

The Fiscal Monitor

A Publication of the Department of Finance

Highlights of financial results for March 1997

Deficit of \$1.8 billion reported in March 1997

The deficit for March 1997 was \$1.8 billion, up \$0.6 billion from March 1996. This year-over-year increase was largely attributable to higher personal income tax refunds (\$0.7 billion), which depressed net personal income tax collections, lower corporate income tax collections (\$0.3 billion) and the inclusion of the funding for the Canada Foundation for Innovation (\$0.8 billion), as announced in the February 1997 budget. However, offsetting much of the impact of these factors on the deficit were unusually high goods and service tax (GST) collections (\$0.8 billion), primarily reflecting the fact that last year a significant portion of GST revenues that accrued in March were reported in the end-of-year accounting period.

Deficit for 1996-97

Year to date

Over the period April 1996 to March 1997, the deficit stood at \$9.6 billion, down \$14.8 billion from the same period in 1995-96.

- Budgetary revenues were up \$8.9 billion or 6.9 per cent, on a year-over-year basis. Over half of this improvement was due to special factors, such as the higher personal income installment payments, the acceleration of employment insurance premium payments, the sale of the air navigation system, and the timing of GST collections.
- Program spending was down \$4.0 billion or 3.8 per cent, primarily reflecting the impact of the restraint measures introduced in the 1994 and 1995 budgets.
- Public debt charges were down by \$1.9 billion, or 4.1 per cent. This reflected declines in interest rates, especially short-term rates.

Final results to come in the fall

The financial results for the April 1996 to March 1997 period are not the final results for the 1996-97 fiscal year. Still to come are the regular end-of-year accounting adjustments.

- Consistent with government accounting principles, these "end-of-year accounting" adjustments incorporate increases to program spending to include the costs of liabilities incurred during the fiscal year for which no payments were made in 1996-97. Adjustments are also made to budgetary revenues, primarily to reflect cash-in-transit at year end.
- The deficit impact of these "end-of-year accounting" adjustments over the last three fiscal years has ranged from \$4 billion to \$6½ billion.
- The results to the end of March 1997 suggest that the deficit for the year as a whole will be no higher than \$16 billion.

The final audited financial results will be available in the *Annual Financial Report*, scheduled for release in the fall of 1997.



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Table 1

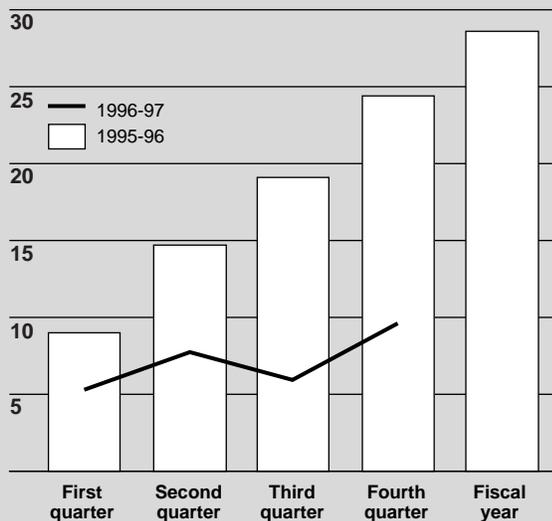
Summary statement of transactions

	March		April to March	
	1996	1997	1995-96	1996-97
	(millions of dollars)			
Budgetary transactions				
Revenues	12,507	12,422	128,432	137,312
Program spending	-9,696	-10,434	-106,239	-102,198
Operating surplus	2,811	1,988	22,193	35,114
Public debt charges	-3,991	-3,798	-46,654	-44,750
Deficit/surplus	-1,180	-1,810	-24,461	-9,636
Non-budgetary transactions	-586	1,967	7,532	10,768
Financial requirements/source (excluding foreign exchange transactions)	-1,766	157	-16,929	1,132
Foreign exchange transactions	-3,182	-2,058	-4,738	-7,524
Total financial requirements	-4,948	-1,901	-21,667	-6,392
Unmatured debt transactions	8,168	6,377	28,533	7,192

Note: Positive numbers indicate net source of funds. Negative numbers indicate net requirement for funds.

