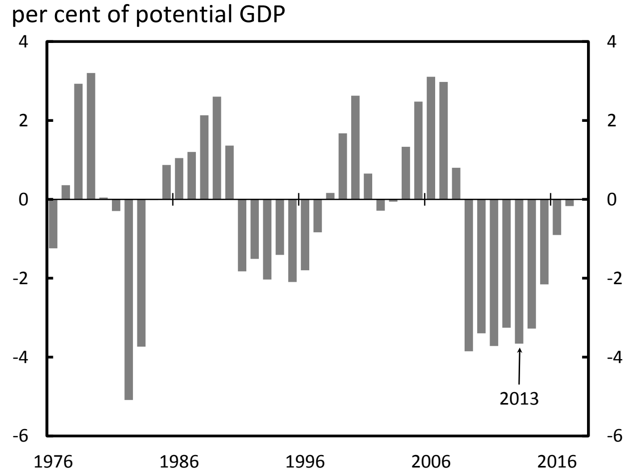
The medium-term projection also continues to assume that the U.S. Federal Reserve will maintain its policy interest rate at historic lows until the middle of 2015 while continuing to taper its asset purchases at a steady pace. This assumption is consistent with the target federal funds rate projections made by Federal Reserve Board members and Federal Reserve Bank presidents during the March 18-19 meeting of the Federal Open Market Committee.

Based on its updated growth outlook, PBO projects that the U.S. economy will remain below its potential GDP (i.e., maintain a negative output gap) over the medium term (Figure 1-2). The persistent and large output gap reflects the nature of the U.S. recovery, which has been characterized by continued balance sheet repair, persistently high unemployment, and fiscal consolidation.

Figure 1-2

U.S. Output Gap, 1976 to 2018

per cent of potential GDP



Sources: Office of the Parliamentary Budget Officer; Bureau of Economic Analysis.

[1] See CBO (2014) for an overview of the U.S. labour market. http://www.cbo.gov/sites/default/files/cbofiles/attachments/45011-LaborMarketReview.pdf.

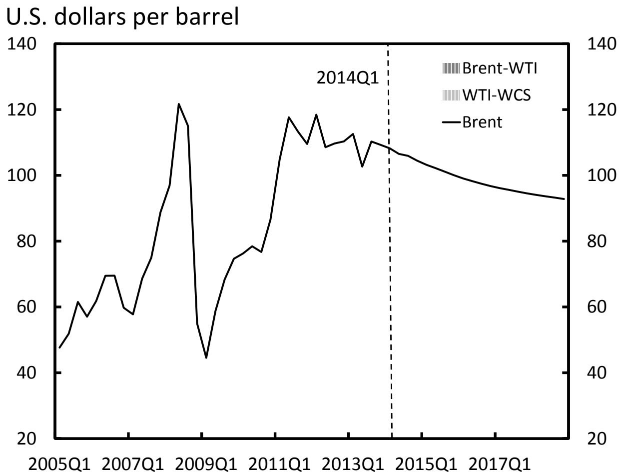
1.2 Commodity price outlook

Based on the Bank of Canada's Commodity Price Index (BCPI), non-energy commodity prices fell, on average, in the second half of 2013 while energy commodity prices increased.

The modest increase in energy prices through the first quarter of 2014 was largely due to an increase in the price of West Texas Intermediate (WTI) light, sweet crude oil, somewhat offset by a widening in the discount paid on Western Canadian Select (WCS) heavy crude oil (Figure 1-3). While this discount is expected to diminish over the projection, according to futures prices, it is not expected to return to the lows observed prior to the 2008-09 recession. Further, PBO does not expect this discount to disappear entirely at any point over the projection due to the higher cost of refining WCS crude into refined products relative to WTI as a result of its lower quality.[2]

Figure 1-3

Crude Oil Historic and Futures Prices, 2005Q1 to 2018Q4



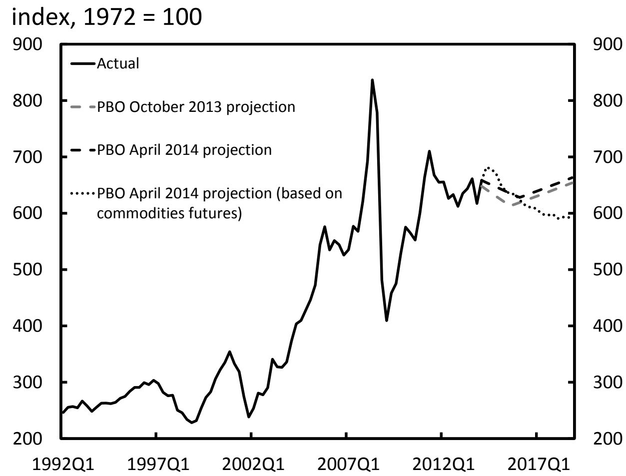
Sources: Office of the Parliamentary Budget Officer; Bloomberg.

The energy price growth at the end of 2013 was in line with the PBO October 2013 EFOU projection, while non-energy commodity prices were modestly weaker. As a result, the PBO outlook for commodity prices is little changed from the October 2013 EFOU projection (Figure 1-4).[3]

However, energy and non-energy futures prices suggest commodity prices will be much lower than the projections used in the April 2014 EFO and October 2013 EFOU, and therefore pose a potential risk to the outlook. This is largely the result of futures prices for crude oil indicating a modest but persistent decline, on average, from current prices. The decline in the price of crude oil over the projection is due, in part, to the expected increased supply of oil in North America as the proliferation of enhanced recovery technologies supports a large increase in oil production in the U.S. and elsewhere while also increasing the viability of some existing conventional formations.

Figure 1-4

Commodity Price Projection, 1992Q1 to 2018Q4



Sources: Office of the Parliamentary Budget Officer; Bank of Canada; Bloomberg.

More specifically, the PBO projection using energy and non-energy futures prices suggests that the level of nominal GDP will be $26 billion below PBO's current projection in 2018. As a result, the level of nominal GDP would be $8 billion lower than the current PBO projection, on average, if commodity futures prices were to be used.

[2] See PBO (2013) for more information. http://www.pbo-dpb.gc.ca/files/files/EFOU_October_2013_follow-up_EN.pdf.

[3] Annex A of the April 2013 EFO provides a detailed description of PBO's approach to projecting the Bank of Canada's energy commodity price index. A similar approach has been applied to the Bank of Canada's non-energy commodity price index.

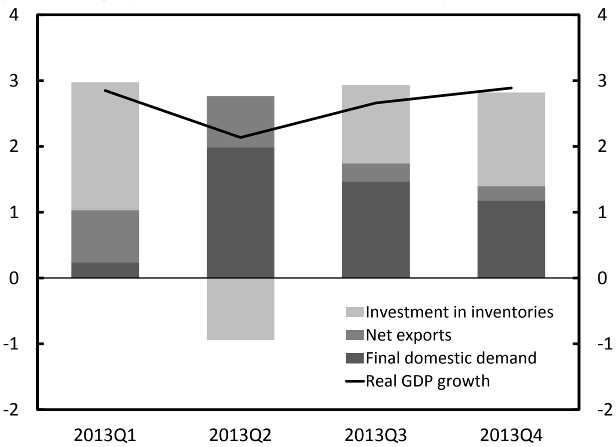
2 Canadian economic outlook

Real GDP growth in Canada picked up in 2013 from its sluggish pace in 2012. On an annual basis, real GDP advanced by 2.0 per cent in 2013, markedly higher than the 1.7 per cent increase observed in 2012. Underlying the 2013 real GDP growth were positive contributions from final domestic demand (1.4 percentage points), investment in inventories (0.3 percentage points), and net exports (0.3 percentage points) (Figure 2-1).

Figure 2-1

Contributions to Real GDP Growth in 2013

percentage points, annualized, quarter/quarter



Sources: Statistics Canada; Office of the Parliamentary Budget Officer.

Real GDP growth of 2.0 per cent in 2013 was 0.4 percentage points stronger than PBO projected at the time of the October 2013 EFOU. This reflected stronger growth in the second half of 2013 than expected in October 2013, as well as upward revisions to historical growth rates in the first half of 2013.[4,5] In contrast, GDP inflation of 1.2 per cent in 2013 was weaker than the 1.3 per cent projected in the October 2013 EFOU. Taken together, nominal GDP growth in 2013 (3.3 per cent) was higher than the 2.9 per cent projected in the October 2013 EFOU and the 2013 annual level of nominal GDP was $6.4 billion higher than projected.

2.1 Recent economic indicators

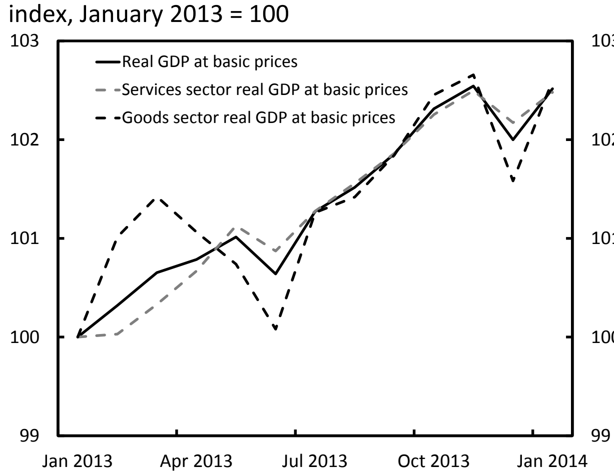
On balance, recent economic indicators suggest that real GDP growth in the first quarter of 2014 will be weak relative to the average quarterly growth observed through 2013.

Despite the 0.5 per cent decline in real GDP at basic prices in December 2013 resulting from the power outage in Ontario and more widespread effects of unseasonably cold weather across Canada, the 0.5 per cent increase in January 2014, combined with the solid growth posted from July 2013 to November 2013, resulted in a 2.5 per cent year-over-year increase in real GDP at basic prices from its January 2013 level (Figure 2-2). Underlying the year-over-year growth in real GDP at basic prices was a 2.5 per cent increase in real services output, with output increasing in all major services industries. Meanwhile, real goods output increased 2.6 per cent on positive but variable growth across all major goods industries, with the exception of construction which fell by 0.7 per cent over its January 2013 level of real output.

Figure 2-2

Monthly Real GDP at Basic Prices by Sector, January 2013 to January 2014

index, January 2013 = 100



Sources: Statistics Canada; Office of the Parliamentary Budget Officer.

Activity in the housing sector has been mixed since the third quarter of 2013. According to the Canada

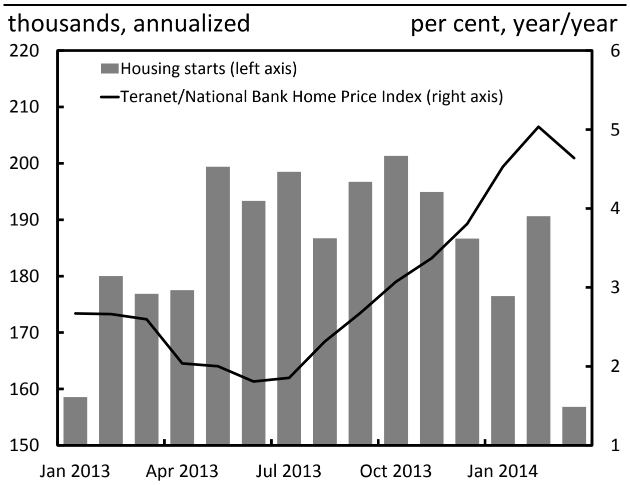
[4] Real GDP grew by 2.6 per cent, at annualized rates, in the second half of 2013 as opposed to the 2.0 per cent projected at the time of the October 2013 EFOU.

[5] Real GDP in the first half of 2013 was revised up to 2.2 per cent, at annualized rates, from 1.8 per cent at the time of the October 2013 EFOU.

