

November 20, 2009

Speech by the Honourable Jim Flaherty, Minister of Finance, to the Canadian Club of Toronto and the Empire Club of Canada

Toronto, Ontario

I want to thank the Empire Club and the Canadian Club for the opportunity to be here today.

I want to talk today about two things. First, I want to look back at what has been a trying time for the entire global economy in the past year and second, spell out what's next in our Government's plans to ensure a solid recovery and long-term prosperity for Canadians.

The past year was consumed by a global crisis. This economic crisis did not originate in Canada; it originated globally. But it has had a serious effect on our economy.

We had to act swiftly and decisively earlier this year in the midst of a faltering global economy and an international financial system that was on the verge of collapse. This action required leadership, discipline and tough choices.

We listened to Canadians and we listened to Canadian businesses, large and small. Then we acted boldly and quickly.

Our Economic Action Plan is working. Today, there are some tentative indications of recovery. But even with these early positive signs, there's still little evidence of firm, entrenched growth.

So we have more challenges ahead. We must see our Economic Action Plan through to ensure that a recovery takes hold. We will continue to exhibit the leadership, discipline and tough choices that have put us on the right track to recovery.

I would like to say a few words about where we've been in the past year. I hope I've seen the last of international finance meetings this year. I was in St. Andrews about 10 days ago to meet with my G20 colleagues, and then last week I was in Singapore to meet with my APEC colleagues. Finance Ministers have been meeting very frequently, as have our Leaders.

We had to act decisively. The global economy we're all connected to has not faced a greater challenge since the Second World War. Over the past year, I sat at many a conference table hearing warnings of banks too big to fail that were failing, or markets that may not open as investor confidence evaporated.

I can assure you that these risks were real. What kept this catastrophe from unfolding were decisions no one had ever thought we would have to make.

For example, about 13 months ago, on Friday, October 10, 2008, we were in the midst of a federal election campaign here in Canada. And it was on that morning that I announced some support for our banks—that we would acquire some insured mortgages, provide liquidity to our banks, try to level the playing field because, as you will recall, governments around the world were offering various types of support to their banks. We did not have to use taxpayers' money, unlike most of our allies.

In the afternoon, I was in the Cash Room of the United States Treasury with then Secretary of the Treasury Hank Paulson and my other G7 colleagues. The meeting began with a declaration

that we were all in deep trouble and that we needed to speak frankly to each other.

We tore up the communiqué and had a very frank discussion. It was the most direct and frank discussion I've ever seen in my four years or so as Finance Minister, with some recriminations toward the Americans because of the fact that Lehman Brothers had been permitted to fail. There were recriminations with respect to some of the European banks that were highly leveraged and that had participated in the purchase of some of those assets that later turned out to be toxic.

We all agreed that we had to act. There was concern that the markets would not open on Monday. There was concern that, in particular in the UK, some banks would not open and there would be a run on British banks. And there were some other concerns in the United States and in Europe.

So we developed a five-point plan. I insisted to some of my colleagues that we get this on one piece of paper and that we get the support of the G20, the IMF and the World Bank over the weekend, which we did.

The five points were as follows:

- We would not allow any systemically important financial institution to fail.
- Secondly, we would do whatever had to be done to unfreeze credit and money markets.
- Thirdly, we would re-establish confidence and lending by whatever means necessary.
- Fourth, confidence in national deposit and guarantee programs would be assured no matter how bad the crisis became.
- And finally, all of us would restart secondary markets for mortgages and other securitized assets.

These weren't empty promises. The next morning at 7 a.m. we met with President Bush, and he supported what we had done immediately following that meeting. We then had meetings with the IMF, the World Bank, the G20 and the Finance Ministers of the Americas, all on the Saturday. So by Saturday night, we had agreement among all of the major economies that we would comply with this five-point plan.

This worked. The markets opened and things were more stable during the following week and the weeks after that.

We did realize full well the potential consequences of these open-ended commitments. We chose to act the way we did. The costs of not acting would have been disastrous.

Following these tough decisions, others emerged.

Leaders and Finance Ministers of the G20 nations have met frequently in the past year and have continued to apply these basic principles so that we can ensure that we don't fall back into recession.