The federal deficit 1995-96 and 1996-97

Year to date
billions of dollars



Budgetary revenues up \$8.9 billion

Over the April 1996 to March 1997 period, budgetary revenues were up \$8.9 billion or 6.9 per cent, on a year-over-year basis. However, more than half of this increase was attributable to one-time factors, with the result that the underlying year-over-year increase in revenues is about 3 per cent. This increase is in line with the 1996 increase in nominal income of 2.8 per cent.

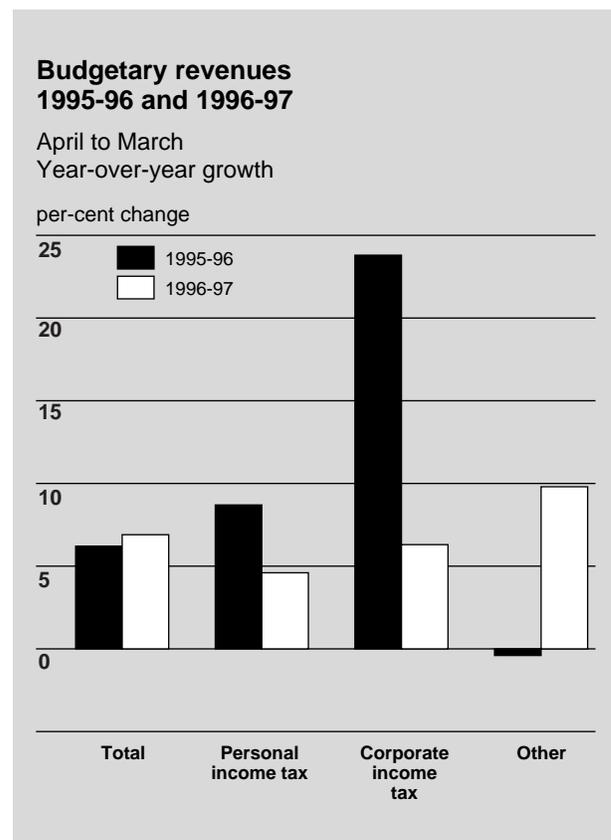
- Personal income tax collections were up 4.6 per cent or \$2.8 billion. Over half of this increase relates to taxes paid on filing and quarterly installment payments. Taxes paid on filing in 1996-97 pertain to developments affecting the 1995 taxation year. The sharp increase in quarterly installment payments was largely due to more taxpayers being required to make tax installment payments on income not subject to withholding. In previous years, such tax liabilities would be remitted at the time of final tax filing. As such, the higher installment payments represent a one-time acceleration of taxes from 1997-98 into 1996-97. Partially offsetting the impact of these factors were higher refunds processed in March 1997 relating to the 1996 taxation year, resulting from higher average refunds rather than more returns being processed. In contrast, deductions from employment income were up only about 2 per cent, in line with the growth in wages and salaries during 1996.

Table 2

Budgetary revenues

	March		April to March		Per cent change (%)
	1996	1997	1995-96	1996-97	
	(millions of dollars)				
Income taxes					
Personal income tax	3,650	2,948	60,423	63,175	4.6
Corporate income tax	3,459	3,131	15,148	16,102	6.3
Other	150	175	1,928	2,120	0.7
Total income tax	7,259	6,254	77,499	81,726	5.5
Employment insurance premiums	1,466	1,866	18,480	19,800	7.1
Excise taxes and duties					
Goods and services tax	1,014	1,765	15,211	16,658	9.5
Customs import duties	276	204	2,805	2,503	-10.8
Other excise taxes/duties	702	595	7,095	8,028	13.2
Total excise taxes and duties	1,992	2,564	25,111	27,189	8.3
Total tax revenues	10,717	10,684	121,090	128,715	6.3
Non-tax revenues	1,790	1,738	7,342	8,597	17.1
Total budgetary revenues	12,507	12,422	128,432	137,312	6.9