Mortgage and Housing Corporation (CMHC), year-to-date housing starts in the first quarter of 2014 were broadly in line with the annual average observed in 2013 (Figure 2-3). This reflected resurgence in the construction of multi-family dwellings since early 2013, as growth in single-family housing starts moderated. Further, the Canadian Real Estate Association reports that sales activity in March 2014 was 4.9 per cent higher than year-ago levels. On a year-over-year basis, increases in existing home prices have resumed their solid pace of growth, increasing to 4.6 per cent in March 2014.

Figure 2-3

Housing Starts and Increases in Existing Home Prices, January 2013 to March 2014



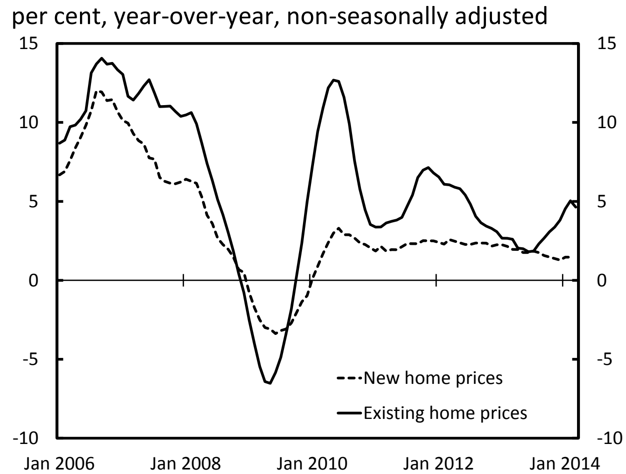
Sources: Canada Housing and Mortgage Corporation; Teranet/ National Bank.

Note: The Teranet/National Bank Home Price Index is the Composite 11 index (not seasonally adjusted). CMHC housing starts data are presented at seasonally adjusted, annualized levels.

However, when examined over a longer time period, PBO believes that risks associated with the housing sector continue to diminish, as signaled by the more modest growth in housing starts, residential mortgage credit, new home prices, and existing home prices over the past year relative to previous years (Figure 2-4).

Figure 2-4

Growth in Home Prices, January 2006 to March 2014



Sources: Office of the Parliamentary Budget Officer; Statistics Canada; Teranet/ National Bank.

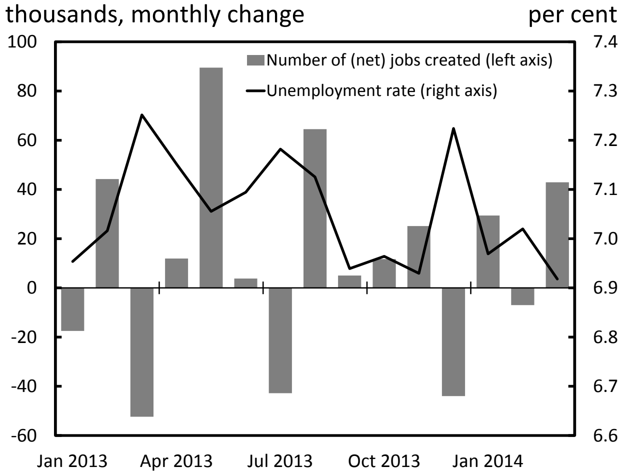
Note: New home prices refer to Statistics Canada's New Home Price Index and existing home price refer to the Teranet/National Bank Home Price Index Composite 11.

Despite solid real GDP growth through 2013, only 20,000 net new jobs were created in the second half of the year, with the majority of the 99,000 increase in employment in 2013 coming in the first half of the year (Figure 2-5). In contrast, roughly 65,000 net jobs have been created in the first three months of 2014. These recent gains have almost entirely been in full-time employment and in the private sector. Despite these employment gains, broadly unchanged levels of unemployment and the labour force (the sum of employed and unemployed Canadians) have left the unemployment rate broadly unchanged through the first quarter of 2014 at 7.0 per cent.[6]

[6] For more information on the state of the Canadian labour market, see PBO (2014). http://www.pbo-dpb.gc.ca/files/files/Labour_Note_EN.pdf.

Figure 2-5

Employment Gains and the Unemployment Rate, January 2013 to March 2014



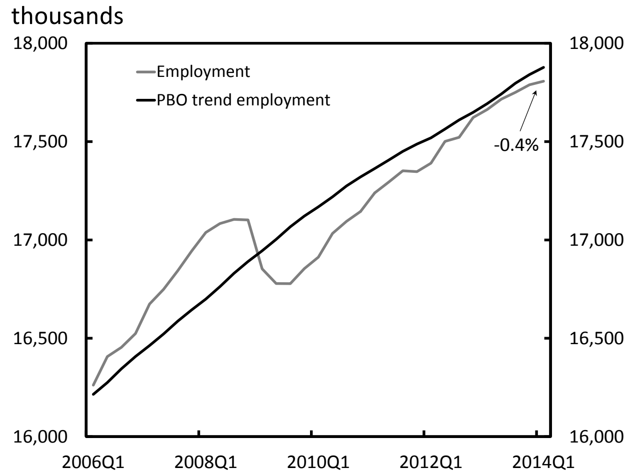
Sources: Statistics Canada; Office of the Parliamentary Budget Officer.

After taking account of the modest increase in employment in the first quarter of 2014, PBO estimates that employment in Canada was 0.4 per cent, or approximately 71,000 jobs, below its potential, or trend, level in the first quarter of 2014, pointing to continued slack in the Canadian labour market (Figure 2-6).[7]

It is also informative to examine average weekly hours worked since it, combined with employment, determines the total labour input into the production process. PBO estimates that average weekly hours worked continued to be below trend by about 0.4 per cent in the first quarter of 2014 (Figure 2-7). As a consequence of employment and average weekly hours remaining below trend, total labour input in the first quarter of 2014 was about 0.8 per cent below its trend level.

Figure 2-6

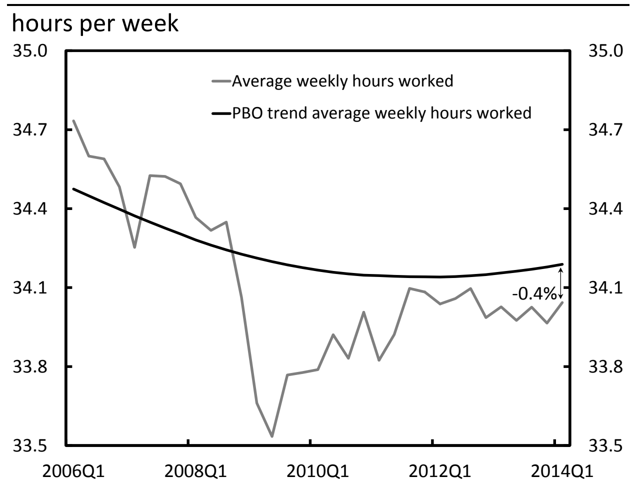
Employment, 2006Q1 to 2014Q1



Sources: Office of the Parliamentary Budget Officer; Statistics Canada.

Figure 2-7

Average Hours Worked, 2006Q1 to 2014Q1



Sources: Office of the Parliamentary Budget Officer; Statistics Canada.

Based on recent monthly indicators, PBO expects real GDP growth to moderate from 2.9 per cent (fourth quarter of 2013) to 1.5 per cent in the first quarter of the year. This deceleration largely reflects drag from inventory investment offsetting a robust expansion in final domestic demand, with an inconsequential contribution from net exports.

As a result of the weak economic growth expected in the first quarter of 2014, PBO estimates that the Canadian economy is currently 1.1 per cent below its level of potential GDP (Figure 2-8). This output gap of -1.1 per cent reflects contributions of

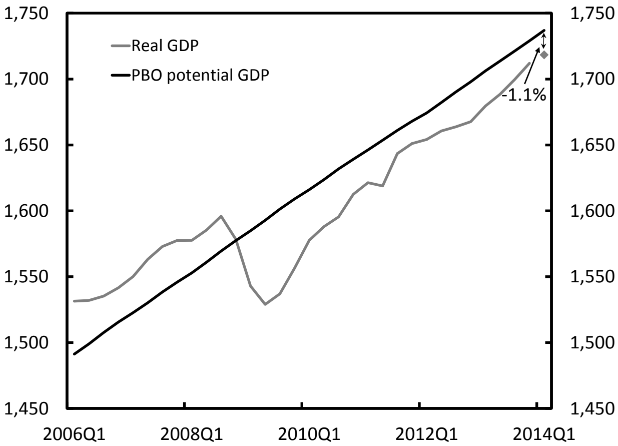
[7] Trends are taken from PBO's Fiscal Sustainability Report (FSR) 2013 (PBO (2013)). http://www.pbo-dpb.gc.ca/files/files/FSR_2013.pdf.

0.8 percentage points from total hours worked and 0.3 percentage points from labour productivity being below their respective trend levels.

Figure 2-8

Real GDP, 2006Q1 to 2014Q1

billions of chained (2007) dollars



Sources: Office of the Parliamentary Budget Officer; Statistics Canada.
Note: The estimate for real GDP in the first quarter of 2014 is based on growth of 1.5 per cent.

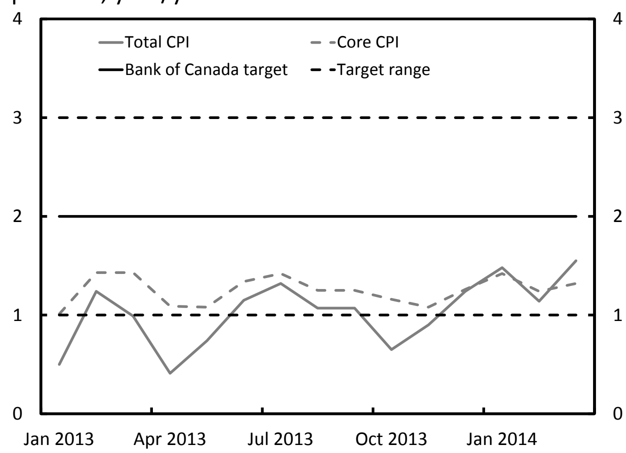
Further, since the onset of the recovery in late 2009, economic growth has modestly outpaced its potential growth rate and, as a result, the output gap has gradually narrowed, with approximately two-thirds of the gap being eliminated since the second quarter of 2009.

Consistent with the level of real GDP being below potential, consumer price index (CPI) inflation has remained below its 2 per cent target since April 2012, although it has generally remained within the target range of 1 to 3 per cent (Figure 2-9). As noted by the Bank of Canada in its March 2014 interest rate announcement, "Excess supply in the economy and competition in the retail sector will likely keep inflation well below the 2 per cent target this year."[8]

Figure 2-9

Total and Core Consumer Price Index (CPI) Inflation, January 2013 to March 2014

per cent, year/year



Sources: Statistics Canada; Bank of Canada.
Note: The core CPI index excludes eight of the most volatile components (fruit, vegetables, gasoline, fuel oil, natural gas, mortgage interest, inter-city transportation and tobacco products) as well as the effect of changes in indirect taxes on the remaining components.

Additionally, consumer prices have now increased by less than the 2 per cent Bank of Canada target for twenty-three consecutive months. As noted by the Bank of Canada in its April 2014 interest rate announcement, "With underlying inflation expected to remain below target for some time, the downside risks to inflation remain important."[9]

2.2 Medium-term outlook for the Canadian Economy

In addition to a broadly unchanged external outlook, the PBO projection for the Canadian economy has been updated to reflect the impact of measures in Budget 2014. On the whole, while Budget 2014 includes both stimulative measures (i.e., "actions to support jobs and growth") and savings measures (i.e., spending reductions and revenue increases), these measures are relatively small when compared to measures introduced in past federal budgets in recent years. However, when combined with the spending, savings and

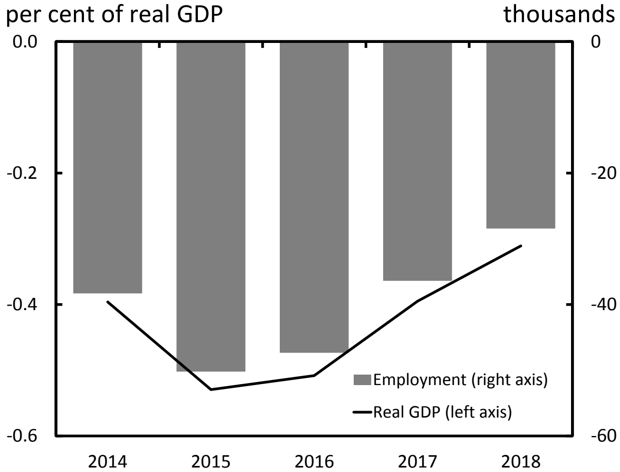
[8] http://www.bankofcanada.ca/wp-content/uploads/2013/11/fad-press-release-2014-03-05.pdf.

