

Opinion | Analysis of federal budget reveals concerns about inflation and interest rate projections

By Athena Koros and Charles Smedmor, Contributors

Federal Finance Minister Freeland presented her second budget on Thursday and here are some of the key projections for the fiscal year ending March 31, 2023, with comparisons to fiscal 2022.

- Total revenues: \$408.4 billion, \$10,258 per person (up 3.5 percent over 2022).
- Total spending: \$452.3 billion, \$11,657 per person (down 9.2 percent from 2022).
- Deficit: \$52.8 billion, \$1,361 per person (down 53.9 percent from fiscal 2022).
- Interest costs, included in spending: \$26.9 billion, \$693 per person (up 13.4 percent from 2022).
- Federal debt: \$1.213 trillion, \$31,280 per person (up 4.6 percent from 2022).
- Net debt as a percentage of gross domestic product (GDP): 45.1 percent (a 1.4 percentage point improvement from 2022).
- Consumer price index (CPI) increase: 2.4 percent for 2023 (up 0.1 percentage point from the fall economic update).
- 10-year government bond rate: 2.4 percent, the same as projected inflation, (also up 0.1 percentage points from the fall economic update).

The last two budget inputs are important. Projected inflation and interest rates impact the budget's program spending and interest expense, affecting the deficit.

The budget also provides detailed projections to 2027, including a 2027 deficit of \$8.4 billion and a debt-to-GDP ratio of 41.7 percent, down 3.4 percentage points from 2023.

These desirable 2027 results depend on actual inflation and interest rates. For 2023 to 2027, this budget relies on inflation not exceeding 2.5 percent per year and long-term interest rates not exceeding 3 percent per year. Neither is likely to occur.

Inflation will not be 2.4 percent for 2023; Statistics Canada reported a 5.7 percent annual inflation rate for February 2022. The Bank of Canada is forecasting inflation of more than 5 percent.

Using problematic inflation and interest rate projections can prevent Ottawa from achieving its desired 2027 results.

- Program spending: Inflation in program spending to 2027 is projected not to exceed 2.5 percent annually. While inflation also pushes up revenues, many revenues will increase at a lower rate. Annual program spending exceeds \$400 billion. For each percentage point where inflation exceeds the budget's predicted rate, \$4 billion could be added to the annual deficit, making the 2027's target deficit of \$8.4 billion harder to achieve.
- Interest rates below market: With \$1.2 trillion in federal debt, a 1 percentage point increase in interest costs could add \$1.2 billion to the deficit.

Inflation and housing

Housing sector inflation is much higher than the overall CPI increase. Controlling housing inflation requires both decreasing the dollars bidding for real estate and increasing the available number of units. Not all budget measures will create more units, some just create more competition:

- Discouraging house flippers: the budget disallows the principal residence exemption for properties flipped in under 12 months; 24 months would be better to discourage flippers competing with ordinary Canadians.
- New Housing Accelerator Fund: This \$4 billion will allow municipalities to develop improved and speedier housing start approvals. However, faster approvals just pressure already limited construction resources, driving up labour and material costs.
- New First Home Savings Account and improved first-time Home Buyers' Amount. Both are intended to assist young Canadians with housing ownership. Both plans put more people and money into the housing market without increasing housing supply.

Fiscal 2022's results are better than anticipated thanks to efforts by Freeland and her staff. Her second budget tries to bring Canada back from the COVID-19's crisis and address Canada's housing challenges. However, Canadians need a budget with objective financial estimates and more measures to actually increase housing.

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Correction — April 14, 2022: *This column was edited to correct that the federal debt for the current fiscal year is projected to be \$1.213 trillion. The amount was misstated in a previous version.*

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