

Federal Expenditures in Canada:  
The Millennial Vision and its Tensions

Lars Osberg  
Department of Economics  
Dalhousie University

June 14, 2000

I would like to thank Lynn Lethbridge for her exemplary work on this project and the Social Sciences and Humanities Research Council of Canada for its financial support under Grant 010-97-0802.

The Budget Plan tabled in the House of Commons on February 28, 2000 begins with the assertion that it “sets out the federal government’s plan for Canada in the 21<sup>st</sup> century.” To this end, it projects expenditure and revenue to 2003 and establishes a long term rule for the level of federal expenditures. Of course, there may be some level of cynicism that such a long term plan will be the victim of the priorities of the next federal re-election campaign - but this paper takes the budget at its face value. [One reason for doing so is the budget’s early announcement of future tax cuts, and its indexation of the income tax system, which builds in a constraint on future expenditure initiatives.]

This paper argues that an enduring long term vision must be both politically and economically sustainable, and the paper’s major theme is a discordance between the level and allocation of rhetorical and financial emphasis that runs through the budget speech. This discordance is produced by, and is evidence of, a gulf between popular preferences and elite opinion that poses a real problem for the long-term sustainability of current federal financial planning.

Other papers in this volume speak to the tax side of the federal accounts, but in analysing the expenditure side, it seems natural to consider first the total level of spending and then the allocation of expenditure among competing alternatives. Since a federal government budget is both a political and an economic document, this paper considers the level and allocation of both rhetorical and financial expenditure<sup>1</sup>. Underlying this approach is the hypothesis that if a plan for

---

<sup>1</sup>The measure of rhetorical discordance proposed here is the variance of the “PURC” - (Per Unit Rhetoric Cost - billions of dollars spent per page allocated in the Minister’s budget speech).

the 21<sup>st</sup> century is to endure, it will be helpful if there is some consistency between its rhetorical and actual emphases.

In the hierarchy of “big issues” of political economy, surely one of the biggest issues is the relative size of government - and the budget speech has big news. It notes (pg. 8) that “federal government spending, as percentage of GDP, is at its lowest level in 50 years. . . . program spending next year will be 4 billion dollars lower than it was when (the Liberals) took office in 1993”. The budget document continues: “Let there be no doubt - we will control spending . . . growth in program spending is projected to be in line with inflation, plus population growth”. This commitment to freeze government spending in real per capita terms implies that as per capita real GDP grows, federal government expenditure will continue to shrink as a percentage of Canada’s economy.

The importance of this announcement of a small and forever declining role for the federal government in Canadian economic and social life is hard to overstate. It means that the cuts to federal expenditures that have marked the last seven years are not to be seen as temporary belt tightening. Although Canadians were encouraged to think of expenditure restraint in terms of the necessary sacrifices needed to solve a deficit problem, Canada’s federal budget is now in surplus - but there is no intention to restore expenditure. This announcement is thus highly important - indeed historic. Surely if this was thought to be a politically popular initiative, one would have thought that the message of “reducing the size of government” would have been repeated throughout the budget document. Instead, it is mentioned only briefly on page 8 (taking up approximately 1.2% of the total length of the budget speech). Although the introduction and the

conclusion are full of rhetoric on the brighter future and better lives that await Canadians, the long term trend in the size of government receives no explicit mention in either.

The importance of the issue raises the question - why is this trend to a smaller federal government downplayed?

It should not be thought that reducing the size of the federal government has been a small achievement. As Chart 1 indicates, total federal program spending fluctuated in the range of 15% to 16.2% from 1959/60 to 1989/90 but is forecast at 11.6% in 2000/2001. In fact, from 1951 to 1994, total federal spending was only once below 14% of GDP.<sup>2</sup> In 1948/49 total federal program spending (including transfers to the provinces) was 10.3% of GDP and in 1949/50 it was 11.5%<sup>3</sup>. In sum, since the Second World War, there are only two years in which federal spending fell short of the 11.6% of GDP which is anticipated for 2000/2001 - and since federal spending will not in future reflect real per capita growth, future years will have a even lower federal share of GDP.

