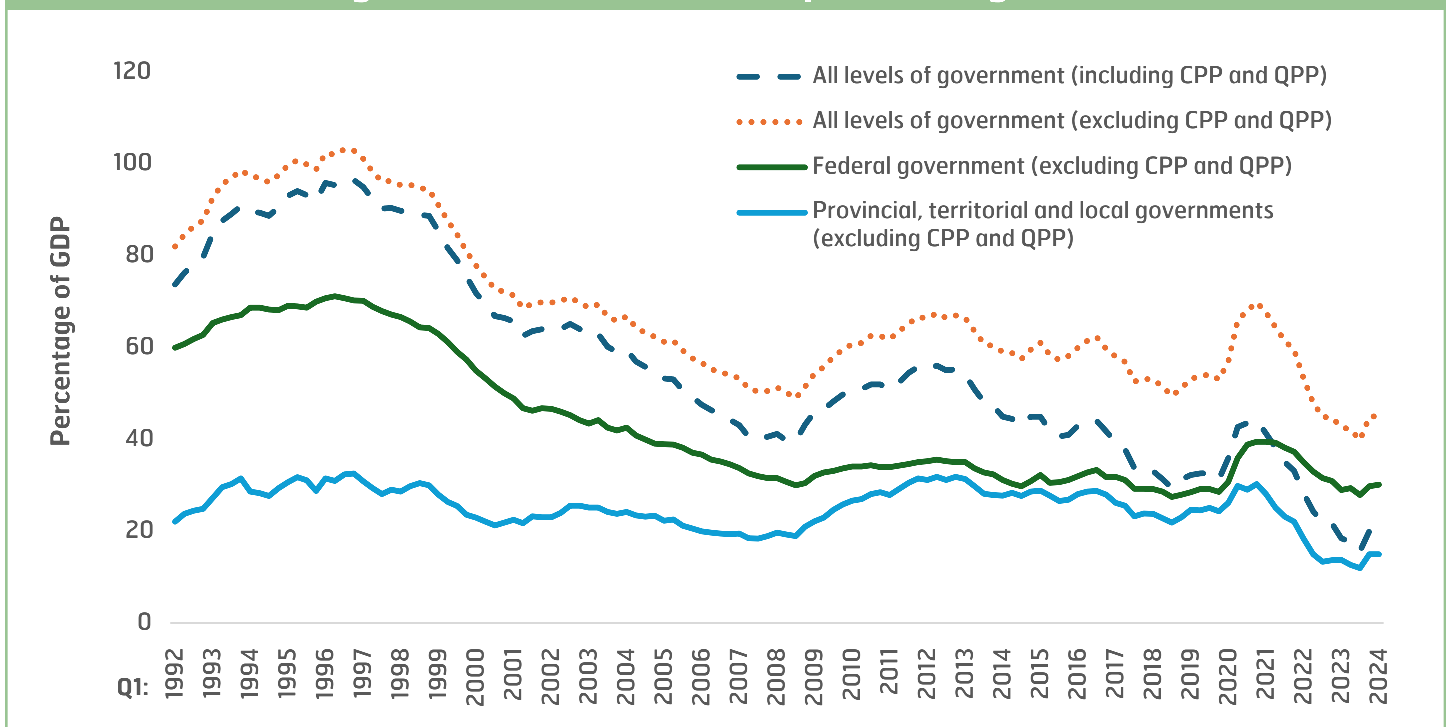
Is government debt really causing our economic problems?

Governments regularly borrow money to fund infrastructure and services. When these investments lead to economic growth, improve quality of life or prevent higher costs in the future, borrowing can make good fiscal sense.

If the economy is growing faster than the government's debt, it suggests that borrowing is supporting economic growth. To measure this, many governments, including the Trudeau government, use the net debt-to-GDP ratio. This ratio expresses net debt as a percentage of gross domestic product (GDP), or the total value of all goods and services produced by an economy. Net debt is calculated by subtracting the value of government assets, like land, buildings and financial assets, from the total debt.