[9] http://www.bankofcanada.ca/wp-content/uploads/2014/04/fad-press-release-2014-04-16.pdf.

revenue measures, as well as revisions to spending levels, introduced beginning in Budget 2012, the projected level of real GDP is projected to be 0.5 per cent lower in 2016 than would have been the case in the absence of these measures (Figure 2-10).[10] Further, this economic impact translates into about 46,000 fewer jobs being created by 2016.

Figure 2-10

Economic Impacts of Budget Measures since Budget 2012



Source: Office of the Parliamentary Budget Officer.
Note: The estimated impacts on real GDP and employment do not include changes to employment insurance premiums or take into account offsetting impacts from changes to interest and exchange rates. Impacts are expressed relative to PBO's current projection.

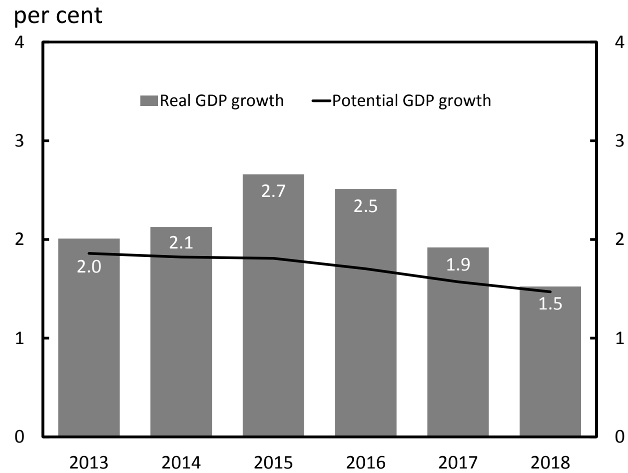
PBO's estimate of the overall employment impact – amounting to a reduction of 46,000 jobs in 2016 – does not mean that PBO expects that, going forward, there will be a decline of 46,000 jobs from the current level of employment (17.8 million jobs as of March 2014). Rather, it means that, in the absence of these savings and revenue measures and revisions to spending levels, projected employment would be higher by 46,000 jobs, all else being equal.

Economic Outlook

PBO projects real GDP growth in Canada to accelerate to 2.1 per cent in 2014 and remain above its potential growth rate until 2018 (Figure 2-11). This solid growth is the result of higher domestic and external demand, offset by government spending reductions and restraint acting as a drag on output and job creation going forward. The deceleration in the growth rate of potential GDP is attributed to the aging Canadian labour force.

Figure 2-11

Real GDP and Potential GDP Growth



Sources: Office of the Parliamentary Budget Officer; Statistics Canada.

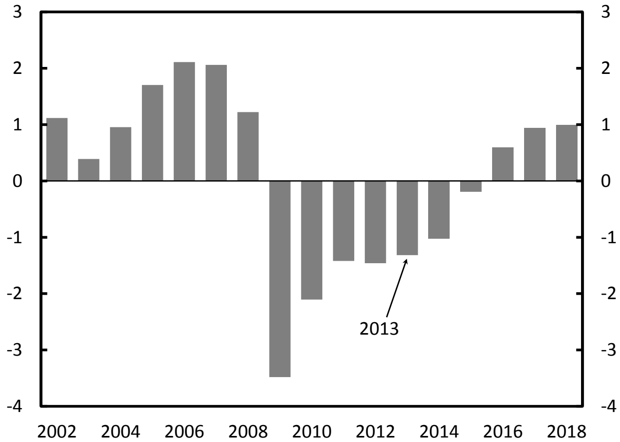
The measures and revisions to spending levels since Budget 2012 have pushed the economy further away from its potential GDP and delayed the economic recovery (Figure 2-12). PBO projects the economy to fully recover (i.e., return to its potential GDP) by mid-2015. After 2015, the output gap is expected to increase to 1.0 per cent in 2018, with the level of real GDP converging to potential GDP thereafter.

[10] For additional background on the PBO methodology for estimating the economic impacts of fiscal policy measures, see Annex A in the April 2012 EFO available at: http://www.pbo-dpb.gc.ca/files/files/Publications/EFO_April_2012.pdf.

Figure 2-12

Output Gap, 2002 to 2018

per cent of potential GDP



Sources: Office of the Parliamentary Budget Officer; Statistics Canada.

PBO's current projection of real GDP growth in 2014 is slightly higher than its October 2013 projection (Table 2-1). This reflects the stronger-than-expected growth in the second half of 2013 and slightly more favourable external outlook, offset by continued government spending reductions and restraint. Over the remainder of the projection horizon, PBO's real GDP growth projection is essentially unchanged from the October 2013 EFOU. Annex A provides a summary table of PBO's current economic projections and comparison to the October 2013 EFOU projections.

Table 2-1

Real GDP Growth Projection

per cent

	2013	2014	2015	2016	2017	2018
October 2013 EFOU	1.6	2.0	2.6	2.6	1.9	1.5
April 2014 EFO	2.0	2.1	2.7	2.5	1.9	1.5

Sources: Office of the Parliamentary Budget Officer; Statistics Canada.
Note: The 2013 value in the April 2014 EFO is the actual value.

Largely as a result of stronger-than-expected real GDP growth in 2013, projected levels of nominal GDP are about $11 billion higher, on average, than the projected levels in the October 2013 EFOU (Table 2-2).

Table 2-2

Nominal GDP Projection

billions of dollars

	2013	2014	2015	2016	2017	2018
October 2013 EFOU	1,873	1,937	2,017	2,110	2,193	2,270
April 2014 EFO	1,879	1,948	2,032	2,120	2,204	2,282

Sources: Office of the Parliamentary Budget Officer; Statistics Canada.
Note: The 2013 value in the April 2014 EFO is the actual value.

Also as a result of the stronger-than-expected growth in real GDP in 2013, the unemployment rate was lower than expected in the October 2013 EFOU, and will continue to be lower over the projection (Table 2-3).

Table 2-3

Unemployment Rate Projection

per cent

	2013	2014	2015	2016	2017	2018
October 2013 EFOU	7.2	7.3	7.0	6.5	6.3	6.1
April 2014 EFO	7.1	7.0	6.8	6.4	6.1	6.0

Sources: Office of the Parliamentary Budget Officer; Statistics Canada.
Note: The 2013 value in the April 2014 EFO is the actual value.

Owing to the sluggish pace of the economic recovery, and given the firm anchoring of inflation expectations[11], PBO expects the Bank of Canada to maintain its policy interest rate at 1 per cent until the second quarter of 2015 before gradually, but steadily, raising its policy rate over the remainder of the projection (Table 2-4). This projection is in line with the stated policy of the U.S. Federal Reserve and is similar to the projection provided in the October 2013 EFOU.

[11] http://www.bankofcanada.ca/wp-content/uploads/2014/04/bos-spring2014.pdf.

Table 2-4

3-month Treasury Bill Rate Projection

per cent

	2013	2014	2015	2016	2017	2018
October 2013 EFOU	1.0	1.0	1.4	2.8	4.0	4.2
April 2014 EFO	1.0	1.0	1.4	2.5	3.5	4.2

Sources: Office of the Parliamentary Budget Officer; Statistics Canada.
Note: The 2013 value in the April 2014 EFO is the actual value.

2.3 Risks to the private sector economic outlook

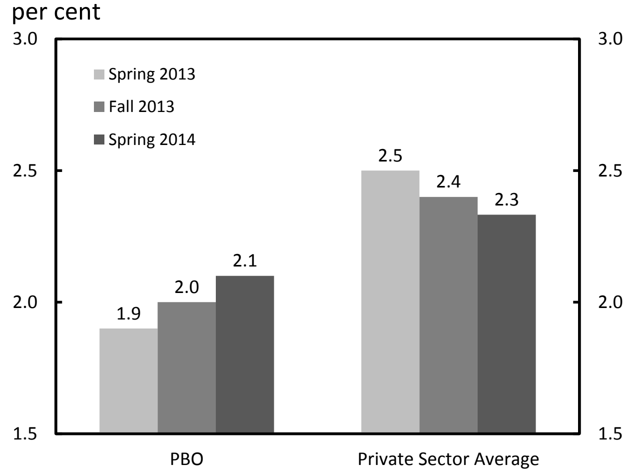
PBO's economic outlook incorporates its judgment of the balance of risks. As a result, it can be viewed as a "balanced" projection, which means that higher or lower outcomes are equally likely. Further, PBO uses its outlook to highlight what it believes are the key risks to the private sector economic outlook on which the Government's fiscal projections are based.

Since the release of PBO's October 2013 EFOU, private sector forecasters have modestly revised down their outlook for real GDP growth in 2014, bringing the average forecast more into line with PBO's projection (Figure 2-13). In contrast, PBO has revised up its 2014 real GDP growth projection since October 2013, in large part as a result of stronger-than-expected momentum from the second half of 2013.

Figure 2-13

Evolution of 2014 Real GDP Growth Projections

per cent



Sources: Office of the Parliamentary Budget Officer; Finance Canada.
Note: PBO estimates that adjusting the private-sector average projection for the most recent National Accounts data would result in 2014 real GDP growth being elevated to around 2.5 per cent from 2.3 per cent.

Compared to the average private sector forecast in Finance Canada's December 2013 survey (reported in Budget 2014), PBO is projecting lower real GDP growth in 2014 (Table 2-5) and lower GDP inflation in 2014 through 2016. After 2016, PBO is projecting lower real GDP growth as the Canadian economy returns to its level of potential GDP, while its projection of GDP inflation matches that of Finance Canada. Consequently, over the projection horizon, PBO's outlook for nominal GDP – the broadest measure of the Government's tax base – is lower, by $17 billion annually, on average, than the projection based on private sector forecasts (Table 2-6).[12] Annex B provides a comparison table of PBO's projections and the average private sector economic forecasts from Budget 2014.

[12] The private-sector outlook for nominal GDP based on the average of private-sector forecasts of real GDP growth and GDP inflation published in December 2013 is higher than the Budget 2014 fiscal planning assumption for nominal GDP, which adjusted downward the December 2013 private sector outlook by $20 billion annually over the period 2014 to 2018.

Table 2-5

Real GDP Growth Projections

per cent

	2014	2015	2016	2017	2018
PBO April 2014	2.1	2.7	2.5	1.9	1.5
Finance Canada December 2013 survey	2.3	2.5	2.5	2.3	2.2

Sources: Office of the Parliamentary Budget Officer; Finance Canada.

Table 2-6

Nominal GDP Projections

billions of dollars

	2014	2015	2016	2017	2018
PBO April 2014	1,948	2,032	2,120	2,204	2,282
Finance Canada December 2013 survey	1,952	2,040	2,132	2,226	2,320
Budget 2014 planning assumption	1,932	2,020	2,112	2,206	2,300

Sources: Office of the Parliamentary Budget Officer; Finance Canada.

Consequently, PBO judges that the balance of risks to the average private sector forecast for nominal GDP is slightly tilted to the downside, reflecting both weaker real GDP growth and GDP inflation. This likely reflects larger negative impacts from savings measures and revisions to spending levels since Budget 2012 than assumed in the private-sector forecast, as well as differences in views on commodity prices and their impacts on real GDP growth and GDP inflation.

