2007 Federal Economic Statement: Brief Summary and Analysis

Federal Finance Minister Jim Flaherty brought in a surprise economic statement and mini-budget ahead of schedule on October 30. The economic statement includes a number of expected – and unexpected – tax cuts, but nothing else to improve the long-term health of the economy.

The tax cuts announced include:

- 1 percentage point cut to GST effective January 2008.
  - cost of $6 billion a year, $34 billion over six years
- Cut to lowest personal income tax rate from 15.5% to 15% retroactive to January 2007.
  - cost of $1.3 billion a year, $8.4 billion over six years
- Cut of corporate income tax rate from 22% today down to 15% by 2012, with an immediate one percentage point cut in January 2008.
  - immediate cost of $1.3 billion, total cost of $14.1 billion over five years, and rising to an annual cost of over $10 billion a year
- Bringing forward the cut in small business tax rate by one year to 11 per cent in 2008.
  - temporary cost totalling $265 million
- Accelerating the increase in the basic personal amount for federal taxes to $9,600 for 2007 and 2008 and to $10,100 in 2009.
  - temporary two year cost totalling $2.4 billion

The total cost of these measures will amount to about $60 billion over the next five years. In total, the Conservatives claim that they have cut taxes by $190 billion since they came into office. The cost of the tax cuts that they have introduced and announced will amount to over $25 billion annually by next year, but there is little evidence that working families have benefited so far or will do so in the future.

With just $20 billion, the federal government could have made dramatic improvements to public services and reducing poverty by:

- Phasing in a national non-profit public child care and early learning program: guaranteeing a space for every 3-5 year old in Canada.
- Restoring enough funding to cities and municipalities to end their budget crises, rebuild their infrastructure and community services.
- Starting a national pharmacare program to provide affordable medicine to all Canadians.
- Providing enough resources for First Nations and Aboriginal communities to fund the Kelowna Accord and meet further health, educational, housing, land claims, environmental, fiscal and child welfare needs.

These measures would have done much more to benefit working families and to build a stronger country and economy.

Over 80% of the value of the tax cuts announced in this statement for the next five years are for the GST and corporate tax cuts. The corporate tax cuts could eventually cost well over $10 billion a year. Corporate tax revenues are $40 billion annually now: a cut of almost 30% of this works out to over $11 billion. Canada's corporate tax rates would be the lowest of all major industrialized countries by 2011 and 12 percentage points below the rate in the United States. Past corporate tax cuts and skyrocketing profits have done little to boost investment in Canada.

The cut in the personal income tax rate is very small -- amounting to less than 10% of the ongoing value of the tax cuts announced today – and will provide no more than $186 this year for those with taxable income over $37,000. The increase in the basic personal amount provides a temporary benefit of $150 per year for those who qualify. Those with lower incomes will benefit much less and the poor will not benefit at all.

There is no guarantee that the GST cut will be passed on to consumers. A considerable portion of last year's GST cut was gobbled up by retailers through higher prices. This was evident not just at the check-out counter, but also through a much lower than expected drop in inflation and a 22% increase in retailers' profits.

The discussion in the *Economic Statement* focuses on the weakening U.S. economy and global economic uncertainty. A number of economic statistics for the fall will be coming out shortly and they are expected to show signs of weakness in the Canadian economy, with further weakness in the manufacturing sector and lower exports because of the high dollar.

The cut in the GST and the retroactive income tax cut won't provide any substantial benefits to the Canadian economy, but they will give it a short-term boost. This will help to prevent bad economic numbers over the next few months, just before Harper is expected to force a federal election.

These deep tax cuts could also lead to federal deficits in future years – which would probably lead to cuts to public services. These types of policies by the Harris government in Ontario caused lasting damage to public services, which the province still hasn't recovered from. Tax cuts to stimulate the U.S. economy by the Bush administration have also clearly not worked.

The Economic Statement slams the door on a great opportunity. The federal government had enough funds to make substantial investments in infrastructure, education, public services and reducing poverty, which would have provided lasting benefits to Canadians across the country and strengthened the economy for the long-term. Instead, it has squandered it on expensive corporate and sales tax cuts that will provide little lasting benefit.

<u>Further information:</u>

The economic projections are based on private sector surveys, which are probably now dated. Recent economic forecasts have been more pessimistic because of the weakening U. S. economy, problems in financial markets, higher interest rates the higher dollar.

The fiscal projections are provided for five years. The federal surplus is expected to fall to $4.4 billion for each of the next two years before rising again. According to the sensitivity estimates, this surplus could be wiped out if real GDP growth and GDP inflation were both 1 per cent lower than expected.

The Economic Statement also includes proposals to:

- Maintain the GST credit at its current level. This only partially makes up for the 12% decline in the value of the GST credit during the 1990s when it wasn't indexed to inflation.
- Maintain the GST/HST rebate rate for new housing – amounting to $290 million in benefits for the purchase of new homes.
- Retain GST rebates to public sector bodies – such as universities, hospitals, schools and charities – at current rates. According to the statement, this will mean $165 million in benefits for these bodies.
- Pay down the federal debt by $10 billion in 2007-8.

The federal government is pushing provinces to reduce their corporate tax rates down to 10%.

The federal government is also strongly pushing Ontario, Saskatchewan, Manitoba and British Columbia to harmonize their retail sales taxes with the GST. This would provide further large benefits to businesses, but would hurt consumers because many goods are exempt from the provincial retail sales taxes.

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October 31, 2007