Comparing net debt to GDP doesn't capture all the benefits of government investments to the economy. However, it does capture some of the benefits to economic growth of government investment in infrastructure and services. The net debt-to-GDP ratio thus gives a more accurate view of how borrowing affects the economy than looking at government debt levels alone.

In Canada, we measure the net debt-to-GDP ratio in two ways: with and without the Canadian Pension Plan (CPP) and Quebec Pension Plan (QPP) included. The CPP and QPP are considered government financial assets. Statistics Canada reports the net debt both with and without these funds because they are different



Source: Statistics Canada tables 10-10-0015-01 and 36-10-0104-01

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from other financial assets. If you only want to consider assets the government can use to pay off its debt, you need to exclude the CPP and QPP because these assets are reserved for people's pensions and can't be used for other purposes. On the other hand, including these funds in net debt calculations helps us better understand the overall impact of government borrowing on the economy, since they represent real investments in our future.

Mainstream economists advise governments to keep their net debt-to-GDP ratios as low as possible, but academic research shows that there's no magic number. Most observers are looking for stability, and big increases or decreases warrant further investigation.

In the mid-1990s, debt across all levels of government in Canada, excluding CPP and QPP, hit over 100% of GDP. This led to significant federal budget cuts. These cuts were based on the idea that too much government debt was bad for the economy, reflecting the so-called Reganomics approach that continues to influence global economic policy today.

Debt levels subsequently fell from the mid-1990s until the 2008 financial crisis. After the crisis, net debt-to-GDP remained stable at the federal level but increased slightly at the provincial level.

During the COVID-19 pandemic, all levels of government increased spending to stabilize the economy. At the same time, GDP fell. Both factors caused net debt-to-GDP to rise in 2020 and 2021.

Despite this, federal government net debt-to-GDP, excluding CPP and QPP, is now lower than it was when Justin Trudeau was first elected nine years ago. In the fourth quarter of 2015, federal net debt-to-GDP was 31.2%. By early 2024, it had dropped to 30.2%. Provincial, territorial and local government debt has also decreased, falling from 28.1% in early 2021 to 15% in early 2024.

In fact, net debt-to-GDP levels across all levels of government are now lower than at any time in the past 30 years. The most dramatic drop is in total government net debt, including CPP and QPP, because both pension plans have continued to grow over the years.

So, remember – if someone tells you government debt is the root of all our problems, they're spinning quite the tall tale. The reality is that government debt, when measured against the size of the economy, is lower than it has been in decades.

Rate hikes lead to weaker labour market

When the Bank of Canada (BoC) started to increase interest rates in 2022, its goal was to reduce inflation. Typically, higher interest rates make borrowing more expensive. This decreases consumer spending and business investment, helping to keep prices down. Importantly, raising interest rates also weakens the labour market by slowing job growth and limiting wage increases. As a result, workers have less ability to spend and demand falls even more, further curbing inflation.

As expected, data shows that recent rate hikes have had a negative impact on Canada's labour market.

You can measure the strength of the labour market by looking at job vacancy numbers. High job vacancy numbers are a sign of a healthy job market. Around the time the BoC began raising interest rates in the spring of 2022, there were more than a million job vacancies, totalling 5.7% of total labour demand (the combined number of filled and vacant jobs).

Over the past two years, however, the number of job vacancies has fallen from over a million in May 2022 to about 560,000 in May 2024. The job vacancy rate has dropped to 3.1%, which is even lower than it was in the fall of 2020 following the major labour market disruption caused by the COVID-19 pandemic. These changes suggest the labour market is weakening.

You can also measure labour market health by looking at unemployment and underemployment rates.

Unemployment refers to individuals who do not have a job but who are actively looking for work.

Underemployment includes workers who are:

- jobless and wanted work, but have given up looking,
- jobless but on temporary layoff or waiting for a job to start soon,
- working part-time but looking for more hours.