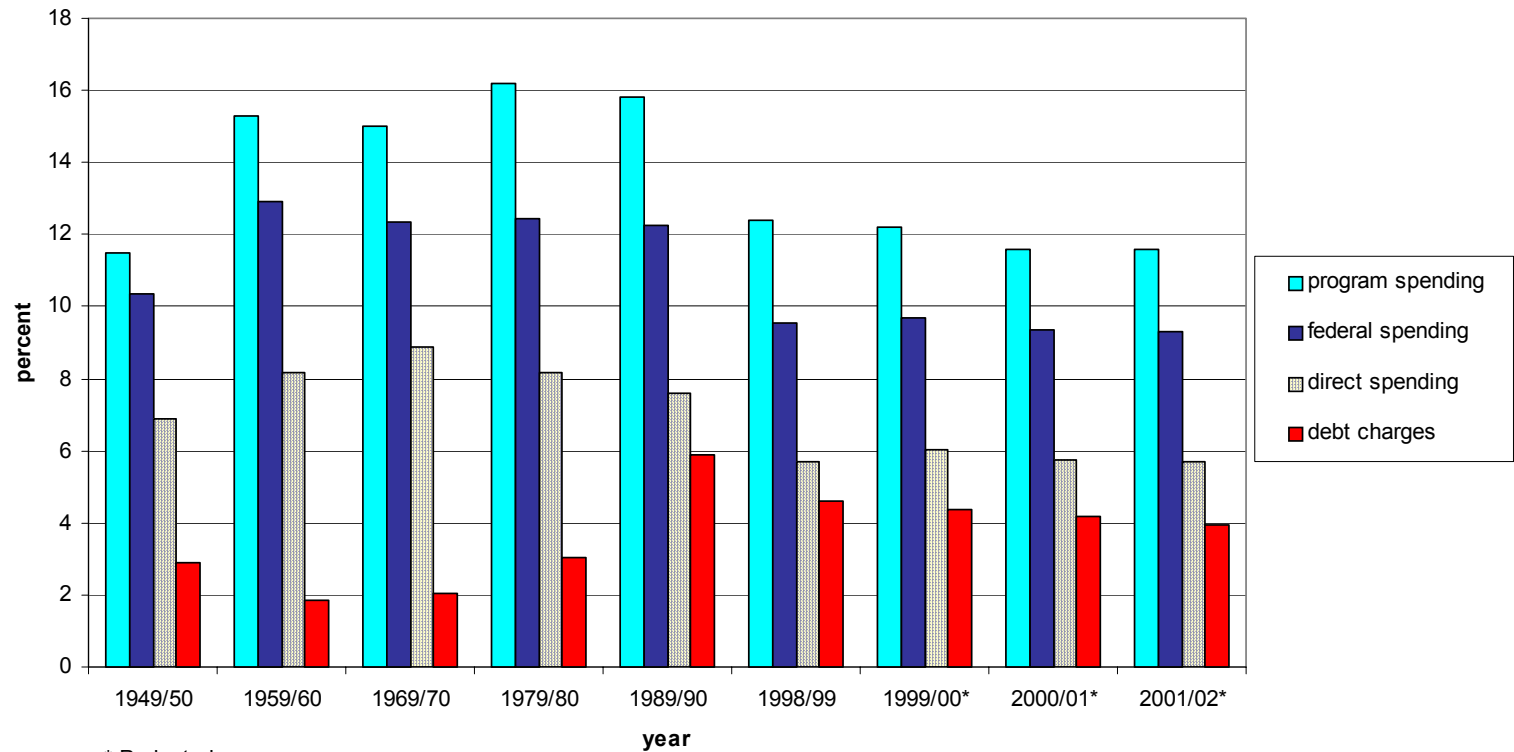
However, the 1948 to 1950 period was exceptional. 1940 - 47 was dominated by the war effort, when federal expenditure was a considerably higher fraction of aggregate national output. Hence, the federal government budget documents understate the level of achievement of program expenditure control. One really has to go back to the 1930s to find a similar span of time in which federal government expenditure has been a comparable share of aggregate Canadian GDP.

---

<sup>2</sup>In 1965-66, at 13.7% of GDP.