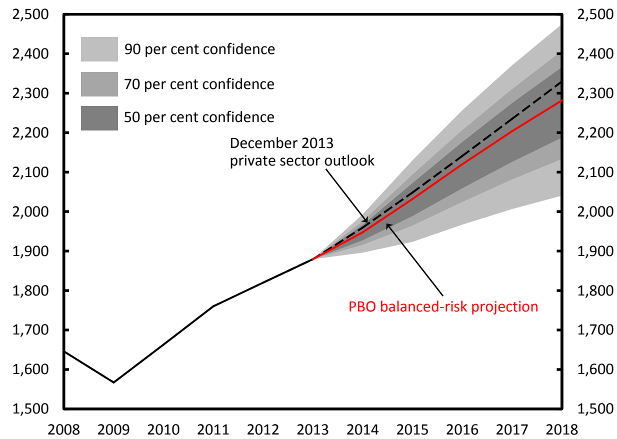
This said, PBO views the average private-sector outlook as being subject to less downside risk than was the case for Budgets 2012 and 2013. In fact, the Budget 2014 nominal GDP level projection, which consists of the private-sector average projection less a $20 billion risk adjustment for each year of the projection, is lower, by $3 billion annually, on average, than the PBO projection.

To illustrate the uncertainty and balance of risks to the private sector forecast of nominal GDP in Finance Canada's December 2013 survey, PBO constructed a fan chart based on the historical forecast performance of Finance Canada's survey of private sector forecasters since 1994 (Figure 2-14).

Figure 2-14

Nominal GDP Projections

billions of dollars



Sources: Office of the Parliamentary Budget Officer; Finance Canada; Statistics Canada.

Based on its projection of nominal GDP, PBO judges that the downside risk to the private sector outlook for nominal GDP is broadly in line with the Government's $20 billion annual adjustment for risk. Over the period of 2014 to 2018, PBO's nominal GDP projection is about $17 billion lower annually, on average, than the private sector forecast based on Finance Canada's December 2013 survey. After accounting for the Government's adjustment for risk, PBO's projected nominal GDP is $3 billion (0.1 per cent) higher annually, on average, than the Budget 2014 planning assumption for nominal GDP.

3 Fiscal outlook

PBO has revised its medium-term fiscal outlook for the federal government to include the latest economic projections and fiscal developments.[13] Full fiscal tables, along with comparisons to PBO's EFOU 2013 outlook and Budget 2014, are provided in Annexes C, D, and E.

[13] Prior to this document, PBO's latest fiscal outlook was published in the Revised Economic and Fiscal Outlook 2013, available at http://www.pbo-dpb.gc.ca/files/files/Revised_EFOU_2013.pdf. This outlook included the impact of measures and estimates in Finance Canada's Update of Economic and Fiscal projections 2013. References to PBO's EFOU 2013 refer to these revised projections.

PBO's fiscal outlook is based on government policy announced in Budget 2014, the Public Accounts of Canada 2012-13, Finance Canada's monthly financial statistics bulletins up to January 2014, and other public reports and information supplied by federal departments.

Prospects for budgetary surpluses are higher over the outlook than in PBO's December fiscal update due to the revised economic outlook and measures in Budget 2014. A summary of PBO's projection of the federal government's operations is given in Table 3-1.

Table 3-1

Summary statement of operations

billions of dollars

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Budgetary revenues	268.3	280.0	297.1	310.4	320.3	332.5
Program expenses	251.0	250.7	258.7	267.8	276.0	284.5
Public debt charges	28.9	29.8	30.5	33.4	36.8	38.9
Budgetary balance	-11.6	-0.5	7.8	9.1	7.5	9.1
Federal debt	614.0	614.5	606.7	597.6	590.1	580.9
Per cent of GDP						
Budgetary revenues	14.3	14.4	14.6	14.6	14.5	14.6
Program expenses	13.4	12.9	12.7	12.6	12.5	12.5
Public debt charges	1.5	1.5	1.5	1.6	1.7	1.7
Budgetary balance	-0.6	0.0	0.4	0.4	0.3	0.4
Federal debt	32.7	31.6	29.9	28.2	26.8	25.5

Source: Office of the Parliamentary Budget Officer.

PBO estimates that the budgetary deficit will be 0.6 per cent of GDP in 2013-14 and will be balanced in 2015-16, maintaining an average surplus of 0.4 per cent of GDP over the remainder of the outlook. The return to balance is possible mainly through economic growth and a $5.7 billion decrease in budgeted direct program expenses in 2014-15.

Federal debt (accumulated deficit) is projected to grow at a slower rate than GDP in 2013-14 and 2014-15, and decline both as a share of GDP and in nominal terms as budgetary surpluses accumulate in 2015-16 and beyond.

A budgetary surplus could be achieved in 2014-15 (one-year earlier than the government's target) if one or more of the following uncertainties are realized:

- PIT revenues rebound in 2014-15 at a higher rate than expected.
- Departments underspend (lapse) at a similar rate as fiscal years 2009-10 to 2012-13 (over 8 per cent of appropriations).

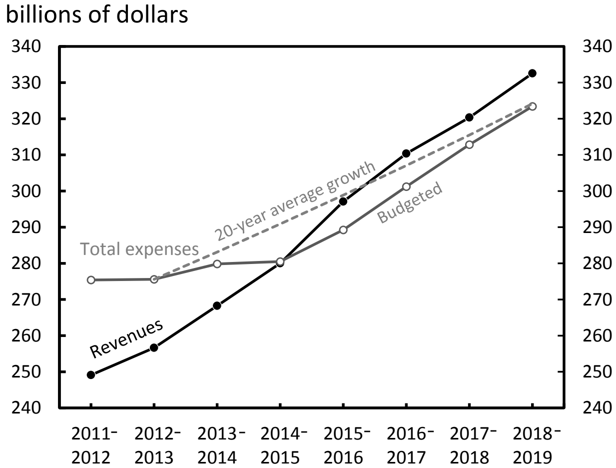
Conversely, returning to surplus in 2015-16 would be challenging under a combination of the following scenarios:

- Budgeted direct program expenses cuts prove unsustainable.
- EI premium rates are set at the operating account breakeven rate in 2015 and 2016.
- Planned asset sales are not realized.

The most significant risk to the government's 2015-16 balanced budget target is the outlook for direct program expenses (DPE). The government's plan in 2014-15 includes the greatest year-over-year reduction of direct program expenses since 1998-99. If DPE savings do not materialize as planned, a budgetary surplus is likely to still be achieved in 2016-17 through revenue growth, which is projected to exceed the 20-year historical growth rate of total expenses (Figure 3-1). More background on the uncertainty surrounding this restraint is provided in Subsection 3-7.

Figure 3-1

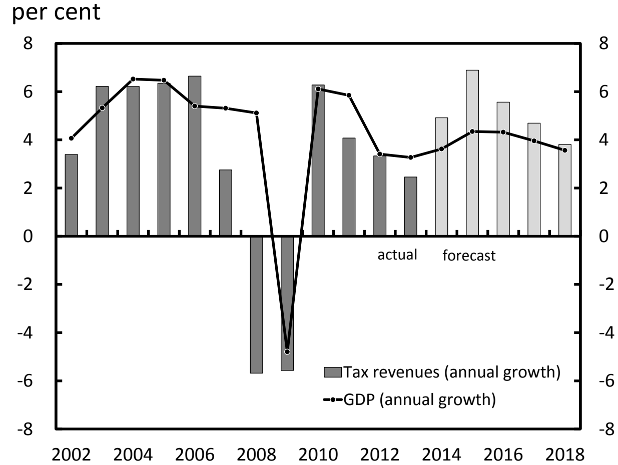
Outlook for revenues and expenses



Source: Office of the Parliamentary Budget Officer.

Figure 3-2

Tax revenues and GDP growth



Sources: Office of the Parliamentary Budget Officer; Finance Canada.

3.1 Economic growth and the budget outlook

The fiscal outlook is based on PBO's projections for nominal output (both real economic growth and price movements), the incomes accruing to different agents of the economy (individuals and corporations), and how income is spent (household consumption, saving, and the choice between domestic and foreign consumption).

Growth in tax revenues closely follows the growth of nominal GDP (Figure 3-2). Revenue growth often exceeds GDP growth during economic expansions (and is projected to do so over 2014-15 and 2015-16 as the economy returns to potential). This is mostly due to *bracket creep*, where tax revenues increase at a faster rate than incomes because certain properties of a progressive tax system—such as income tax thresholds, credits, and deductions—are not fully indexed to real income growth and inflation.

The response of revenues to GDP growth contributes significantly to the prospects of the federal budgetary balance. PBO estimates that about 45 per cent of the projected improvement in the budgetary balance over 2014-15 and 2015-16 is attributable to revenue increases from the growth of nominal GDP and its components.

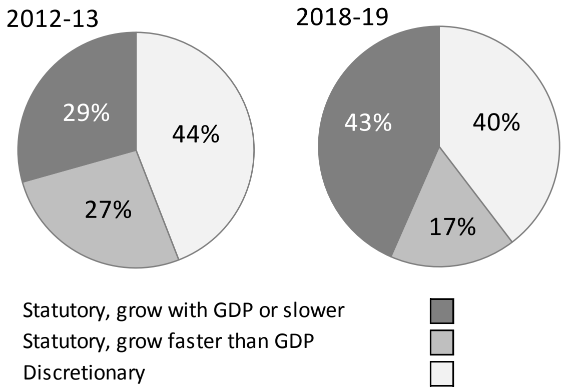
Government spending is influenced both directly and indirectly by economic growth. GDP influences spending directly through formula funding arrangements with provinces and territories that escalate annually with the rate of growth of GDP. For these transfers, higher GDP growth will increase expenses roughly one-to-one. The economic outlook also affects spending indirectly through inflation, wages, and the labour market.

The structural relationship between expenses and economic growth has been reformed significantly in recent years. Changes to transfer arrangements, particularly decreasing the CHT escalator from 6 per cent to a moving average of GDP growth, will increase the share of expenses which grow with GDP or at a slower rate than GDP from 29 per cent in 2012-13 to 43 per cent in 2018-19 (Figure 3-3).

Figure 3-3

Program expenses and economic growth

per cent of program expenses



Sources: Office of the Parliamentary Budget Officer; Finance Canada.
Note: Expenses in 2018-19 which grow faster than GDP are primarily elderly benefits.

CHT reform, combined with transfers which are indexed below GDP growth (e.g. CST is escalated at 3 per cent per year, the Gas Tax Fund is escalated at 2 per cent per year, and the Universal Child Care Benefit is not indexed), restrains the growth of total program expenses to less than the rate of GDP and contributes significantly to the budget balance in 2017-18 and beyond.

3.2 Budgetary measures

PBO adjusted its fiscal projection to account for the estimates of the impact of tax and spending measures announced in Budget 2014. The fiscal impacts were scaled to PBO's projection of tax bases and economic growth where appropriate. The impact of measures on the budgetary balance is presented in Table 3-2.

Table 3-2

Fiscal impact of Budget 2014 policy decisions

millions of dollars

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
PIT	6	-27	78	93	98	108
CIT	0	0	303	300	282	290
NRIT	0	0	0	0	0	0
GST/HST	0	-10	-10	-10	-10	-10
Custom import duties	0	0	0	0	0	0
Other excise taxes	96	686	662	642	620	596
Public debt charges	0	-5	-15	-21	-27	-33
Direct program expenses	1,517	1,327	1,188	1,078	-88	-576
Total	1,620	1,971	2,206	2,083	875	376

Sources: Office of the Parliamentary Budget Officer; Finance Canada.
Note: Budget measures were adjusted for PBO's economic outlook and for the PSHCP agreement reached on March 26, 2014.

The most significant revenue measure was an increase in tobacco duty which contributes an additional $0.6 billion to $0.7 billion per year to the budgetary balance. The government's decision to index the taxation of tobacco helps slow the erosion of excise taxes in the tax mix (Box 1).