Significantly, both unemployment and underemployment rates have grown over the past year. The number of unemployed workers increased by 220,000, pushing the unemployment rate from 5.9% to 6.8%. At the same time, the number of underemployed

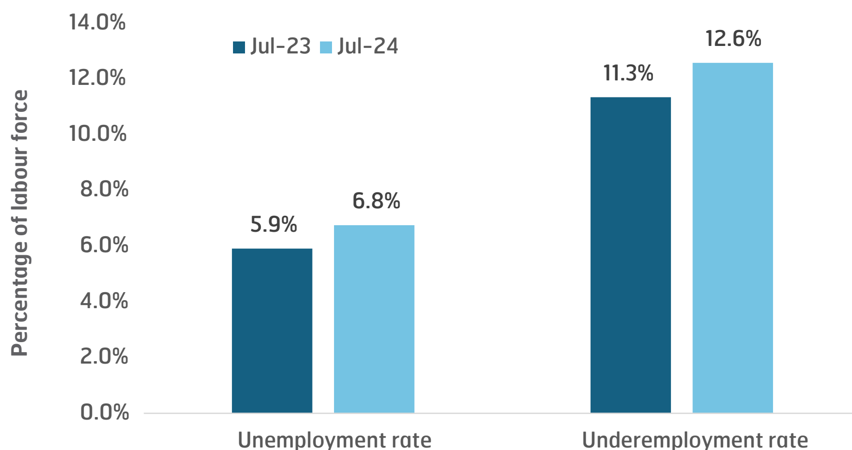
continued on page 3

continued from page 2

workers has grown by about 130,000, raising the underemployment rate from 11.3% to 12.6%.

The BoC's rate hikes have triggered a worrying shift in the labour market. With fewer available positions, workers are experiencing more competition and rates of underemployment and unemployment are on the rise.

Underemployment and unemployment, July 2023–July 2024



Source: Statistics Canada Labour Force Survey

Work stoppages and inflation

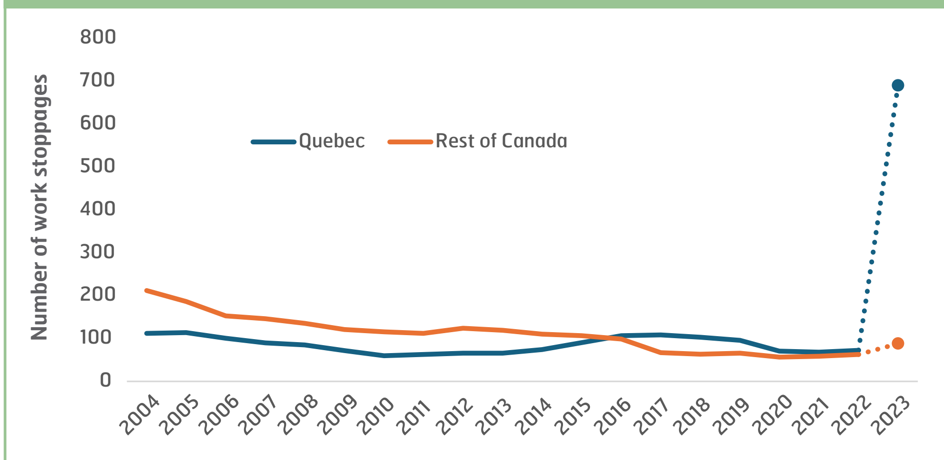
Strikes are a powerful tool that workers rely on to make their voices heard. This is especially true during tough economic times. When economic pressures like inflation push workers to their breaking point, labour action often follows. We saw this clearly in the 1970s, when rising inflation led to a spike in strikes and lockouts.

As inflation surged again in 2022, many wondered if we would see a similar rise in strikes and lockouts. Recently released data confirms that we did, particularly in Quebec.

The Labour Program at Employment and Social Development Canada (ESDC) tracks work stoppages due to strikes or lockouts that result in 10 or more lost person-days of work. A person-day of work represents one person's work for one day. For example, 10 workers on strike for one day counts as 10 person-days of work lost.

Looking at a rolling 5-year average starting in the early 2000s, the number of work stoppages in Canada has been slowly falling over time.