<sup>3</sup>All figures from Fiscal Reference Tables, available at <http://www.fin.gc.ca/afr/frm99e.pdf>

**Chart 1**  
**Federal Spending As a Percentage of GDP in Canada**



\* Projected

notes: federal spending=program spending-transfers to provinces

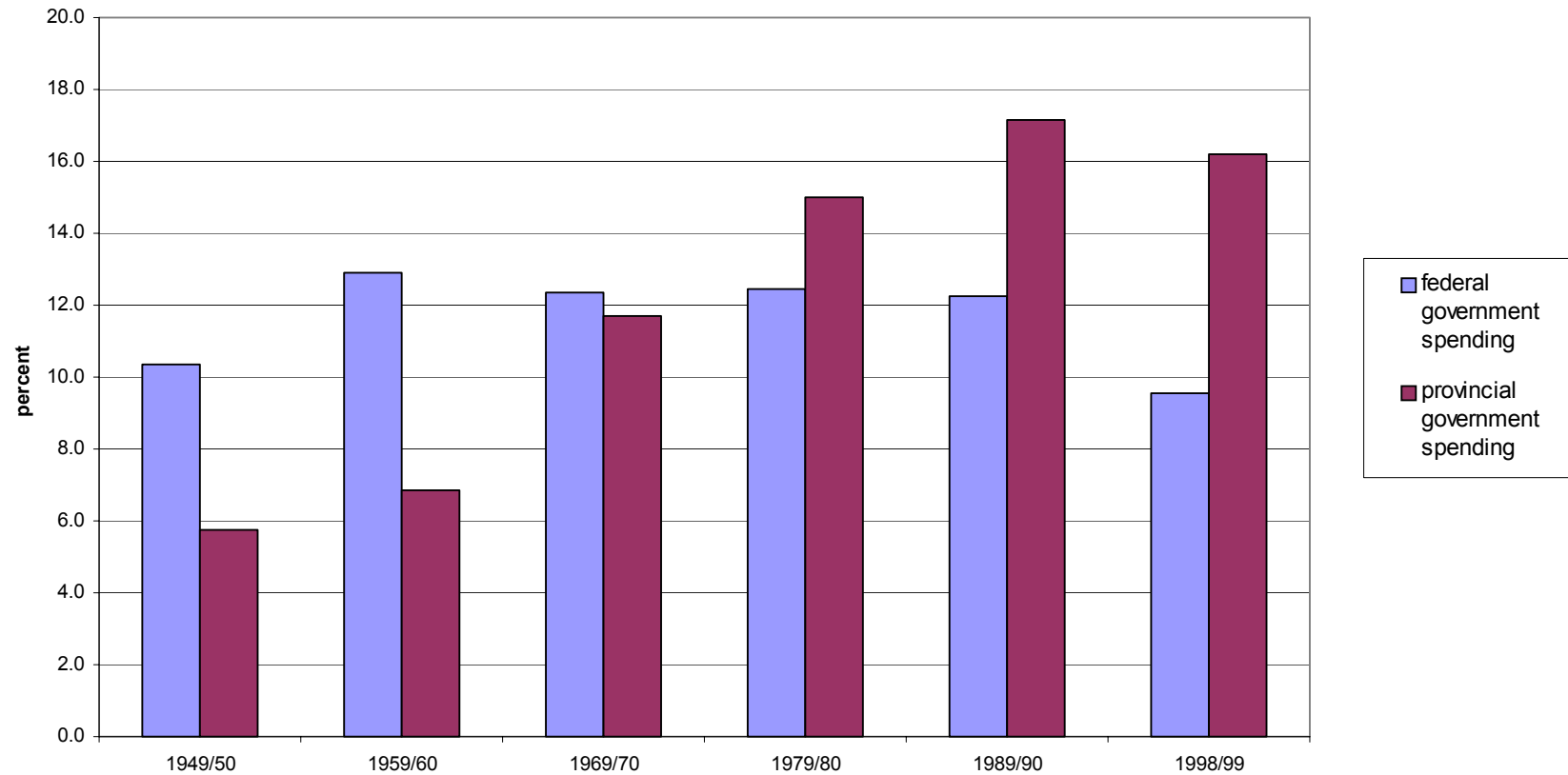
direct program spending=federal spending-transfers to individuals

Sources: <http://www.fin.gc.ca/afr/ft99e.pdf>

[http://www.fin.gc.ca/budget00/bpe/bpch1\\_2e.htm](http://www.fin.gc.ca/budget00/bpe/bpch1_2e.htm)

A Fiscal History of Canada- The Post-War years

**Chart 2**  
**Federal and Provincial Program Expenditures**  
**As a Percentage of GDP**



note: Figures exclude debt charges. Transfers to other governments are excluded from the federal figures.