- Corporate income tax collections were up 6.3 per cent, or \$1.0 billion. About 25 per cent of net collections are received in March, given the remittance regulations for large corporations. Although March 1997 collections were only marginally lower than those reported in March 1996, the high monthly installment payments during 1996-97 resulted in an increase in net collections for the year as whole. The growth in net collections to date significantly exceeded the reported growth in corporate tax liabilities which, for 1996, was about the same as in 1995.
- Employment insurance premiums were up 7.1 per cent, or \$1.3 billion. However, most of this increase was attributable to changes to the base on which premiums are levied, from weekly maximum insurable earnings to annual maximum insurable earnings, effective January 1, 1997. This results in a one-time increase of about \$1 billion in receipts in the final quarter of 1996-97. This change does not affect the amount paid by employees and employers for the calendar year as a whole. Those employees earning up to the annual maximum insurable earnings are not affected, while those earning above the maximum will pay more of their premium liability earlier in the calendar year and less at the end.
- Net GST collections were up 9.5 per cent, or \$1.4 billion. Over half of this increase occurred in March 1997, primarily reflecting the timing of gross



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receipts. The remittance date for filing is the last day of the month or the first working date following a holiday. In March 1996, the filing date fell on a Sunday, with the result that a large portion of the March 1996 collections were received in early April 1996 and recorded in the 1995-96 end-of-year accounting period. Although the filing date fell on Easter Monday this year, most financial institutions were open, such that collections were received on that day. As a result, net collections were up 74 per cent in March 1997 compared to March 1996. Once the end-of-year accounting periods are included, the annual growth in GST collections should be more in line with the growth in domestic demand of about 3 per cent.

- The increase in sales and excise taxes (up 13.2 per cent, or \$0.9 billion) was largely attributable to a classification change related to the air transport tax. Prior to April 1996, receipts from this tax were netted against costs of running the airports and netted against program spending. With the sale of the air navigation system, these receipts are now part of sales and excise taxes. Since this reclassification affects both revenues and program spending, the deficit is unaffected by this change.
- Non-tax revenues were up 17.1 per cent, or \$1.3 billion. However, this increase is more than accounted for by the net proceeds from the sale of the air navigation system.

Budgetary expenditures down \$5.9 billion

Over the April 1996 to March 1997 period, total budgetary expenditures, which include both public debt charges and program spending, were down \$5.9 billion, or 3.9 per cent. This decline was due to both lower public debt charges and lower program spending.

Public debt charges down \$1.9 billion

Public debt charges were down \$1.9 billion or 4.1 per cent. This decline reflected lower interest rates, especially short-term rates. Fiscal restraint by federal and provincial governments and continued low inflation have provided the necessary conditions for interest rates to come down.

Program spending down \$4.0 billion

Program spending declined by \$4.0 billion, or 3.8 per cent in the April 1996 to March 1997 period, compared to the same period last year. This decline primarily reflects the impact of the 1994 and 1995 budget measures to reduce and restructure federal government spending, affecting all major components of program spending.

- Major transfers to persons (elderly and employment insurance benefits) were down \$0.5 billion or 1.5 per cent. All of this decline was due to lower employment insurance benefits, primarily due to the impact of reform measures. Elderly benefits were

up 2.7 per cent, reflecting increases in the number of people receiving benefits and increases in the average benefit, which is fully indexed to changes in the consumer price index.