The main impact on program spending comes from two measures: a re-profiling of National Defence capital spending, and changes to the contribution rate of retired public servants to the Public Sector Health Care Plan (PSHCP).

The entire impact of the re-profiling of National Defence capital spending is recorded in operating expenses under the fiscal framework. In future years beyond the outlook, the budgeted funds will be allocated between operating and capital amortization, as plans for the acquisition of machinery and equipment for the Canada First Defence Strategy are finalized.

Box 1: Protecting revenues and the tax mix by indexing excise taxes.

Budget 2014 included a measure to adjust the rate of specific (per unit) tobacco duties in 2014 to account for inflation.

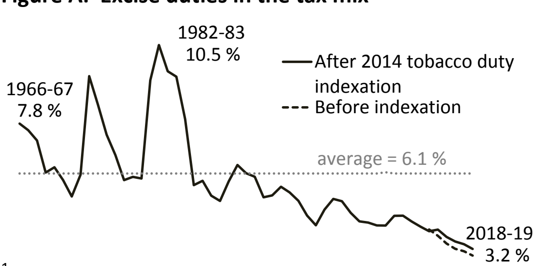
Ensuring specific taxes on tobacco keep up with the increase in the price level prevents the real cost of tobacco products from falling and also preserves excise taxes in the mix of government revenues.

The share of excise taxes in the government's tax mix has been falling over history, as the real value of specific taxes is eroded by inflation (see Figure A). By 2018-19, excise taxes are projected to contribute roughly one-half of their average historical share of government revenues, despite increasing consumption of alcohol and road fuels which outweighs declining tobacco sales.

Other specific taxes on road fuels and alcohol consumption could benefit from indexation for similar goals of preventing real price decreases and protecting the tax mix. For example, the 10 cent per litre duty on road fuels has not changed since 1995. Had the excise tax on road fuels kept up to inflation, it would now be 14 cents and bring in an additional $1.5 billion of revenue (assuming a price elasticity of demand of -0.2).[1]

The declining importance of excise duties, which economic theory suggests have low or negative deadweight burdens of taxation (the economic costs of distorting market behaviour), means relatively more revenue must come from taxes with higher deadweight burdens such as personal and corporate income taxes.[2]

Figure A: Excise duties in the tax mix[3]



[1] This is an average of short and long-run elasticities compiled in a review of peer-reviewed research.

[2] For an overview of the trade-offs between taxing incomes and taxing commodities with externalities such as alcohol and road fuels, see the Institute for Fiscal Studies, *Mirrlees Review* (2010), available at http://www.ifs.org.uk/mirrleesReview.

[3] Source: Finance Canada *Fiscal Reference Tables October 2013;* Office of the Parliamentary Budget Officer.

The government has implemented a measure to increase the contribution rate of retired public servants to the PSHCP from 25 per cent to 50 per cent, initially estimated to reduce expenses by $7.3 billion over the outlook. PBO has adjusted the government's initial estimate of the measure to reflect the agreement reached on March 26, 2014. The measure is now estimated to reduce the accrued liability of the government's share of future contributions by $6.7 billion. At the end of the 2012-13 fiscal year, this liability was $19.7 billion. The reduction in the liability will be spread over 7 years beginning 2013-14, although the plan will not begin to be phased in until January 2016.

While the changes to the Public Sector Health Care Plan have a large impact on its accrued future liability, and a significant impact on the immediate annual budgetary balance profile (an average of $1.2 billion per year over 2013-14 to 2018-19), it has only a small impact on a cash basis. PBO estimates the cash savings will be roughly $0.2 billion per year from 2016-17 over the remainder of the outlook.[14]

Figure 3-4 shows the measures of Budget 2014 in context with previous budgets. While the net impact was small compared to previous budgets, the total value of measures was roughly average compared to other post-recession budgets.

Two additional fiscal developments were announced following Budget 2014: the auction of the 700-MHz frequency wireless spectrum, and the South Korea free trade agreement. PBO has included both measures in the projection; however, their impact is negligible.

Proceeds from the wireless spectrum auction are large ($5.3 billion); however, the annual accrued impact on the budget is small ($264 million) as revenues from the sale are accrued over the 20-year term of the contract. Further, provisions for the sale were already included in the outlook in 2014-15 and 2015-16 as part of the asset sales

[14] The contributions of public servants to the PSHCP were $195 million in 2012-13. A doubling of contribution rates in 2016-17 (from 25% to 50%) are assumed to double receipts, with a corresponding decrease in the government's contributions.

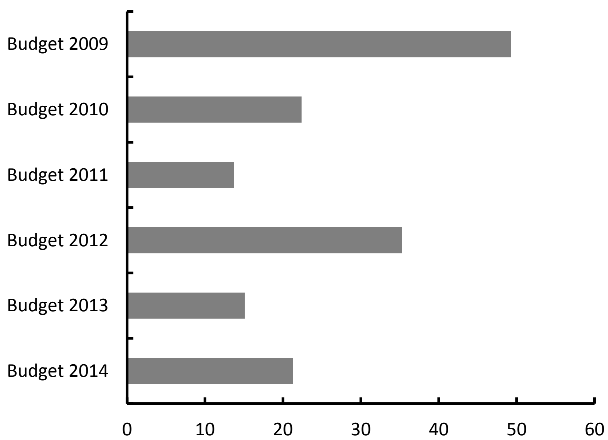
planning assumptions which Finance Canada included in the fall update.

Though details of the trade agreement with South Korea are limited, PBO estimates imports from South Korea to be roughly $5.0 billion per year.[15] If the cost to the fiscal framework of removing tariffs on South Korean imports is comparable to the cost of removing tariffs as part of the Comprehensive European Trade Agreement, then the fiscal impact would be roughly $50 million (adjusted for trade volume).

Figure 3-4

Total value of budget measures

billions of dollars



Source: Finance Canada.
Note: Absolute value of measures.

3.3 Year-to-date revenues and expenses

With 10 months of Finance Canada's statistics bulletins (the Fiscal Monitor) available for fiscal year 2013-14, PBO can assess trends in revenues and expenses to construct an in-year estimate of government operations. Remaining months are estimated using PBO's economic outlook and the annual totals are adjusted for average end-of-year accounting and accruals corrections. Table 3-3 compares PBO's in-year estimate for 2013-14 to the 2012-13 public accounts.

[15] Korean Statistical Information Service (KOSIS); exchange rate on April 12, 2014. http://kosis.kr/statHtml/statHtml.do?orgId=360&tblId=DT_1R11006_FRM101&conn_path=I2&language=en

Revenues are estimated to have grown by 4.5 per cent over 2013-14, which is higher than the past two years, but lower than expected given the historical relation to nominal GDP growth. Finance Canada projected revenue growth of 2.9 per cent in 2013-14, after a risk adjustment.

Table 3-3

In-year estimate 2013-14

billions of dollars, unless noted otherwise

	Actual 2012-13	Estimate 2013-14	Change $	Growth %
Income taxes				
Personal income tax	125.7	130.5	4.8	3.8
Corporate income tax	35.0	34.2	-0.8	-2.2
Non-resident income tax	5.1	6.2	1.1	22.2
Total income tax	165.8	170.9	5.2	3.1
Excise taxes/duties				
Goods and Services Tax	28.8	30.9	2.1	7.1
Custom import duties	4.0	4.3	0.3	7.1
Other excise taxes/duties	10.8	10.6	-0.1	-1.1
Total excise taxes/duties	43.6	45.8	2.2	5.1
EI premium revenues	20.4	22.2	1.8	8.7
Other revenues	26.9	29.4	2.5	9.2
Total budgetary revenues	**256.6**	**268.3**	**11.6**	**4.5**
Major transfers to persons				
Elderly benefits	40.3	41.6	1.4	3.4
Employment Insurance benefits	17.1	17.0	-0.1	-0.7
Children's benefits	13.0	13.2	0.2	1.7
Total	70.3	71.8	1.5	2.1
Major transfers to OLG	58.4	60.4	2.0	3.5
Direct program expenses	117.7	118.8	1.1	0.9
Public debt charges	29.2	28.9	-0.3	-1.0
Total expenses	**275.6**	**279.8**	**4.3**	**1.6**
Budgetary balance	**-18.8**	**-11.6**	**7.2**	**-38.5**

Sources: Office of the Parliamentary Budget Officer; Finance Canada.
Note: Direct program expenses have been adjusted for the revised PSHCP agreement.

Revenue from personal income taxes (PIT) was weak over the first ten months of the fiscal year, despite relatively strong household income. PIT revenue is expected to recover over February and March due to bracket creep, as 2014 income tax brackets were indexed by the very low level of inflation over the 12-month period ending September 30, 2013 (0.9 per cent).

Revenue from corporate income tax (CIT) has been lower in 2013-14 relative to the same period in 2012-13 and is estimated to fall by 2.2 per cent for the year as a whole. Low CIT revenues were expected due to low corporate profits in the first two quarters of 2013 and a subsequent slow recovery.

Year-to-date revenue from non-residents income tax has already surpassed the 2012-13 public accounts annual total and the annual total budgeted by Finance Canada for 2013-14. If the trend continues over the remaining months, non-residents income tax will be 22.2 per cent higher for the year as a whole.

EI premium revenues and other revenues have been high relative to 2012-13 and PBO's estimate in EFOU 2013, growing much faster than nominal GDP. PBO estimates they will grow by 8.7 per cent and 9.2 per cent, respectively, for the year as a whole.

Direct program expenses grew by 2.9 per cent over the first 10 months of 2013-14, which is more than the 0.8 per cent which is budgeted by Finance Canada and which PBO assumes for its outlook (this assumption appears in Table 3-2). Direct program expenses are historically very volatile in the last two months of the fiscal year, and are typically affected by large end-of year accounting revisions. For this reason, year-to-date data is a poor indication of final totals, and PBO defers to the government's estimate.

Combined, the year-to-date monitoring of revenues and expenses suggests the budgetary balance has improved considerably relative to 2012-13 and is on track to end the year at $11.6 billion (0.6 per cent of GDP). This is a $5.0 billion improvement compared to Finance Canada's estimate of $16.6 billion.

The in-year estimate is only a rough indication of final fiscal aggregates for 2012-13, which will not become known until the Public Accounts of Canada 2014 are tabled in the fall. Fiscal Monitor reporting methodology and classifications change frequently—most recently in April 2013. A short history of consistent data, end-of-year accounting adjustments, and significant volatility in the final months of the fiscal year limit the predictive power of Finance Canada's monthly statistics as an indicator of fiscal performance for the year.

3.4 Medium-term outlook for budgetary revenues

PBO estimates federal budgetary revenues will increase as a share of GDP from 14.3 per cent in 2013-14 to 14.6 per cent in 2015-16. Most of the increase comes from PIT revenues, which are expected to increase by 6.5 per cent annually over the next two years.

From 2015-16 to 2018-19, revenues are expected to decline slightly as a share of GDP, due to lower customs duties from the Canada-European Union Comprehensive Economic and Trade Agreement starting in 2015, EI premium rate cuts in 2017, and lower excise taxes, which are not indexed to inflation. Table 3-4 provides a breakdown of the outlook for individual revenues.

Table 3-4

Outlook for revenues

billions of dollars

	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Income taxes					
Personal income tax	138.6	147.4	155.2	162.4	168.9
Corporate income tax	36.0	39.5	42.1	44.5	46.3
Non-resident income tax	6.0	6.5	7.0	7.2	7.5
Total income tax	180.6	193.3	204.3	214.2	222.7
Excise taxes/duties					
Goods and Services Tax	31.9	33.5	34.8	36.1	37.3
Custom import duties	4.6	4.9	4.6	4.7	4.9
Other excise taxes/duties	11.3	11.3	11.3	11.4	11.3
Total excise taxes/duties	47.8	49.7	50.8	52.2	53.5
EI premium revenues	22.7	23.7	23.4	20.6	21.4
Other revenues	28.9	30.3	31.9	33.3	34.8
Total budgetary revenues	280.0	297.1	310.4	320.3	332.5

Source: Office of the Parliamentary Budget Officer.

