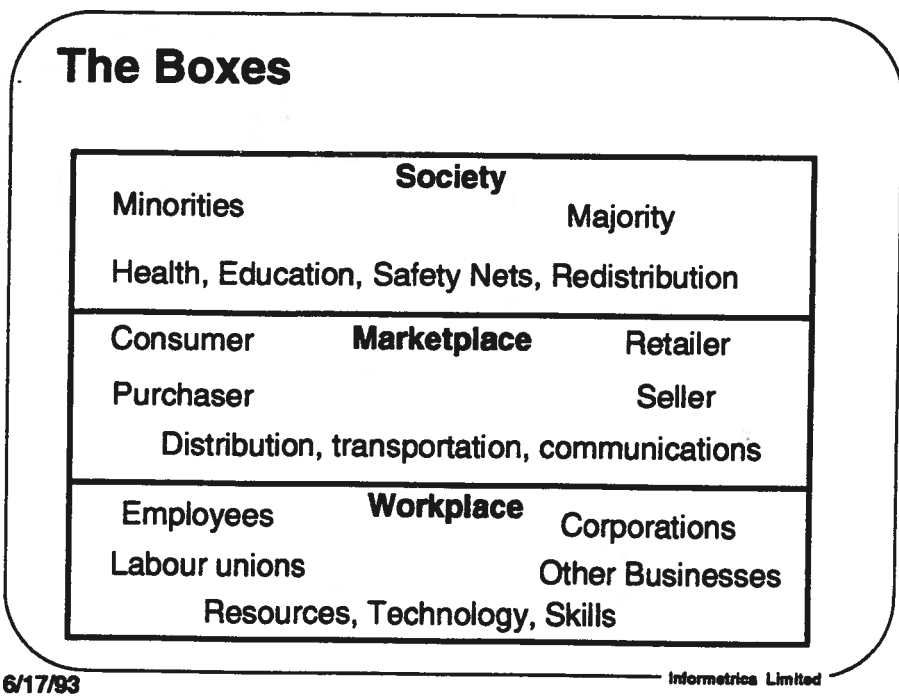


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- Any state can be thought of as a set of stacked boxes.
- Workplace - Firms combine labour, capital, technologies, resources and management to produce goods and services.
- Marketplace - Goods and services are bought and sold, prices signal relative demand and supply. Inputs used by the workplace may be traded here.
- Society - The people: quality of life, family, culture, education, participation.

It is this top box that is the purview of social policy.

It deals with people over their life-cycle - children, youth, those in and out of the workplace, the aged. It also includes immigration policy, aboriginal policies, etc.

Macroeconomic Performance

Healthy Economy

Low Urate
Welfare to employment
All regions improve
Incentives for education
Business trains
Optional retirement
Fiscal capacity

Weak Economy

High Urate
Unemployment to welfare
Double-digit Urate
Education for what?
Why train?
Forced retirement
Fiscal pressures

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Canada's social systems were originally designed from an economy operating close to full employment. We are discovering that they are difficult to maintain in a slack economy.

If you want to tear them down, what better excuse than fiscal constraints?

Changes in formulas, redrawing poverty lines, partial deindexing, etc. will not solve the problem!

Only a major improvement in macroeconomic performance will make a difference.

Current Trends

OAS/GIS next on list to convert to tax credit.

Further cuts in EPF and CAP.

Experience-rated UI - employer pressure to cut benefits.

Government to load up UI with programs to fund through contributions.

Limited indexing.

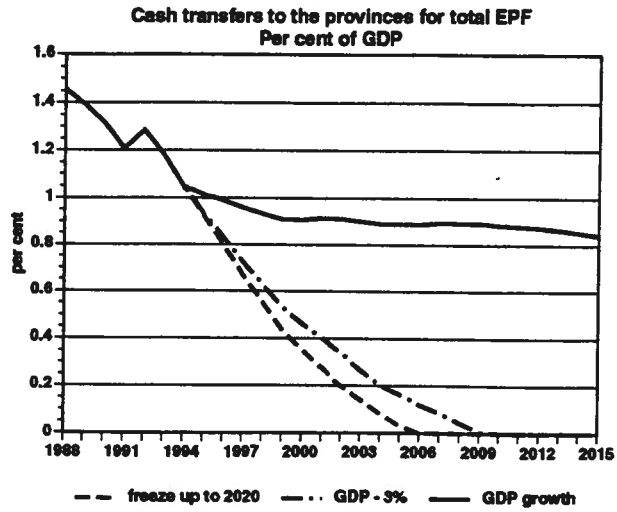
More user charges.