- In the February 1995 budget, the government announced that, on April 1, 1996, the Canada Health and Social Transfer (CHST) would replace the Canada Assistance Plan and Established Programs Financing. In order to give provinces time to plan for these changes, total entitlements – the most appropriate measure of federal support – were largely unaffected in 1995-96. As a result, total entitlements under the CHST, equalization and other transfers to provinces and territories increased by 1.3 per cent in 1995-96. In 1996-97, total transfer entitlements were reduced by 7.7 per cent in 1996-97. It is important to note that transfers are delivered to provincial governments in two fashions – tax transfers and cash transfers. The tax transfer component represents the value of “tax room” which the federal government made available to provincial governments by reducing federal tax rates so that provinces could increase their tax rates by an equivalent amount, with no impact on the taxpayer. The value of the tax transfer component continued to increase at a relatively rapid 5.1-per-cent rate in 1996-97, reflecting the growth in the applicable tax bases. To the end of March 1997, the cash transfer, which is the difference between the total entitlement and an increasing value in the tax point transfer, consequently declined by 16.7 per cent. This decline overstates the decline expected for the fiscal year as a whole. In 1995-96, payments under the

Budgetary expenditures 1995-96 and 1996-97

April to March
Year-over-year growth

per-cent change

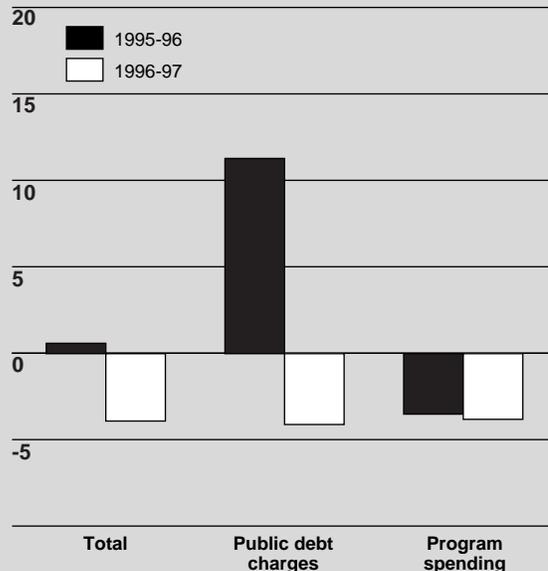


Table 3

Budgetary expenditures

	March		April to March		Per cent change
	1996	1997	1995-96	1996-97	
	(millions of dollars)				(%)
Transfer payments to:					
Persons					
Elderly benefits	1,781	1,841	21,023	21,594	2.7
Employment insurance benefits	1,403	1,176	13,441	12,352	-8.1
Total	3,184	3,017	34,464	33,946	-1.5
Other levels of government					
Canada Health and Social Transfer	1,169	1,051	18,713	14,911	-20.3
Fiscal transfers	1,000	661	10,164	9,533	-6.2
Alternative payments for standing programs	-163	-167	-1,956	-2,012	2.8
Total	2,006	1,545	26,921	22,432	-16.7
Subsidies and other transfers					
Agricultural subsidies	125	90	670	904	34.9
Indian and Inuit programs	188	162	3,314	3,369	1.7
Regional development	92	126	611	552	-9.7
Science and technology	173	143	1,286	1,106	-14.0
International assistance	275	316	1,781	1,755	-1.5
Veterans' pensions/allowances	115	113	1,385	1,363	-1.6
Other	502	2,074	5,200	6,615	27.2
Total	1,469	3,025	14,246	15,673	10.0
Total transfers	6,659	7,587	75,632	72,053	-4.7
Payments to Crown corporations					
Canadian Broadcasting Corporation	73	100	1,171	997	-14.8
Canada Mortgage and Housing Corporation	193	197	1,981	1,898	-4.2
Other	167	108	1,448	1,220	-15.8
Total	433	405	4,600	4,115	-10.5
Operating and capital expenditures					
Defence	871	687	9,362	8,712	-6.9
All other departmental expenditures	1,733	1,755	16,645	17,318	4.0
Total	2,604	2,442	26,007	26,030	0.1
Total program expenditures	9,696	10,434	106,239	102,198	-3.8
Public debt charges	3,991	3,798	46,654	44,750	-4.1
Total budgetary expenditures	13,687	14,232	152,893	146,948	-3.9