Spike in work stoppages, 2023



Statistics Canada table 14-10-0352-01

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Common Front strike — November 23, 2023
Photo: Claude Roussel

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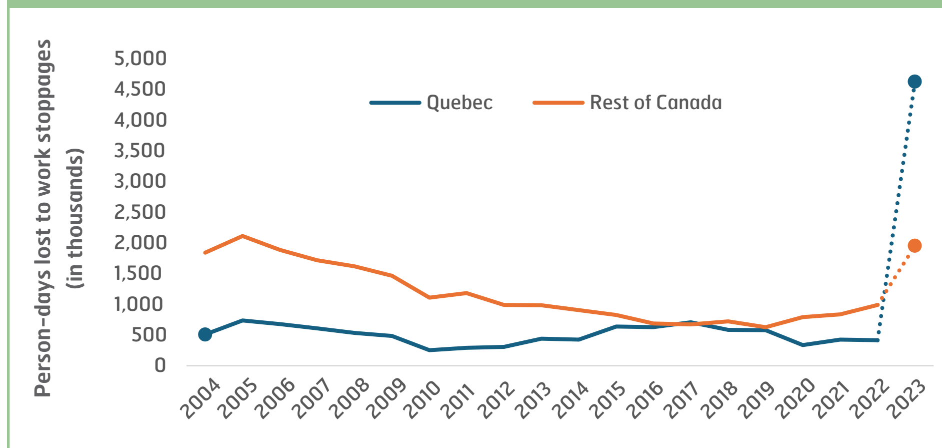
Person-days lost to work stoppages, 2023



Statistics Canada table 14-10-0352-01

But in 2023, this trend reversed, with a dramatic increase in work stoppages in Quebec and a slight rise in the rest of Canada. Quebec recorded 690 work stoppages in 2023, a 9.5-fold increase over the previous 5-year average. The rest of Canada saw a 1.4-fold increase, with 88 work stoppages.

More than 600 of the work stoppages in Quebec occurred in the public sector. The majority of these work stoppages were part of the historic Common Front movement. The Common Front coalition involved 420,000 workers from multiple public sector unions participating in a series of rotating strikes beginning in November 2023. Although the Quebec government initially offered the coalition a 9% wage increase over 5 years, the strikers managed to secure a 17.4% increase by the time their labour action ended in late December 2023. But while the increase in the number of work stoppages in 2023 was significant, it doesn't tell the whole story.

To fully grasp the scale of these labour actions, we also need to consider the person-days lost.

Person-days lost reflect not only how many work stoppages occurred but also how long they lasted and how many people were involved. This metric therefore gives us a clearer picture of how disruptive labour actions really are. For instance, a single, long-lasting strike involving many workers (more person-days lost) can have a much greater impact on productivity and the economy than several shorter strikes with fewer participants (fewer person-days lost).

The 5-year average for person-days lost remained fairly stable throughout the 2000s in Quebec and declined across the rest of Canada between 2005 and 2019. However, in 2023, Quebec reported 4.6 million person-days lost to work stoppages—11 times higher than the previous 5-year average. In the rest of Canada, 1.96 million person-days were lost, double the previous 5-year average.

When you see an increase in work stoppages and an even larger spike in person-days lost like we did across Canada in 2023, it means that strikes and lockouts were not only more numerous than in previous years but also lasted longer or involved more workers. The data from Quebec and the rest of Canada specifically shows that the 2023 labour actions involved more workers. We know this because the average duration of work stoppages actually declined in 2023.

We only have data for the first five months of 2024, but so far, the number of person-days lost has returned to pre-2023 levels. Nevertheless, the dramatic rise in work stoppages and person-days lost in 2023, especially in Quebec, highlights the significant role that collective action plays in protecting workers' rights during challenging economic periods. For public sector workers, this serves as a clear reminder of the power we hold when we stand together.

As economic pressures continue, we must remain vigilant and prepared to use every method at our disposal to secure fair wages and working conditions.

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