A key element of these efforts was a commitment to use extraordinary fiscal stimulus to prevent economic collapse, and this is something that we've all agreed on together in the G20. So our

stimulus package in Canada is vital to G20 members, all of whom have acted to create fiscal stimulus. As I say, this is the most difficult year for the world economy since World War II. This is a synchronized global recession that we have not seen before.

We had to ensure that all nations immediately provided meaningful fiscal stimulus and that each nation's economic boost would work in sync with others. Our approach had to be ambitious enough to deal effectively with an unprecedented crisis. And the risk here was not doing enough, including in Canada. And, yes, we're running a deficit and the question was how large should the deficit be. The danger was we would not stimulate the Canadian economy enough and we would slide back into recession.

So for all nations, tough decisions had to be made in a very brief period of time.

Our discussions worked. The world pulled itself back from the brink. Today the state of the global economy is still fragile but the global downturn has stabilized.

It is also clear that throughout this recession, Canada has managed better than most countries in the world. Because of the actions we had previously taken, we entered this crisis from a position of strength.

Canada prepared for a global crisis by paying down debt in good times. We paid down about \$38 billion worth of debt in the first three years of our Government. This helped put us in good shape as we faced this global recession.

In October, the International Monetary Fund projected that Canada's total government net debt-to-GDP ratio would reach 28 per cent this year. Now compare that with our partners in the G7. The net debt ratio in the United Kingdom and the United States hovers around 60 per cent of GDP. In Germany and France the ratio is closer to 70 per cent. For Japan and Italy, net debt is approaching or tops 100 per cent of GDP.

More significantly, the IMF also projects that our net debt will be only 1 per cent of GDP higher by 2014. On average, net debt in other G7 countries will rise by 25 per cent of GDP.

So be proud of your country's fiscal performance. We are doing relatively well, including vis-à-vis the United States. One person unemployed is one person too many in Canada, but our unemployment rate is about 8.6 per cent. The U.S. unemployment rate is about 10.2 per cent. We have never had a gap that large in the last generation, in fact since 1975, in favour of Canada.

The balance sheets of Canadian corporations and households are in a stronger position than in the United States as well. During the crisis, our banks, our other financial institutions and our regulatory system kept getting noticed, and for all the right reasons.

Our system was deemed the world's soundest by the World Economic Forum for two years running. Our financial system withstood the crisis. Our financial institutions remain sound, well capitalized and less leveraged than their international peers.

Our prudent actions in better times gave us a true fiscal advantage when the difficult times came. It provided us with the possibility of providing one of the largest economic stimulus packages in the G20 without mortgaging our children's future.

When the times demanded it, our country acted boldly, drafting a budget in record time and delivering the earliest budget in the history of our country on January 27th this year. The \$61-billion Economic Action Plan went above and beyond our G20 commitment, estimated at 4 per cent of GDP over 2009 and 2010. That includes the provinces and the territories and their stimulus spending.

And again, you can be proud of your country because in a time of crisis all of the provinces and territories have cooperated with the Government of Canada to provide this stimulus across the board, recognizing how essential it is. The injection of stimulus is the largest in the G7. It is among the largest stimulus packages in the G20.

The Economic Action Plan was intended as an immediate jolt to the nation's economy while being ever mindful of our country's long-term future. It includes permanent tax reductions and help for the unemployed, and we've continued to do that because we've seen the reality of long-tenured workers falling off the system, so we have provided more benefits. The Plan provides for the creation and preservation of jobs through massive infrastructure spending across the country; investments in innovation through improved infrastructure at colleges and universities and support for research and technology; support for industries and communities most affected by the global downturn, including in the auto sector and the forestry sector; and improved access to affordable financing for Canadian households and businesses.

The Economic Action Plan went further and did more than any budget before it. It had to.

After preparing the earliest budget in Canadian history, we wasted no time in implementing it. As indicated in our Third Report to Canadians, 90 per cent of this year's Action Plan stimulus was committed as of September this year.

The Extraordinary Financing Framework was fully operational less than five months after the budget was tabled. Personal income tax reductions and enhanced EI benefits have been in effect since April. As of September, 7,500 infrastructure projects were identified. More than 4,000 of these are already underway. There's no question that this far-reaching, expedited process has helped us to stabilize the Canadian economy.