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Table 4

The deficit and financial source/requirements

	March		April to March	
	1996	1997	1995-96	1996-97
	(millions of dollars)			
Deficit	-1,180	-1,810	-24,461	-9,636
Loans, investments and advances				
Crown corporations	-189	-4	3,367	874
Other	-64	-54	-321	-465
Total	-253	-54	3,046	409
Specified purpose accounts				
Canada Pension Plan Account	435	467	254	117
Superannuation accounts	2,545	2,570	8,380	8,751
Other	210	87	506	528
Total	3,190	3,124	9,140	9,396
Other transactions	-3,523	-1,099	-4,654	963
Total non-budgetary transactions	-586	1,967	7,532	10,768
Financial source/requirements (excluding foreign exchange transactions)	-1,766	157	-16,929	1,132

Table 5

Financial source/requirements, foreign exchange and unmatured debt transactions

	March		April to March	
	1996	1997	1995-96	1996-97
	(millions of dollars)			
Financial requirements (-) / source (+) (excluding foreign exchange)	-1,766	157	-16,929	1,132
Foreign exchange transactions				
Net international reserves	-3,182	-2,058	-4,738	-7,524
Total financial requirements/source	-4,948	-1,901	-21,667	-6,392
Unmatured debt transactions				
Marketable bonds	366	-1,989	28,574	32,414
Canada Savings Bonds	-279	-259	31	2,076
Treasury bills	5,700	7,000	1,650	-30,700
Other	2,249	1,431	-1,761	3,250
Subtotal	8,036	6,183	28,494	7,040
<i>Less:</i>				
Government's holding of unmatured debt	132	194	39	152
Total unmatured debt transactions payable in Canadian dollars	8,168	6,377	28,533	7,192
Change in cash balance	3,220	4,476	6,866	800

Table 6

Cash, unmatured debt and debt balances: at March 31

	1996	1997
	(millions of dollars)	
Cash balances at end of period		
In Canadian dollars	8,468	9,254
In foreign currencies	290	89
Total cash balance	8,758	9,343
Unmatured debt balance		
Payable in Canadian dollars		
Marketable bonds	252,613	282,436
Canada Savings Bonds	31,417	33,503
Treasury bills	166,100	135,400
Other	3,478	3,467
Subtotal	453,608	454,806
<i>Less:</i>		
Government's holdings of unmatured debt	955	883
Total	452,653	453,923
Payable in foreign currencies		
Marketable bonds	9,501	12,257
Notes and loans	310	2,121
Canada bills	6,985	8,436
Subtotal	16,796	22,814
<i>Less:</i>		
Government's holdings of unmatured debt	0	0
Total unmatured debt	469,449	476,737

Youth Allowances Recovery program were netted against this component in the end-of-year accounting period. This fiscal year, they were received in March, thereby overstating the overall year-over-year decline. For the year as a whole, cash transfers are expected to decline by 14½ per cent.

- Excluding major transfers to persons and other levels of government, all other spending, or direct program spending, increased by \$1 billion, or 2.2 per cent. Of this increase, \$0.7 billion relates to the reclassification of the air transport tax to budgetary revenues. Putting both years on a comparable basis reduces the underlying growth rate to 0.6 per cent. This component includes subsidy and other transfer payments, payments to Crown corporations, and the operating and capital costs of departments, including Defence. Unlike the reduction to entitlements to other levels of government, which took effect in 1996-97, this component of program spending declined by 10 per cent in 1995-96, reflecting the major reductions announced in the 1994 and 1995 budgets. In the February 1997 budget, an increase of 1.4 per cent was assumed for this component.
- Within direct program spending, subsidies and other transfers were up \$1.4 billion. Most of this increase was attributable to the commitment made in the

February 1997 budget to invest \$0.8 billion in the Canada Foundation for Innovation. Legislation creating the Foundation was introduced in March and Royal Assent has since been received. The increase in agricultural transfers primarily reflected higher matching contributions to the Net Income Stabilization Account. Payments to Crown corporations declined \$0.5 billion, while defence spending was down \$0.7 billion. All other departmental expenditures were up \$0.7 billion, but this was entirely attributable to the reclassification of the air transport tax.