Relative to PBO's revised EFOU 2013, the revenues outlook has been mainly affected by offsetting increases in personal income taxes and decreases in CIT revenues (as a result of a revised outlook for the share of national income accruing to households and corporations), increases in excise duties from the government's tobacco policy decision, weaker than expected GST/HST receipts following the recession, and lower break-even EI premium rates in 2017-18 and 2018-19.

3.5 Medium-term outlook for expenses

Federal program expenses are expected to decrease by nearly one percentage point of GDP over the medium-term outlook, from 13.3 in 2013-14 to 12.4 per cent in 2018-19. Table 3-5 provides a breakdown of the outlook for individual expenses.

Elderly benefits payments are expected to increase slightly as a share of GDP due to ageing demographics and the indexation of benefits to inflation. This is offset by a decline in children's benefits and Employment Insurance benefits.

Children's benefits decline as a share of GDP because the Universal Child Benefit—at 26 per cent of spending on children's benefits—is not indexed to inflation or economic growth.

Table 3-5

Outlook for expenses

billions of dollars

	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Major transfers to persons					
Elderly benefits	44.0	46.5	49.2	52.0	52.7
Employment Insurance benefits	17.9	19.7	20.0	20.1	20.5
Children's benefits	13.2	13.3	13.5	13.7	13.8
Total	75.1	79.6	82.7	85.8	87.0
Major transfers to OLG	62.5	65.2	68.1	70.5	73.2
Direct program expenses	113.1	114.0	117.1	119.7	124.3
Public debt charges	29.8	30.5	33.4	36.8	38.9
Total expenses	280.5	289.2	301.2	312.9	323.4

Source: Office of the Parliamentary Budget Officer.

After falling in 2013-14, EI benefit payments are expected to increase again when unemployment stops falling in 2014-15, and as the coverage ratio returns to its historical level (see below); however, the increase is projected to be less than the growth of GDP.

In aggregate, major transfers to persons are expected to increase by roughly the same rate as GDP.

Transfers to other levels of government are mostly statutory (set out in legislation) and also grow roughly in-line with nominal GDP in aggregate. There is very little uncertainty until 2016-17, when the main driver for CHT becomes the nominal GDP outlook.

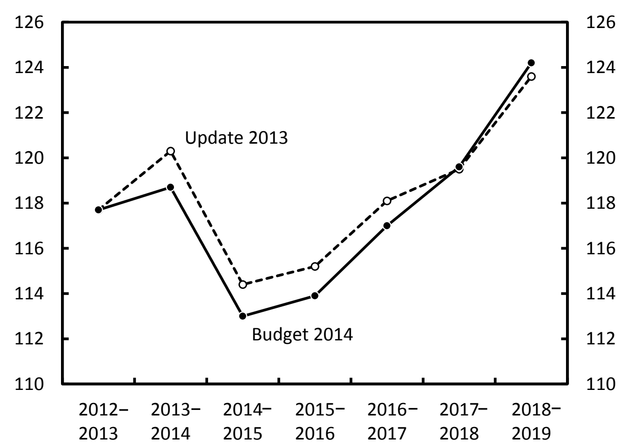
With major transfers growing roughly with GDP, the decline in program expenses as a share of GDP is driven almost entirely by a decrease in direct program expenses (DPE). Finance Canada's planning assumption for DPE (which PBO assumes is achieved) declines as a share of GDP by nearly one percentage point over the outlook, from 6.3 per cent to 5.4 per cent.[16] Over half of this decrease is achieved in 2014-15 alone.

Relative to Finance Canada's Update Of Economic and Fiscal Projections 2013 (Update 2013), the outlook for DPE in Budget 2014 shows savings in the early years of the projections and higher spending in 2017-18 and 2018-19 (Figure 3-5). This is the result of a combination of the savings measures discussed above, and actions to support jobs and growth, which increased direct program expenses by $0.6 billion in 2014-15, $1.0 billion in 2015-16, $1.2 billion in 2016-17 and 2017-18, and $1.6 billion in 2018-19.

Figure 3-5

Direct program expenses in Update 2013 and Budget 2014

billions of dollars



Source: Finance Canada.
Note: The Budget 2014 outlook has been adjusted for the revised PSHCP agreement.

[16] Adjusted for the revised PSHCP agreement announced March 26, 2014.

In addition to program expenses, the government must budget for expenses to service public debt and the accrual of future liabilities (the stock of interest-bearing debt was $892 billion in 2012-13). In 2013-14, interest expenses are expected to be 1.6 per cent of GDP. PBO's projection of the interest rate on market debt and market debt charges is provided in Table 3-6. Other debt charges are incurred from pensions and other future liabilities to arrive at the total interest expenses in the outlook.

Table 3-6

Outlook for effective interest rates on market debt

billions of dollars, unless noted otherwise.

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Interest rate	2.9	3.0	3.0	3.4	3.9	4.2
Market debt charges	18.3	19.1	19.6	22.1	24.9	27.1

Source: Office of the Parliamentary Budget Officer.

3.6 The EI Operating Account and premium rates

The EI operating account is a consolidated specified purpose account within the Accounts of Canada used to track all revenues and expenses related to the *Employment Insurance Act* after December 31, 2008.

The outlook for the EI Operating Account in Budget 2014 and in PBO's own projections continues to improve. PBO expects the account to accumulate and maintain a surplus in 2015-16 and beyond (Table 3-7). If no changes are made to current rate policy, the surplus will be gradually eliminated over a period of 6 years beginning 2017-18.

Table 3-7

Outlook for EI operating account, rate freeze

billions of dollars, unless noted otherwise

	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
EI premium revenues	22.7	23.7	23.4	20.6	21.4
EI benefits	17.9	19.7	20.0	20.1	20.5
	2014	**2015**	**2016**	**2017**	**2018**
Premium rate (frozen) %	1.88	1.88	1.88	1.55	1.56
Operating balance	3.4	2.8	3.0	-1.1	-0.7
Cumulative balance	-1.4	1.4	4.4	3.3	2.6

Source: Office of the Parliamentary Budget Officer.

When the government first published its outlook for the EI operating account in Budget 2012, the cumulative balance was projected to have a deficit of $6.6 billion in 2014. Even with the 2014 rate freeze, the government now projects the account to have a deficit of only $1.5 billion—an improvement of more than $5 billion.[17]

Premium revenues have developed as expected in the government's initial projections. The account improvement is a result of significantly lower benefits expenses. Part I benefits paid out were $1.2 billion (7.5 per cent) less than budgeted in Human Resources and Skills Development Canada's Report on Plans and Priorities for 2012-13.[18] Benefits expenses are now expected to be lower by an average of $1.8 billion each year relative to the projection in Budget 2012.

Benefits expenses are a product of payment amounts and the number of recipients. The average growth in wages (to which benefits payments are indexed) has also developed roughly as expected. Lower EI payments are therefore a result of fewer eligible claimants.

The outlook for unemployment has improved relative to the private sector outlook in Budget 2012, but explains only 6 per cent of the decrease in benefits. Far more important has been the decrease in the proportion of unemployed who are eligible for benefits (the coverage ratio).

[17] Budget 2014 pg. 273

[18] Part I benefits provide temporary assistance to eligible unemployed worker, or workers who are on special benefits for sickness, maternity or paternity leave, or caring for an ill family member.

There is some evidence of a small transitory impact on benefits shortly following changes to suitable employment and reasonable and customary efforts to obtain suitable employment in January 2013; however, there are many confounding factors and it is difficult to draw firm conclusions.[19] The observed impact is consistent with the government's estimate that benefits would be discontinued to 8,000 claimants and does not materially affect projected premium rates.[20]

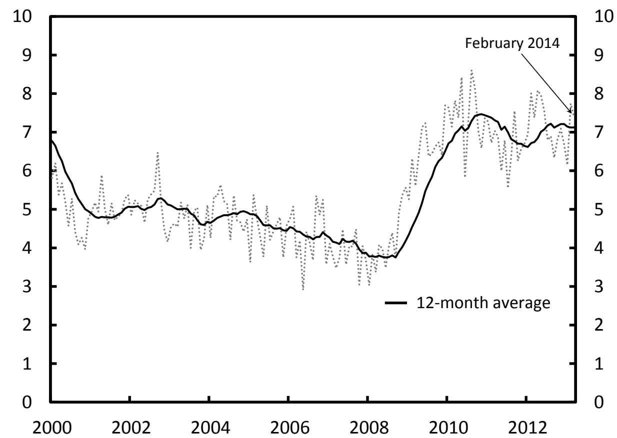
A more important driver of the decline of eligible beneficiaries has been a rising and sustained rate of long-term unemployment. Those who qualify for the maximum period of benefits are no longer eligible after 50 weeks of unemployment (after a two week waiting period and 48 weeks of benefits). Long-term unemployment has increased from under 4 per cent to over 7 per cent of total unemployment following the recession, after a decade of decline (Figure 3-6). The high rate of long-term unemployment can explain as much as 40 per cent of the decrease in benefits.

PBO attributes the remaining decline to other labour market characteristics following the recession that affect EI accessibility, such as higher part-time and temporary employment. PBO assumes the decrease in the coverage ratio is transitory and will return to pre-recession levels as the labour market recovers.

Figure 3-6

Share of long-term unemployed (53+ weeks)

per cent of total unemployment



Source: Statistics Canada (CANSIM Table 282-0047).

The significant decline in the share of unemployed persons eligible for benefits allows a lower premium rate to be set to balance expenses than currently planned in Budget 2014. PBO estimates that the premium rate could be set at $1.76 per $100 dollars of earnings in 2015 and $1.61 per $100 dollars of earnings in 2016 (Table 3-8).

Table 3-8

Outlook for EI operating account, 7-year break-even rates

billions of dollars, unless noted otherwise

	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
EI premium revenues	22.3	21.5	20.8	21.5	22.1
EI benefits	17.9	19.7	20.0	20.1	20.5
	2014	**2015**	**2016**	**2017**	**2018**
Premium rate (break-even) %	1.88	1.76	1.61	1.61	1.60
Operating balance	3.4	1.4	-0.8	-0.2	0.1
Cumulative balance	-1.4	0.0	-0.8	-1.0	-0.9

Source: Office of the Parliamentary Budget Officer.
Notes: Beginning 2016 the cumulative account is balanced over a 7-year forecast.

3.7 Key judgments and risks to the outlook

Employment Insurance premium rates

As PBO discussed in EFOU 2013, the discretion granted to the Governor-in-Council for setting EI premium rates introduces considerable uncertainty in the outlook for revenues.

[19] Based on an assessment of EI payments data, which shows a small deferral of benefits from January to later months.

[20] From the Regulatory Impact Analysis Statement: "It is expected that enhanced compliance measures will result in an estimated 8 000 claimants having their benefits temporarily discontinued until such time as they are able to demonstrate they are meeting their responsibilities under these regulations."
See http://www.gazette.gc.ca/rp-pr/p2/2012/2012-12-19/html/sor-dors261-eng.html.

If the government decides to set rates to balance revenues with forecast expenditures, PBO estimates it would decrease the revenue outlook by $2.2 billion in 2015-16 and $2.8 billion in 2016-17 (Table 3-9). Finance Canada estimates the impact on revenues would be roughly $3.3 billion in 2015-16 and $3.0 billion in 2016-17.[21]

Table 3-9

Impact on outlook of 7-year break-even premium rates

billions of dollars

	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Budgetary balance (rate freeze)	-0.5	7.8	9.1	7.5	9.1
Budgetary balance (break-even)	-0.9	5.6	6.3	8.0	9.6
Difference	0.4	2.2	2.8	-0.5	-0.5

Source: Office of the Parliamentary Budget Officer.

Asset sales

PBO has also identified the government's planning assumption for asset sales as a source of risk to revenues. Because of the discretion afforded to the timing of asset sales, it is difficult for PBO to independently evaluate the impact on the budget outlook. PBO continues to use the government's planning assumption announced in Update 2013 of $0.5 billion in 2014-15 and $1.5 billion in 2015-16.