Sources: <http://www.fin.gc.ca/afr/ft99e.pdf>

[http://www.fin.gc.ca/budget00/bpe/bpch1\\_2e.htm](http://www.fin.gc.ca/budget00/bpe/bpch1_2e.htm)

A Fiscal History of Canada- The Post-War years

An even stronger, and in many senses truer, picture is obtained if one nets out transfers to the provinces, and looks at what the federal government itself does. Federal expenditures on goods and services and direct transfers to individuals will be 9.3% in 2000/2001, a considerable decline from 12.2 percent in 1989/90 or 12.9 percent in 1959/60 (and one tenth less than the 10.3 percent of 1949/50). Hence, if the issue is direct contact with citizens, either through services or transfers provided, the federal government is clearly at a sixty year low.

Chart 2 graphs federal and provincial program expenditures as a percentage of GDP to make the point that although direct federal expenditure on goods and services and transfers to individuals were fairly constant as a percentage of GDP for the best part of 40 years, provincial government expenditures have grown significantly. Although in 1949/50 direct federal spending dwarfed provincial government spending (10.3% compared to 5.8% of GDP), by 1969/70 the provinces and the federal government were close to a balance and by 1989/90, federal expenditures were only about seventy percent of provincial government spending (12.2% compared to 17.1%). For the last quarter of the 20th century, the federal government was, in expenditure terms, the “junior order of government”, and the disparity in size has increased with time.

Chart 3 illustrates the fact that the Federal government in Canada is significantly smaller, as a fraction of GDP, than the federal government in the United States. Whether measured in terms of total expenditures, or program expenditures (i.e. excluding debt charges) or direct spending (i.e. excluding transfers to other levels of government), the federal government in Canada spends significantly less, as a fraction of GDP, than the federal government in the

United States. The difference cannot be explained by defence spending (which has fallen significantly in the US as a fraction of GDP). The projections of the US and Canadian budgets imply that in 2002, non-defence federal government programme spending in the US will be 12.8 % of GDP, approximately one sixth higher than the corresponding percentage in Canada.<sup>4</sup>

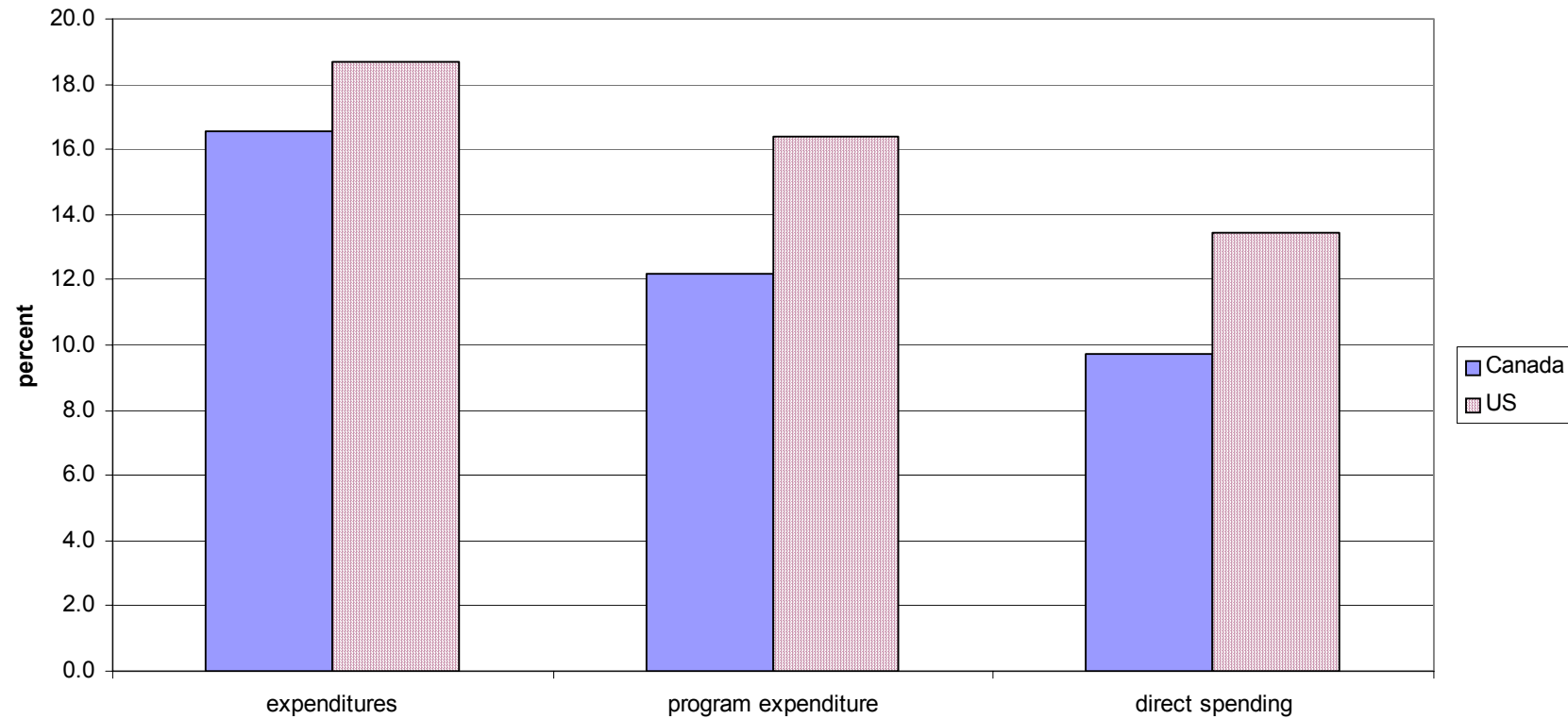
It may take a while before stereotypes of a large and overbearing federal government waste away, but in a remarkably short period of time, Canadians have gotten a smaller federal government. Whether considered as a fraction of aggregate GDP compared to previous decades, or relative to the expenditure of provincial governments, or relative to the expenditure of the United States federal government, the government of Canada is now smaller and is forecast to get smaller still.