Financial source (surplus) of \$1.1 billion reported in 1996-97

Financial source/requirements measure the difference between cash coming in to the government and cash going out. Financial source/requirements – for the fiscal year as a whole – are lower than the deficit, as they also include non-budgetary transactions. The latter includes transactions in loans, investments and advances, government employees' pension accounts, other specified accounts, and other financial assets and liabilities. Unlike the deficit, financial source/requirements are largely unaffected by the end-of-year accounting adjustments.

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Non-budgetary transactions in the April 1996 to March 1997 period resulted in a net source of funds amounting to \$10.8 billion, compared to a net source of \$7.5 billion recorded in the corresponding period of 1995-96. The results to date were affected by extraordinary receipts. Final installment payments relating to the 1995 sale of Canadian National Railways and shares in Petro Canada resulted in the receipt of about \$2 billion in 1996-97. Under the government's accounting principles, the deficit impact of these sales was recorded in 1995-96, when the sales occurred. These final installment payments, therefore, had no impact on the 1996-97 deficit but provided additional cash in 1996-97.

With a deficit of \$9.6 billion and a net source of funds from non-budgetary transactions of \$10.8 billion, there was a net financial source (surplus), excluding foreign exchange transactions, of \$1.1 billion, compared to a net requirement of \$16.9 billion in 1995-96. This is the first net financial source (surplus) since 1969-70. However, as noted above, there were a number of special one-time factors, which impacted favourably on the deficit and non-budgetary transactions during 1996-97.

The purpose of the Exchange Fund Account is to promote order and stability in the foreign exchange market. It fulfills this function by buying foreign exchange (selling Canadian dollars) when there is upward pressure on the value of the Canadian dollar and selling foreign exchange (buying Canadian dollars) when there is downward

pressure on the currency. In 1996-97, foreign exchange transactions resulted in a net requirement of \$7.5 billion, compared to a net requirement of \$4.7 billion in 1995-96.

As a result, total financial requirements, including foreign exchange transactions, were \$6.4 billion in 1996-97, compared to \$21.7 billion in 1995-96.

To finance these requirements, the government borrows from the private credit markets and/or draws down its cash reserves. In 1996-97, the government's net new borrowings from the private credit markets (unmatured debt transactions) amounted to \$7.2 billion, compared to \$28.5 billion in 1995-96. Cash balances were increased slightly (\$0.8 billion), to reach \$9.3 billion by March 31, 1997.

The Debt Servicing and Reduction Account

In June 1991, legislation to establish the Debt Servicing and Reduction Account received Royal Assent. As a result, effective April 1, 1991, all goods and services tax revenue net of the applicable input tax credits, rebates, and the low-income credit, along with the net proceeds from the sale of Crown corporations and gifts to the Crown identified for debt reduction must, by law, go directly to the Debt Servicing and Reduction Account. The funds in this Account can only be used to pay the cost of servicing the public debt and ultimately to reduce the debt. The Account is audited on an annual basis by the Auditor General of Canada.

Table 7

Debt Servicing and Reduction Account (DSRA)

	1991-92	1992-93	1993-94	1994-95	1995-96
	(millions of dollars)				
Gross GST collected	29,564	30,516	32,652	36,715	38,048
Less:					
Refunds and rebates	11,330	12,138	14,271	17,112	18,874
Quarterly low-income tax credit	2,262	2,503	2,685	2,816	2,799
Net GST	15,168	14,868	15,696	16,787	16,374
GST penalties and interest received	19	71	90	129	135
Gains from wind-up of interest in Crown corporations/disposal of shares in Crown corporations	2	110			325
Gifts to the Crown	0.4	0.1	0.2	0.5	0.3
Proceeds to the DSRA	15,190	15,050	15,786	16,916	16,835

Figures to 1995-96 are from the *Public Accounts of Canada*.

Note: Numbers in this newsletter may not add due to rounding.

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