So where are we now? Our housing market is growing. Auto sales are increasing. Employment, while still far too low, appears to have stabilized. According to Statistics Canada, growth in government capital investment almost doubled in the second quarter of 2009 after being on a downward trend for more than a year.

Canada's Economic Action Plan has been hailed internationally as large, timely, well diversified and structured for maximum effectiveness. Just last week, the IMF concluded that Canada's

resiliency during a global crisis is due to strong and credible policies that were introduced when they were needed most.

There's one more report to come in early December—our Fourth Report to Canadians on the stimulus package this year. The Economic Action Plan is making a real difference in communities across Canada. It is protecting and creating jobs, building and improving vital infrastructure and housing, which is a long-term benefit, and keeping us at the front of the global pack with a competitive tax system.

As of 2013, with the cooperation of most of the provinces, the combined corporate tax rate in most parts of Canada will be 25 per cent. We started off federally at about 22 per cent. We'll be down to 15 per cent by 2012–2013. Most of the provinces will be at 10 per cent or lower by that time, so we will have a 25-per-cent corporate tax rate in most of the country by 2013, including in Ontario.

In terms of the implementation of the Economic Action Plan, it is a two-year plan and we are not yet through the first year. So in preparing next year's budget, I have no doubt that we will stay the course, that we will continue with the implementation of the Economic Action Plan into early 2011, which was the plan from the outset.

Now I have no doubt our Government will hear calls to change course. This shortsightedness completely overlooks everything our sound plan has achieved so far.

We don't want to switch gears now. This is a crucial time. It would be misguided for us to take that approach now, and we will not waver from the course that we have embarked on. It would also be an abdication of our commitment in the G20, where our fellow countries are going ahead with their stimulus packages continuing into 2010.

Which is why I will be as clear as I can today on what is in store for the 2010 federal budget.

This will not be the usual budget. It will be a budget that completes the implementation of economic stimulus that's among the largest in the world, which will complement the fiscal measures of other nations in the G20.

The budget will support Canadian families and businesses. The Economic Action Plan is a plan that is working and we will persist with it.

In other words, Budget 2010 will be year two of our two-year Economic Action Plan. We will not undertake major new spending initiatives. We will stay the course with the Economic Action Plan already announced to protect and create jobs.

Just yesterday in their most recent economic outlook, the OECD advised that Canada's focus should be on rolling out already committed spending as quickly as possible. As the report cautioned, "Additional expansionary measures should be resisted." And I can assure you we will resist them. "Instead, governments should be preparing detailed, credible, medium-term fiscal

consolidation plans to be announced soon and implemented when the recovery is firmly underway.”

We agree with that view. Our focus will not be on new initiatives or added stimulus. Our focus will be on following through in getting the measures already announced out the door and into the economy.

We will stay the course. We will fulfill our promise to Canadians for a strong and sustained recovery by fully implementing one of the most ambitious economic stimulus packages in the world. While doing so, we will resist any pressures to take extraordinary actions or to assume indefinite obligations.

Ronald Reagan, with some insight, once remarked that “the nearest thing to eternal life we will ever see on this Earth is a government program.” There’s much truth in that observation. I have no intention of being the kind of government minister President Reagan was talking about.

Our Economic Action Plan was a dramatic response to a specific dramatic situation. It is not created for eternal life.

The Action Plan contains a built-in exit strategy based on necessary but temporary measures. And temporary, as you know, means lasting only for a limited period of time. In the case of the Economic Action Plan that means two years. The temporary stimulus measures will end as planned, in line with the expected improvements in the economy, by the end of the next fiscal year, 2010–2011.

But just as overcoming an immediate global crisis is not easy, neither will be determining precisely when it’s over. That brings us to our next challenge: preparing for a post-crisis global economy.

While it’s widely expected the global economy will recover from its recent downturn, what that recovery will look like is a matter of some debate. The IMF is expecting the recovery to be weak because a large amount of economic activity pre-recession was simply not sustainable and will not be coming back. That uncertainty makes our fiscal planning beyond 2011 a challenging task, since recovery in Canada will depend to a considerable extent on what will happen to the global economy.