---

<sup>4</sup> For US data see Table 3.1, Page 49; Budget of the United States Government - Historical Tables- <http://w3.access.gpo.gov/usbudget/fy2001/pdf/hist.pdf> ; for Canadian see Table 3.6, Page 66, Government of Canada (2000) Budget Plan



**Chart 3**  
**Federal Government As Percentage of GDP**  
**Canada and the US**  
**1999/2000**

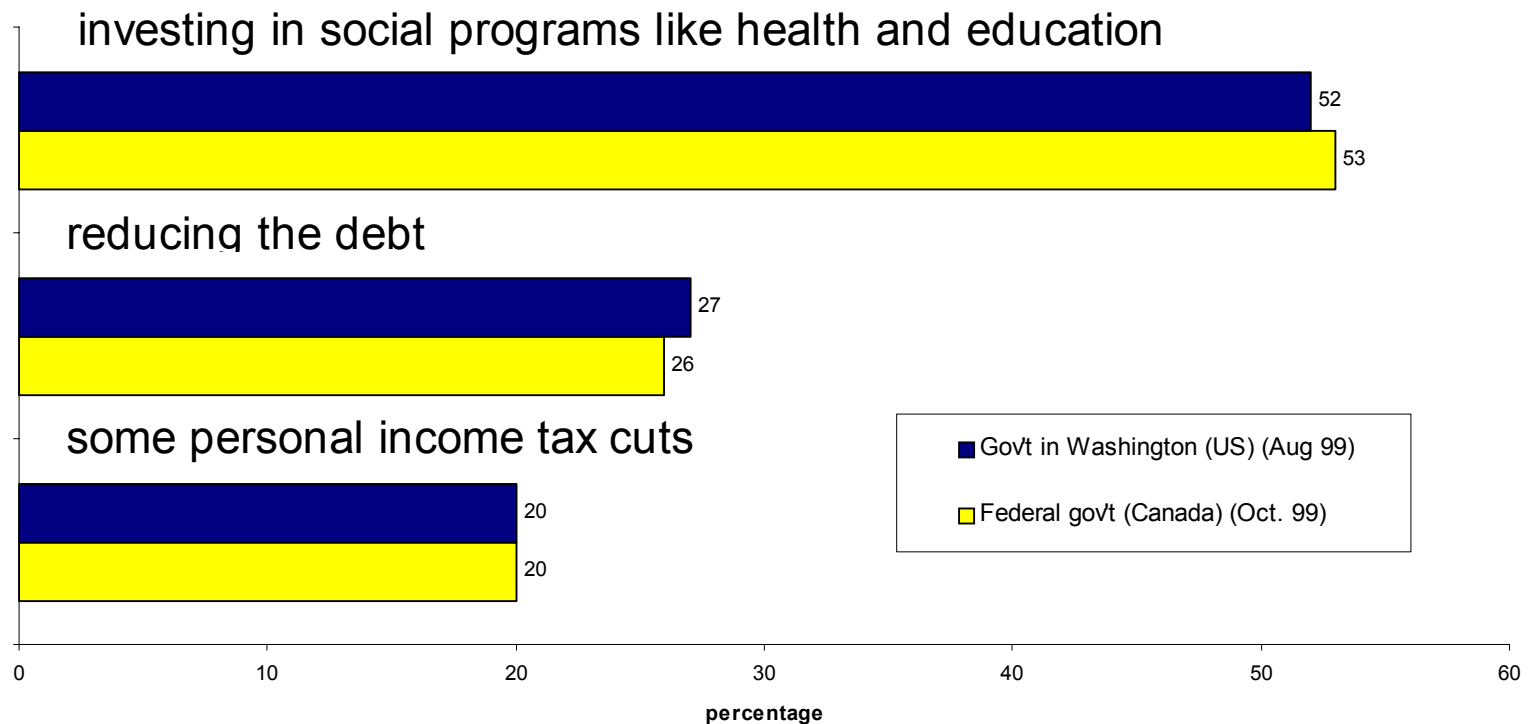


notes: program spending=total expenditure - debt charges;  
direct spending=program spending - transfers to other levels of government

Sources: <http://www.fin.gc.ca/afr/ft99e.pdf>  
<http://w3.access.gpo.gov/usbudget/fy2001/pdf/hist.pdf>

## Preferred Budget Emphasis

In planning its budget for next year, where should the ... put the most emphasis?



Source: Ekos research Associates Inc. URL: <http://www.ekos.com/press/DEC22/sld008.htm>

Canadians may be getting a smaller federal government, but is there any evidence that this is what they want? Chart 4 reproduces an EKOS poll of 1999 which indicates that American and Canadian attitudes to federal government budget planning are fundamentally similar. The wording of the question is a forced choice, in which respondents are prevented by design from saying that they want both more spending and lower taxes. A majority of both Canadians and Americans prefer increased expenditure on social programs like health and education to the alternative of either reducing the debt or cutting personal income taxes. Other polling results are quite comparable. Canadians regularly rank health care spending, education, child poverty, crime and justice, environmental degradation, improving economic productivity and unemployment above such issues as reducing the national debt or cutting the level of taxation<sup>5</sup>. Only in 1994, and only for a brief period of time, did the national debt jump into prominence above health care or unemployment as a public priority for the federal government.