Immigration backlash.

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EPF Cash Transfers



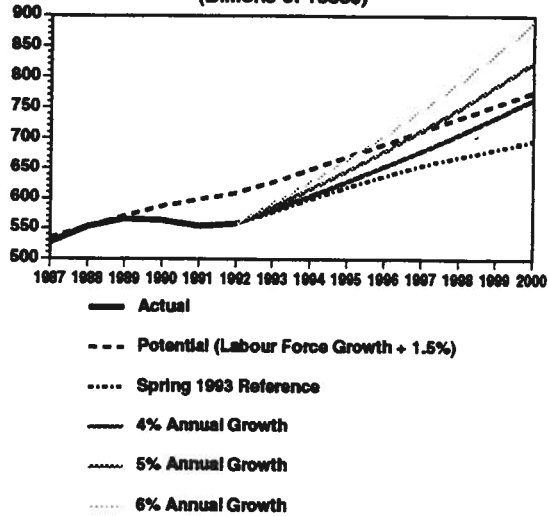
Source: Informetrica Limited

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Challenges Facing the Canadian Economy

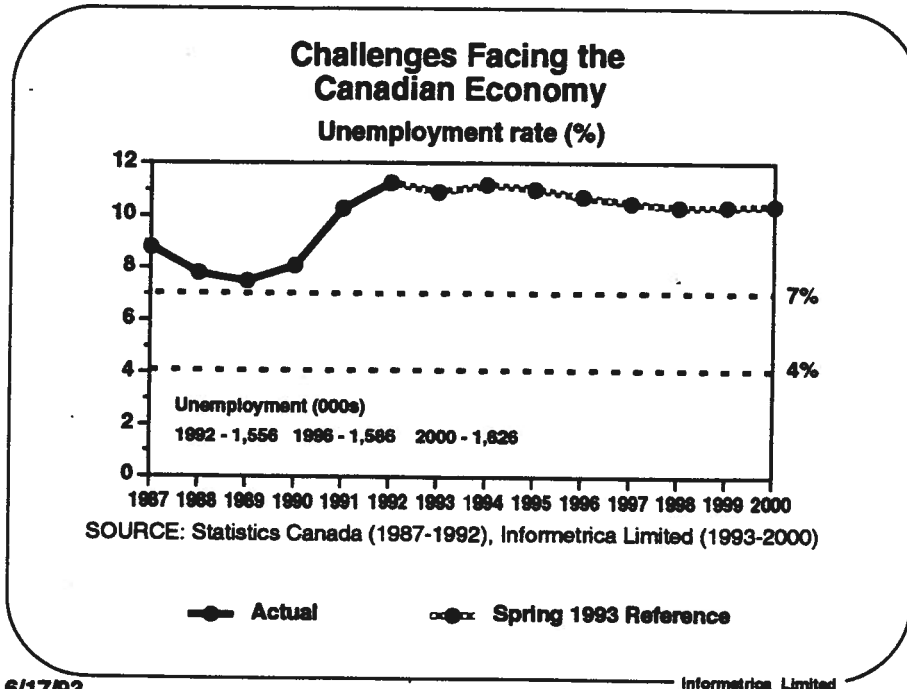
Potential and Actual Gross Domestic Product
(Billions of 1986\$)



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- Vigorous growth of 4% or greater is required to close the "output gap" that has opened up since 1988 (10% in 1992) by the turn of the century. (5% -1997, 6% - 1996)
- In our most recent forecast the challenge is not met, as the gap is more than 10% in 2000. This "unusual" behavior reflects a continuation of current monetary and fiscal policy, with a focus on zero inflation and reduction of government spending and deficits.



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- The same concept of a "gap" can be translated into unemployment rate terms. The result is an unemployment rate in excess of 10% through 2000, and the number of unemployed in excess of 1,500,000.