That brings a whole new set of circumstances to our strategy to return once again to balanced budgets when an economic recovery remains so uncertain. Act in haste and the risk would be precipitating another economic slowdown. Wait too long and the result could be chronic deficits. Canadians worked very hard to abolish, the kind of structural deficits that other nations are dealing with right now.

Add to that a number of challenges like ensuring our businesses continue to be more innovative and competitive globally. We will not be able to address these medium-term challenges and take advantage of opportunities if we don’t have our fiscal house in order.

So, fortunately, as I said earlier, Canada will be able to respond to our longer-term challenges from a solid, strong starting point. Compared to most countries in the world, we are in an enviable position.

As a result, although we had to run temporary deficits in response to the global recession, Canada's fiscal position remains the best in the G7. This fiscal advantage will serve just as well years from now as it did when the global recession hit our country.

As I stressed earlier, our priority in the weeks and months ahead is to implement the Economic Action Plan. Responsible government demands that we do nothing less.

Once we are certain that recovery has fully taken hold, we will move forward on our plan to return to balanced budgets in the medium term. Our commitment will be based on the same principles that we relied on to turn back the recession: leadership, discipline, tough choices.

Along the way, our Government will not do certain things. We will not raise taxes. We will not put in jeopardy the growth track of major transfers to persons—our seniors, our children, those receiving EI benefits. And we will not reduce the transfers to other levels of government.

Meeting this challenge won't be an easy task, but once the uncertain becomes the undeniable it will become the next challenge the Government will confront head-on. This Government is ready to make the right tough choices for Canada and for our children and grandchildren in the years ahead.

Budget 2010 will focus on completing the implementation of the Economic Action Plan to secure Canada's recovery. Once the recovery is secure, we will steadily implement our exit strategy.

First of all, we will end the temporary extraordinary stimulus measures, as planned, in Budget 2009 in January of this year. Those measures comprise a large part of this year's projected deficit.

About half of this year's deficit comes from one-time stimulus and support to the automotive industry, as well as temporary measures we took to increase benefits for unemployed workers and freeze EI premiums for individuals and for businesses. As that temporary spending ends, we will move closer to balanced budgets.

At the same time, we will be experiencing a recovery, however modest, with economic growth and increased government revenues. By 2014–2015 we are forecasting a small but manageable deficit of about \$5.2 billion.

When the time is right, when the economic recovery is clear and entrenched and if it's necessary, we will determine the amount of spending growth restraint that will be required to balance the budget. If we have to restrain growth in spending, when the time comes, we will find that

restraint in the remaining \$100 billion of federal program spending that is projected to grow at 3.3 per cent a year.

So just to talk about budgeting for a moment, we have the transfers to the provinces. We have the transfers to individuals in Canada—to people who are unemployed, for the benefit of children, the benefit of seniors, and so on. And then the third large category is program spending in the Government of Canada. As I say, that's been growing at about 3.3 per cent a year and we can restrain that rate of growth if it's necessary to do that, depending on how much economic growth we have in the Canadian economy in the medium term.

And in following through on the Economic Action Plan and planning our return to balanced budgets, our Government's commitment to responsible financial management is firm. It will mean honouring our commitment to Canadians and to our global partners to ensure unprecedented fiscal measures do what they're supposed to do—lay the foundation for an entrenched recovery and truly sustainable prosperity.

It will mean next year rejecting demands—and I know there will be many—to make extraordinary temporary stimulus measures permanent government programs. We will not do that.

And it will mean a well-planned return to balanced budgets that will keep a sudden economic downturn from becoming an unending financial burden.

Getting there won't be easy. None of this in the past year has been easy.

But we have demonstrated the discipline and leadership that was required during the crisis to put us on the road to recovery. We will continue to demonstrate that discipline and we will continue to make the tough decisions to make sure we complete the journey.

I'm proud of everything that has been achieved this year, even if I'm still glad to see 2009 come to a close.

Make no mistake, we have important work ahead. And in so doing we will continue to make a difference in the lives of Canadians now, in 2010 and for the next generation.

Thank you for having me here today.