In a 1997 EKOS poll, for example, between 90% and 93% of respondents stated that they wanted to see government increase or maintain its involvement in the areas of unemployment, job training, transportation safety, education, health care, job creation, environment and managing our natural resources. In every case but transportation safety, the split between those who wanted to “increase” or “maintain” government involvement was strongly for “increase” (61% to 30% for unemployment, 59 % to 32% for job training, 65% to 25% for education, 65% to 28% for health care, 65% to 26% for job creation, 57% to 37% for environment and 54% to

---

<sup>5</sup>(See EKOS Research associates (1999): *Long Term Tracking of Priorities*”) available at <http://www.ekos.com./press/dec22/sld006.htm>)

39% for managing our natural resources). An increased or maintained government role was supported by somewhat fewer when the issue was promoting international trade (89%), social assistance (81%), promoting Canadian identity and culture (78%) or immigration (70%) - but these are still substantial margins in favour of a more activist government.<sup>6</sup> Certainly there is no support in these numbers for a long term shrinkage of the federal government's role in Canadian economic and social life.

Indeed, one way of reading the Budget speech is as evidence that the Finance Minister knows that public attitudes favour greater spending to meet social problems. The Minister's budget speech itself is 21.5 pages long, much of which (pages 9 - 17) is devoted to an extended discussion of spending initiatives, under the headings of the new economy, skills and knowledge, supporting research, the environment and children. Given the rhetorical emphasis devoted to these issues, one might have thought that there would be a corresponding cash expenditure. However, the total additional spending over the next 5 years under these initiatives amounts to a rather modest 2.9 billion dollars, some 5% of the size of the tax changes simultaneously announced.