Policy Package

- **Change in Monetary Policy**
- **Change in Fiscal Policy**
- **Change in Incomes Policy**
- **Change in Structural Policies**

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The challenge for a new government will be to "close the gap" as quickly as possible.

This will require actions on several fronts.

Monetary Policy

- **Real interest rates less than 3%.**
- **Floating Exchange Rate**
- **Encourage Domestic Lending**
- **Reduce Credit Gaps**

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Real interest rates less than 3% - this is the condition necessary for debt stability.

A floating exchange rate is necessary for interest rate rule.

The banking system is created by the state, with monopoly powers to create money. It should be regulated for "success". Foreign investments by the banking community are not a critical part of that role.

Credit gaps exist for some small businesses, some high-tech firms, and in some regions.

Fiscal Policy

Objective: Stimulus of Demand

- **Accelerate Infrastructure Spending**
- **Social Employment Programs**
- **Stimulus to consumers through tax cuts or transfer increases**
- **Keep UI premiums flat**

- **When full employment approached, raise taxes.**
 - **CPP/QPP contributions up.**
 - **Personal income taxes up.**

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Infrastructure spending is primarily a PLH responsibility. Feds can help with financing and coordination.

Social employment programs could include literacy training, environmental cleanup, and even tree planting. Key is quick start and emphasis on employment incomes.

When will we reach full employment? What is it?

Topic for another day.... it is a lot lower than we have experienced in period since 1975!

Incomes Policy

- **Consensus on national wage and price guidelines.**
- **Encourage voluntary sectoral guidelines.**
- **Enforcement of overshooting is a federal and provincial responsibility.**
- **Net CPI for Indexing (omit effects of indirect taxes, exchange rate, and commodity price shocks).**

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We now have an incomes policy.

- Bank of Canada price targets.
- Enforcement through high unemployment, through interest rate hikes and credit rationing. (Beat with a stick.)
- Massive income transfer from debtors to creditors.

Is this the "best" incomes policy that can be devised?

NO!

Structural Policies

- **Raise investment effort.**
- **Improve Productivity.**
 - Education and training
 - R&D
- **Trade Promotion.**
- **Promote Innovation.**

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Investment share of output is key determinant of productivity growth.

Improvements in human capital and adoption of technology are also important.

Increasing exports and developing goods and services that can compete with imports are important to prevent a balance of payments constraint, to earn an appreciation, and as a source of increased demand.

Promotion of venture capital, initial public offerings (IPOs), and other ways of encouraging risk-taking investments are aimed at improving innovation in Canada by removing credit gaps.

Institutional Realities

- **Federal-Provincial**

- Cooperation/Coordination
- Infrastructure planning and finance
- Rationalization of Indirect taxes
- Reduced borrowing costs

- **National Institutions**

- Incomes policy (ECC-like institution?)
- Training and education
- Science and technology
- Health (drug prices, health promotion, etc.)

Finance and the Bank of Canada at the table!

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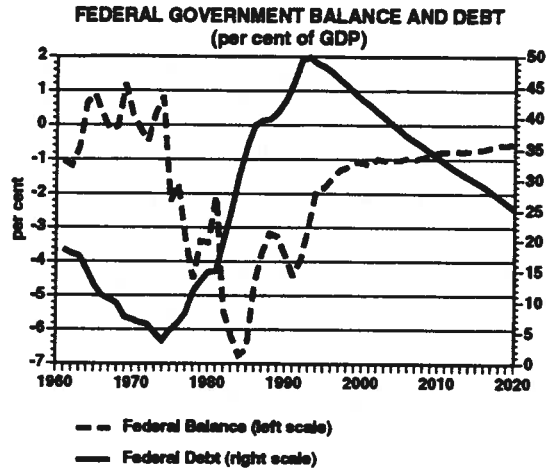
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Integration (or rationalization) of indirect tax field, including the GST.

Feds offload costs onto provinces, who in turn have to borrow at higher cost. If their credit ratings decline, then the cost of all new debt (and rollovers) are higher. Seems to violate the "Same Taxpayer" rule!

Wage and price guidelines for government operations and as a participant in establishing them in the private sector.

Debt and Deficit



Source: Statistics Canada and Informetrica Ltd.

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