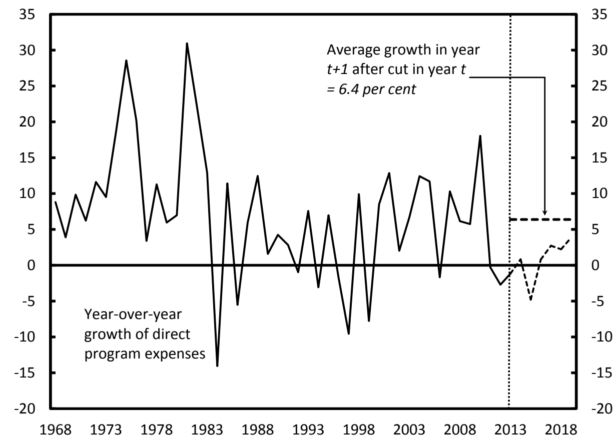
Direct Program Expenses restraint

DPE will face significant pressure following the planned 2014-15 cuts. Such prolonged restraint has not been achieved in the history of the modern Public Accounts. Historically, a year of reductions is typically followed by a year of increases in DPE of around 6.4 per cent on average (Figure 3-7). If the typical rebound from a period of DPE reductions were to occur in 2014-15 or 2015-16, it could eliminate the projected surplus in 2015-16.

Figure 3-7

Historical and assumed DPE growth

per cent



Source: Office of the Parliamentary Budget Officer; Finance Canada.

3.8 Uncertainty in PBO's Fiscal Projection

To estimate the sensitivity of the outlook to economic uncertainty, PBO constructs a probability distribution around its budgetary balance projection and presents the results in a fan chart (Figure 3-8). The probability distribution is estimated using the historical errors of the average private sector forecast, an assessment of the balance of risks to the average private sector forecast in Budget 2014, and the sensitivity of budgetary revenues and expenses to economic shocks published by Finance Canada.[22]

PBO estimates that the likelihood of realizing a balanced budget or better is approximately 50 per cent in 2014-15, 70 per cent in 2015-16, 60 per cent in 2017-18, and 65 per cent in 2018-19.

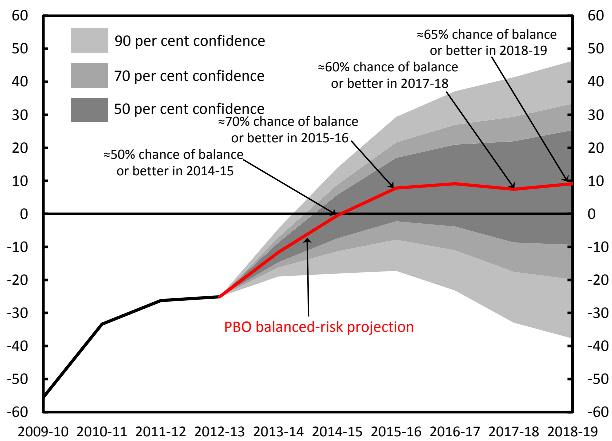
[21] See Budget 2014, p. 273.

[22] See Budget 2014, p. 287

Figure 3-8

Budgetary balance outcomes given economic uncertainty

billions of dollars



Sources: Office of the Parliamentary Budget Officer; Finance Canada.

3.9 Comparison to the Budget 2014 Fiscal Outlook

PBO projects a budgetary balance that is $5.0 billion higher than Finance Canada's estimate for 2013-14 and roughly the same on average over the medium term (Table 3-10).

The differences between PBO's and Finance Canada's outlooks are mostly due to *other revenues* over 2014-15 to 2016-17, a higher projected 7-year break-even EI premium rate in 2017, and higher public debt charges.[23] A complete table of comparisons is provided in Annex E.

Table 3-10

Comparison of PBO and Budget 2014 fiscal outlooks

billions of dollars

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Budgetary revenues	4.3	3.7	3.8	3.6	2.6	0.1
Program expenses	-0.2	0.5	1.8	1.2	0.7	-1.8
Public debt charges	-0.4	0.8	0.5	1.3	2.4	3.1
Budgetary balance	5.0	2.4	1.4	1.0	-0.6	-1.2

Sources: Parliamentary Budget Officer; Finance Canada.
Note: Differences are presented as the outlook in EFO 2014 subtracted by the outlook in Budget 2014.

4 PBO's estimate of the federal structural budget balance

Budgetary deficits and surpluses can result from a combination of two factors: revenues from tax policy being fundamentally sufficient or insufficient for a given level of spending when the economy is growing at trend (structural factors), and the impact on revenues and expenses when the economy is growing faster or slower than trend (cyclical factors). Distinguishing between structural and cyclical components of a government's budgetary balance is important because cyclical surpluses or deficits are transitory, while structural surpluses or deficits can be addressed only by policy action. PBO routinely revises its estimates of the government's structural budgetary balance based on revised estimates of the economy, announced measures, and changes in elasticity assumptions.

The projected budgetary balance improves over the medium term from a deficit of $11.6 billion in 2013-14 to a surplus of $7.8 billion in 2015-16 (Table 4-1). This is largely the result of an improvement in the projected structural balance (mostly from DPE restraint). PBO projects that the government's structural deficit will be eliminated in 2014-15, giving rise to a structural surplus of $8.9 billion in 2015-16. The decrease in the structural balance over 2016-17 and 2017-18 largely reflects the reduction in the EI premium rate in 2017 (to $1.55 per $100 of insurable earnings), as well as decreases in the annual growth of potential real GDP in 2017 and 2018 (to 1.6 and 1.5 per cent, respectively).

Table 4-1

Structural and cyclical balance estimates

billions of dollars

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Budgetary balance	-11.6	-0.5	7.8	9.1	7.5	9.1
Structural balance	-4.5	4.8	8.9	5.7	2.0	3.1
Cyclical balance	-7.1	-5.3	-1.1	3.4	5.5	6.0

Source: Office of the Parliamentary Budget Officer.

[23] PBO's projection of other revenues grows partially with GDP and partially with PBO's projection of nominal interest rates.

5 Comparing PBO and Finance Canada's estimates of the structural balance

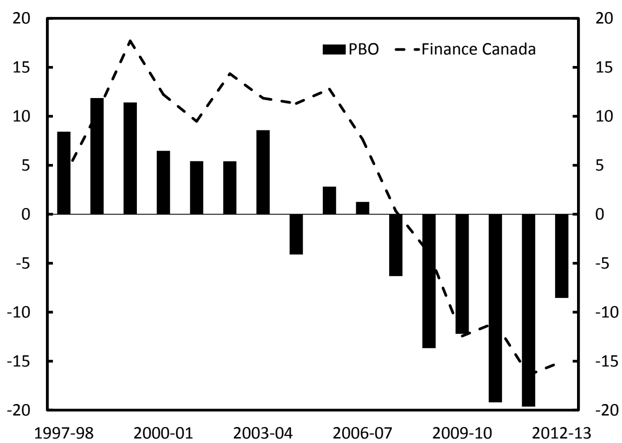
Since a government's structural budget balance is not directly observable and must be estimated, it is useful to compare estimates produced by different organizations such as Finance Canada and PBO.

Finance Canada publishes the Fiscal Reference Tables (FRT) on an annual basis, which include its estimate of the government's structural budget balance.[24] In FRT 2013, Finance Canada estimated structural deficits over the period of 2008-09 to 2012-13, which is consistent with PBO's estimates (Figure 5-1).

Figure 5-1

Estimates of the government's structural budget Balance, 1997-98 to 2012-13

billions of dollars



Sources: Office of the Parliamentary Budget Officer; Finance Canada.

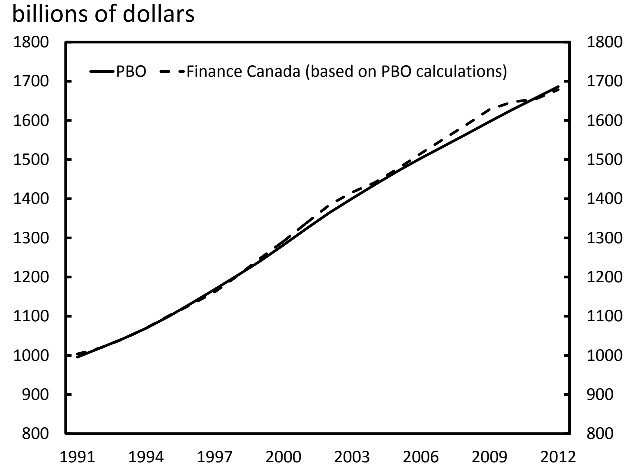
Both Finance Canada and PBO appear to employ a similar methodology that attempts to adjust transitory fluctuations in commodity prices and temporary factors in their estimation of the government's structural budget balance. The differences in Finance Canada's and PBO's estimates of the structural budget balance likely reflect differences in the underlying estimates or assumptions of revenue and spending sensitivities as well as differences in estimates of potential GDP and trends in terms of trade. Unfortunately, Finance Canada has not published or provided its estimates of potential GDP and terms of trade or its revenue and spending sensitivities underlying the structural budget balance estimates.[25] However, FRT 2013 provides estimates of budget balances relative to nominal potential GDP, which allows PBO to calculate what it believes to be Finance Canada's estimates of potential GDP and output gap over the historical period.[26]

Based on PBO's calculation, PBO and Finance Canada's estimates of potential GDP track each other closely from 1991 to 2000, with PBO's estimates being lower by $1.6 billion annually on average (Figure 5-2). From 2001 to 2010, the difference between the two series increased, with PBO's estimates lower by $16.7 billion annually on average. PBO's estimates are higher than Finance Canada's (based on PBO calculations) by $2.9 billion in 2011 and by $7.6 billion in 2012.

Figure 5-2

Estimates of Potential GDP, 1991 to 2012

billions of dollars



Sources: Office of the Parliamentary Budget Officer; Finance Canada.

[24] Available at: http://www.fin.gc.ca/frt-trf/2013/frt-trf-13-eng.asp.

[25] PBO has requested this data (November 30, 2011: http://www.parl.gc.ca/PBO-DPB/documents/InformationRequests/Requests/IR0056_IMF_submission.pdf; February 3, 2012: http://www.parl.gc.ca/PBO-DPB/documents/InformationRequests/Requests/IR0056_IMF_submission_followup.pdf; and March 9, 2012: http://www.parl.gc.ca/PBO-DPB/documents/InformationRequests/Requests/IR0077_Finance_FRT.pdf) Finance Canada has not provided its estimates of potential GDP and the output gap to the PBO.

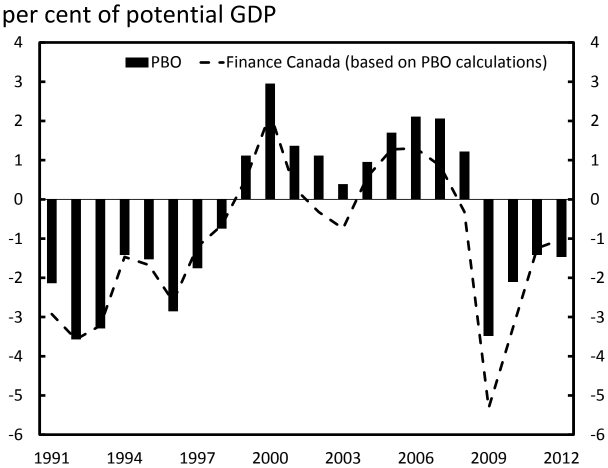
[26] The 2013 *Fiscal Reference Tables* provide estimates of federal and total government budget balances expressed relative to nominal potential GDP from 1991 to 2012. Using the actual GDP deflator, PBO determines the levels of potential GDP residually.