Table 1 itemizes the spending initiatives and tax changes discussed in the budget speech. Pages in the Budget Speech can be seen as an indicator of what government thinks the public wants to hear, while dollars of budget cost reflect actual choices made. Putting the political and the financial together, one can calculate the PURC ("Per Unit Rhetoric Cost" - billions of dollars

---

<sup>6</sup>See EKOS- "Rethinking Government" - detailed tables available at <http://www.ekos.com/rg971/97-1.htm> The percentage of respondents who express a preference for eliminating a government role is typically 1% to 2% - except for the cultural promotion question, which hits 7%.

of spending or tax cuts per page of budget speech) of each initiative. The disparity in PURCs can thus be seen as an index of the mismatch between words and deeds in the federal budget.

Although the federal government announced increased health and post secondary transfers of \$2.5 billion (over 4 years) and municipal infrastructure spending of \$2.1 billion, such transfers to other levels of government have limited rhetorical opportunities, and occupied in total less than a page of the budget speech. (PURC = 5 and 5.25 respectively). Expenditures on high tech initiatives such as research chairs, genome research, environmental technology and innovation centres received far more rhetoric (6.2 pages) but considerably less money. The PURC for Research Chairs was, for example, only 0.3 - less than a tenth than the PURC for intergovernmental transfers. Cash transfers to encourage research reflect an activist approach to encouraging innovation, with the hope of long term benefits to productivity - but the money involved was less than 2% of the cost of tax cuts. The really big money in the 2000 federal budget was the \$58 billion in tax changes announced, whose cost per page (PURC = 9.66) dwarfed that of all federal spending initiatives.

Table 1

## Words and Dollars: Initiatives Announced in Budget Speech

PURC <sup>1</sup>	TOTAL \$B COST	% OF TAX CUTS <sup>2</sup>		PAGES
5.00	\$ 2.5	4.31	INCREASE IN HEALTH & POST-SECONDARY TRANSFERS	0.5
5.25	\$ 2.1	3.62	MUNICIPAL INFRASTRUCTURE <sup>3</sup>	0.4
0.30	\$ 0.9	1.55	RESEARCH CHAIRS <sup>4</sup>	3
1.80	\$ 0.9	1.55	INCREASE FOR CFI	0.5
0.32	\$ 0.16	0.28	GENOME RESEARCH	0.5
0.32	\$ 0.7	1.21	ENVIRONMENTAL TECHNOLOGY	2.2
0.34	\$ 0.24	0.4	FARM AID	0.7
9.66	\$ 58		TAX CHANGES (“RELIEF”)	6

<sup>1</sup> PURC = PER UNIT RHETORIC COST = (ANNOUNCED COST \$Billion) ÷ (PAGES IN BUDGET SPEECH)

<sup>2</sup> TOTAL SPENDING OVER 5 YEARS AS % CUMULATIVE TAX REDUCTION (\$58 BILLION - P. 22)

<sup>3</sup> \$450M IN FIRST 2 YEARS + 3 YEARS @ \$550M; HEALTH & POST SECONDARY SPREAD OVER 4 YEARS; ENVIRONMENTAL TECHNOLOGY SPREAD OVER 3 YEARS

4 “NEW ECONOMY” (PAGES 9, 10) HARD TO ALLOCATE - PURC FOR ALL RESEARCH = 0.49

Why is there such an extreme imbalance between rhetoric and reality in the federal government's budget documents?

Why does the Minister of Finance feel compelled to talk so much about some things (the spending initiatives) while actually doing so much more on the tax cut front?

Why is so much attention paid to spending initiatives (which are a small share of the operations of a federal government that is shrinking in relative size), while so little attention is paid to the aggregate size of the federal government?

If it really were the case that Canadians wanted a smaller role for the federal government in Canadian social and economic life, then one would expect a reverse sort of emphasis. When one sees in the budget documents tables with headings like “Improving the Quality of Life for Canadians and their Children” and “Making Canada's Economy More Innovative”, it is clear that the presentation of the budget document has been carefully calculated so as to maximize political popularity.<sup>7</sup> Hence, it is altogether likely that the federal government knows that most Canadians want their federal government to play an activist role in meeting pressing social problems - certainly that is what their pollsters are telling them.

---

<sup>7</sup> When asked “If you were Prime Minister for a day, and had to pick an overall national goal for Canada to achieve for the year 2010, which of the following would you chose?”, respondents to an EKOS poll picked “best quality of life in the world” as their top priority followed by “best health care system”, “lowest incidence of child poverty”, and “lowest crime rate/safest community”. The option “lowest overall tax burden” was 20 percentage points below “quality of life” at number 7. See <http://www.ekos.com/press/dec22/sld007.htm>. In earlier times, budget tables headings listed the Ministry that was to be responsible for each spending initiative - information that was not presented in the February 2000 documents.