Since Finance Canada's and PBO's estimates of potential GDP are close to each other from 1991 to 2000, PBO's estimates of the output gap track Finance Canada's estimates closely over the same period (Figure 5-3). PBO's estimates are higher by only 0.1 percentage points annually on average from 1991 to 2000. Since PBO and Finance Canada's estimates of potential GDP differ more significantly from 2000 to 2010, PBO's estimates of the output gap are higher by 1.1 percentage points annually on average over the same period. PBO's estimate of the output gap is smaller than Finance Canada's by 0.2 percentage points in 2011, and by 0.4 percentage points in 2012.

Figure 5-3

Estimates of the Output Gap, 1991 to 2012

per cent of potential GDP



Sources: Office of the Parliamentary Budget Officer; Finance Canada.

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Annex A

Table A – Comparison of EFOU 2013 and EFO 2014 economic outlooks

	2014	2015	2016	2017	2018
Real GDP growth (%)					
October 2013 EFOU	2.0	2.6	2.6	1.9	1.5
April 2014 EFO	2.1	2.7	2.5	1.9	1.5
difference	0.1	0.0	-0.1	0.0	0.1
GDP inflation (%)					
October 2013 EFOU	1.4	1.5	1.9	2.0	2.0
April 2014 EFO	1.5	1.6	1.8	2.0	2.0
difference	0.1	0.1	-0.1	0.0	0.0
Nominal GDP growth (%)					
October 2013 EFOU	3.4	4.2	4.6	4.0	3.5
April 2014 EFO	3.6	4.3	4.3	4.0	3.6
difference	0.2	0.2	-0.3	0.0	0.1
Nominal GDP level (billions of dollars)					
October 2013 EFOU	1,937	2,017	2,110	2,193	2,270
April 2014 EFO	1,948	2,032	2,120	2,204	2,282
difference	11	15	10	10	12
3-month treasury bill rate (%)					
October 2013 EFOU	1.0	1.4	2.8	4.0	4.2
April 2014 EFO	1.0	1.4	2.5	3.5	4.2
difference	0.0	-0.1	-0.3	-0.5	0.0
10-year government bond rate (%)					
October 2013 EFOU	3.2	3.8	4.5	5.2	5.3
April 2014 EFO	2.7	3.6	4.4	5.1	5.3
difference	-0.4	-0.2	-0.1	-0.1	0.0
Exchange rate (US cents/C$)					
October 2013 EFOU	96.5	96.6	96.0	95.6	94.6
April 2014 EFO	90.8	93.5	94.6	94.5	93.6
difference	-5.7	-3.0	-1.4	-1.2	-1.0
Unemployment rate (%)					
October 2013 EFOU	7.3	7.0	6.5	6.3	6.1
April 2014 EFO	7.0	6.8	6.4	6.1	6.0
difference	-0.2	-0.2	-0.2	-0.1	-0.1
Total CPI inflation (%)					
October 2013 EFOU	1.7	1.9	2.0	2.0	2.0
April 2014 EFO	1.7	2.0	2.0	2.0	2.0
difference	0.0	0.0	0.0	0.0	0.0
US real GDP growth (%)					
October 2013 EFOU	2.7	3.4	3.6	3.3	2.6
April 2014 EFO	2.7	3.5	3.6	3.1	2.5
difference	0.0	0.1	0.0	-0.2	-0.1

Source: Office of the Parliamentary Budget Officer.

Annex B

Table B – Comparison of Budget 2014 and EFO 2014 economic outlooks

	2014	2015	2016	2017	2018
Real GDP growth (%)					
Budget 2014	2.3	2.5	2.5	2.3	2.2
April 2014 EFO	2.1	2.7	2.5	1.9	1.5
difference	-0.2	0.2	0.0	-0.4	-0.7
GDP inflation (%)					
Budget 2014	1.6	2.0	2.0	2.0	2.0
April 2014 EFO	1.5	1.6	1.8	2.0	2.0
difference	-0.1	-0.3	-0.2	0.0	0.0
Nominal GDP growth (%)					
Budget 2014	3.9	4.5	4.5	4.4	4.2
April 2014 EFO	3.6	4.3	4.3	4.0	3.6
difference	-0.3	-0.2	-0.2	-0.4	-0.7
Nominal GDP level (billions of dollars)					
Budget 2014	1,952	2,040	2,132	2,226	2,320
April 2014 EFO	1,948	2,032	2,120	2,204	2,282
difference	-4	-8	-12	-22	-38
3-month treasury bill rate (%)					
Budget 2014	1.0	1.5	2.7	3.6	4.0
April 2014 EFO	1.0	1.4	2.5	3.5	4.2
difference	0.0	-0.1	-0.3	-0.1	0.2
10-year government bond rate (%)					
Budget 2014	3.0	3.5	4.1	4.6	4.8
April 2014 EFO	2.7	3.6	4.4	5.1	5.3
difference	-0.3	0.1	0.3	0.5	0.5
Exchange rate (US cents/C$)					
Budget 2014	93.7	95.3	95.9	96.2	96.3
April 2014 EFO	90.8	93.5	94.6	94.5	93.6
difference	-2.9	-1.8	-1.3	-1.7	-2.7
Unemployment rate (%)					
Budget 2014	6.8	6.6	6.4	6.3	6.2
April 2014 EFO	7.0	6.8	6.4	6.1	6.0
difference	0.2	0.2	0.0	-0.1	-0.2
Total CPI inflation (%)					
Budget 2014	1.5	1.9	2.0	2.0	2.0
April 2014 EFO	1.7	2.0	2.0	2.0	2.0
difference	0.2	0.1	0.0	0.0	0.0
US real GDP growth (%)					
Budget 2014	2.7	3.1	3.0	2.9	2.6
April 2014 EFO	2.7	3.5	3.6	3.1	2.5
difference	0.0	0.4	0.6	0.1	-0.1

Sources: Office of the Parliamentary Budget Officer, Finance Canada.

Annex C

Table C –PBO fiscal outlook

billions

	2012-2013	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Income taxes							
Personal income tax	125.7	130.5	138.6	147.4	155.2	162.4	168.9
Corporate income tax	35.0	34.2	36.0	39.5	42.1	44.5	46.3
Non-resident income tax	5.1	6.2	6.0	6.5	7.0	7.2	7.5
Total income tax	165.8	170.9	180.6	193.3	204.3	214.2	222.7
Excise taxes/duties							
Goods and Services Tax	28.8	30.9	31.9	33.5	34.8	36.1	37.3
Custom import duties	4.0	4.3	4.6	4.9	4.6	4.7	4.9
Other excise taxes/duties	10.8	10.6	11.3	11.3	11.3	11.4	11.3
Total excise taxes/duties	43.6	45.8	47.8	49.7	50.8	52.2	53.5
EI premium revenues	20.4	22.2	22.7	23.7	23.4	20.6	21.4
Other revenues	26.9	29.4	28.9	30.3	31.9	33.3	34.8
Total budgetary revenues	**256.6**	**268.3**	**280.0**	**297.1**	**310.4**	**320.3**	**332.5**
Major transfers to persons							
Elderly benefits	40.3	41.6	44.0	46.5	49.2	52.0	52.7
Employment Insurance benefits	17.1	17.0	17.9	19.7	20.0	20.1	20.5
Children's benefits	13.0	13.2	13.2	13.3	13.5	13.7	13.8
Total	70.3	71.8	75.1	79.6	82.7	85.8	87.0
Major transfers to OLG	58.4	60.4	62.5	65.2	68.1	70.5	73.2
Direct program expenses	117.7	118.8	113.1	114.0	117.1	119.7	124.3
Public debt charges	29.2	28.9	29.8	30.5	33.4	36.8	38.9
Total expenses	**275.6**	**279.8**	**280.5**	**289.2**	**301.2**	**312.9**	**323.4**
Budgetary balance	**-18.9**	**-11.6**	**-0.5**	**7.8**	**9.1**	**7.5**	**9.1**
Federal debt	602.4	614.0	614.5	606.7	597.6	590.1	580.9

Source: Office of the Parliamentary Budget Officer.

Annex D

Table D – Changes to PBO's fiscal outlook since EFOU 2013

billions

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Income taxes						
Personal income tax	-2.1	-2.8	-1.7	-1.6	-1.3	-1.3
Corporate income tax	0.0	1.8	2.4	2.0	1.5	1.3
Non-resident income tax	0.6	0.2	0.4	0.5	0.4	0.4
Total income tax	-1.5	-0.8	1.0	0.8	0.6	0.4
Excise taxes/duties						
Goods and Services Tax	0.0	-0.3	0.0	-0.1	0.0	-0.1
Custom import duties	0.1	0.1	0.0	0.0	0.0	0.0
Other excise taxes/duties	-0.2	0.6	0.7	0.8	0.8	0.8
Total excise taxes/duties	-0.1	0.4	0.6	0.7	0.7	0.7
EI premium revenues	0.5	0.0	0.1	0.1	0.2	0.0
Other revenues	1.6	-0.3	-1.2	0.2	0.2	0.2
Total budgetary revenues	**0.6**	**-0.7**	**0.5**	**1.8**	**1.8**	**1.4**
Major transfers to persons						
Elderly benefits	-0.1	0.0	0.0	0.1	0.1	0.2
Employment Insurance benefits	0.0	-0.6	0.5	0.2	0.2	0.1
Children's benefits	0.1	0.0	-0.1	-0.1	0.0	-0.1
Total	-0.1	-0.6	0.4	0.2	0.3	0.2
Major transfers to OLG	-0.1	-0.2	-0.1	-0.1	-0.1	-0.2
Direct program expenses	-1.9	-2.3	-1.9	-1.9	-1.7	-0.2
Public debt charges	-0.9	-0.7	-1.1	-0.5	0.5	-0.1
Total expenses	**-3.0**	**-3.8**	**-2.7**	**-2.3**	**-1.0**	**-0.2**
Budgetary balance	**3.6**	**3.1**	**3.3**	**4.2**	**2.8**	**1.6**
Federal debt	-3.6	-6.6	-9.9	-14.1	-16.8	-18.4

Source: Office of the Parliamentary Budget Officer.

Annex E

Table E –Difference between PBO's fiscal outlook and Budget 2014

billions

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Income taxes						
Personal income tax	0.4	0.8	1.6	2.0	1.9	1.2
Corporate income tax	-0.8	-1.0	0.0	-0.1	0.0	-0.2
Non-resident income tax	0.7	0.3	0.5	0.5	0.3	0.2
Total income tax	0.3	0.2	2.1	2.4	2.3	1.2
Excise taxes/duties						
Goods and Services Tax	1.0	0.6	0.3	-0.3	-0.6	-1.0
Custom import duties	0.1	0.2	-0.1	-0.1	-0.2	-0.2
Other excise taxes/duties	0.0	0.0	0.0	0.0	0.0	-0.1
Total excise taxes/duties	1.0	0.8	0.2	-0.3	-0.8	-1.3
EI premium revenues	0.7	0.0	0.1	0.4	1.2	1.2
Other revenues	2.3	2.7	1.3	1.1	-0.1	-1.0
Total budgetary revenues	**4.3**	**3.7**	**3.8**	**3.6**	**2.6**	**0.1**
Major transfers to persons						
Elderly benefits	-0.4	-0.1	0.1	0.2	0.3	-1.7
Employment Insurance benefits	-0.3	0.0	1.2	1.0	0.6	0.2
Children's benefits	0.1	0.0	-0.1	-0.1	0.0	-0.1
Total	-0.6	-0.1	1.3	1.2	0.9	-1.6
Major transfers to OLG	-0.1	-0.1	-0.1	-0.2	-0.5	-0.6
Direct program expenses	0.1	0.1	0.1	0.1	0.1	0.1
Public debt charges	-0.4	0.8	0.5	1.3	2.4	3.1
Total expenses	**-0.7**	**1.3**	**2.3**	**2.5**	**3.2**	**1.3**
Budgetary balance	**5.0**	**2.4**	**1.4**	**1.0**	**-0.6**	**-1.2**
Federal debt	-2.0	-4.4	-5.7	-6.7	-6.1	-5.1

Sources: Office of the Parliamentary Budget Officer; Finance Canada.