My own opinion is that Canadians would be quite willing to accept a private sector solution to social problems - if that should happen. It seems to me that the number of Canadians who are ideologically in favour of increased government involvement on principle is small (and from the polling numbers, it is clear that the number who are *in general* against government involvement is very small). My opinion is that Canadians are fairly pragmatic, and that if the trend to a smaller federal government produces good results, then it would be accepted.

However, cuts to the welfare state have been going on for some time now, and as yet there is little sign of improved living standards. Although average incomes have recently begun to revive with the decline in the unemployment rate, the Budget Plan itself notes (page 28) that real per capita income in 1999 had not yet recovered the loss of the first half of the 1990s. In average real income terms, Canadians are still worse off now than they were in 1989. Throughout the decade the concentration of income gains at the top of the income distribution has meant especially little recovery in consumption for the bulk of the population.

Furthermore, one of the implications of cuts to social assistance and unemployment insurance has been an increase in poverty in Canada, (at the same time as poverty has been falling in the USA - Osberg, 2000). Since living standards depend on the level of economic security with which individuals face the future and on the poverty and inequality that are produced by the distribution of total income, full calculation of trends in living standards shows a fall in recent years (Osberg and Sharpe, 1999). And Canadians continue to be concerned about the erosion of their “social wage” of public services - particularly health care.

If rapid and prolonged economic growth were to produce rising living standards throughout the income distribution, presumably many malcontents would be quieted. However, the prospect for such growth depends heavily on the demand management decisions of the Bank of Canada, whose sole



priority remains maintaining very low inflation. As of the time of writing (May, 2000) the Bank of Canada was demonstrating, yet again, its proclivity for strangling nascent growth by raising interest rates - even though the core inflation rate was only 1.3% (close to the bottom of the announced target range), and declining.

The more likely prognosis for the Canadian economy, therefor, is slow to moderate growth and a continuation of the chronic excess capacity that has characterized the Canadian labour market in the 1990s. It is possible that Canadian expectations are now so low that *any* growth in living standards will be interpreted as a welcome change - but one implication of “globalization” is the fact that citizens increasingly make international comparisons. Since the US Federal Reserve has successfully emphasized growth as a priority, and continues to do so, comparison with US outcomes are likely to continue to show what could have been achieved. It is therefor likely that most of the public will continue to have good reason for dissatisfaction with economic outcomes. Future years are therefor likely to see continuing tensions between a public that wants an activist government, and a policy elite that wants a shrinking federal role.

## References:

Budget of the United States Government - Historical Tables - available at

<http://w3.access.gpo.gov/usbudget/fy2001/pdf/hist.pdf>

EKOS Research associates (1999): *Long Term Tracking of Priorities*) available at

<http://www.ekos.com./press/dec22/sld006.htm>

EKOS- "Rethinking Government" - available at <http://www.ekos.com/rg971/97-1.htm>

Government of Canada (2000) *Better Finances, Better Lives: The Budget Speech 2000* Department of

Finance, Ottawa, February 28, 2000

Government of Canada (2000) *Better Finances, Better Lives: The Budget Plan 2000* Department of

Finance, Ottawa, February 28, 2000

Government of Canada (2000) Fiscal Reference Tables, available at <http://www.fin.gc.ca/afr/frt99e.pdf>

Osberg, L. (2000) "Poverty in Canada and the USA: Measurement, Trends and Implications"

Presidential Address to the Canadian Economics Association, Vancouver, June 3, 2000:

forthcoming *Canadian Journal of Economics*

Osberg, L. and A, Sharpe (2000) "International Comparisons of Trends in Economic Well Being"

(with Andrew Sharpe) American Economics Association, January

7, 2000, Boston, Massachusetts

Osberg, L. and A, Sharpe (1999) "An Index of Economic Well-Being for Canada" in Living Standards

and the Quality of Life in Canada, forthcoming University of Toronto Press, L. Osberg and A.

Sharpe (editors).

Perry, J. H. (1989) *A Fiscal History of Canada - The Post War Years* Canadian Tax Paper No. 85,

Canadian Tax Foundation, Toronto, 1989

