MORTGAGEBROKERS OTTAWA

Flaherty urged to keep spending taps open

Jeremy Torobin and Tavia Grant

Ottawa, Toronto — Globe and Mail Update Published on Monday, Feb. 01, 2010 8:15PM EST Last updated on Tuesday, Feb. 02, 2010 6:40AM EST

Canada's leading private economists are urging Finance Minister Jim Flaherty to tread a cautious path in his March budget and keep spending flowing in a fragile recovery.

At a meeting in Ottawa on Tuesday, the economists will suggest Mr. Flaherty look past some of the better-than-expected data in Canada and the United States and resist moving too quickly to rein in the deficit.

The economists have boosted their projections for the economy, which Mr. Flaherty uses to shape his own assessments. They now see average economic growth of 2.7 per cent this year, according to a Bloomberg survey. That's higher than the 2.3 per cent Mr. Flaherty projected in his September fiscal update, but still well below the 5 per cent to 6 per cent that typically follows a deep slump.

"The dominant theme here is that unlike recoveries from previous recessions this one's going to be fairly slow and drawn out," said Craig Alexander, deputy chief economist at Toronto-Dominion Bank. "I don't think the government should be tightening fiscal policy before the recovery has gained greater traction."

In the U.S., President Barack Obama is facing intense political pressure to start taming a deficit on track to reach a record $1.6-trillion (U.S.), even as a stubbornly high unemployment rate forced him to ask Congress on Monday for another $100-billion to create jobs.

Canada, by comparison, is in a better position to carefully talk about a plan for tackling the budget shortfall that the global downturn spawned. Mr. Flaherty and newly minted Treasury Board President Stockwell Day have said the budget will include a road map to bring the budget back into balance within five years.

Most Canadian economists say outlining such a strategy is a good idea, but caution against being too aggressive.

"Unless economic growth turns out to be significantly stronger than economists like myself are projecting, the recovery won't do enough to get back into a balanced budget," TD's Mr. Alexander said. "The budget is an opportunity to lay out a framework for what you try to do over a five-year horizon, and in that context there's a perfectly good opportunity to outline how you intend to, after the economy's gained significant momentum, get back into a balanced budget."

At the same time, some economists are so cautious in their outlook that they say it's premature to even talk about spending restraint. Avery Shenfeld, chief economist at Canadian Imperial Bank of Commerce, said that even if the Parliamentary Budget Officer's recent warnings come true and Canada faces a so-called structural deficit of up to $19-billion (Canadian) five years from now, the country's debt load wouldn't be rising at a pace that increases the ratio of debt to gross domestic product.

"We're not Greece, so we don't have to impose an austerity program while the economy's still weak, or even talk about it," Mr. Shenfeld said. "There's lots of time to adjust fiscal policy if it turns out three or four years from now we're still running a modest deficit."

The deficit spending, and when and how to refill the hole, will be the front-and-centre topic at today's meeting, said Michael Gregory, senior economist at BMO Nesbitt Burns, not least because of nagging concerns about the effect that an aging population and health-care costs will have on long-term growth, regardless of the economic slump.

Reports late last week on both sides of the border showed Canada's economy grew at a faster-than-anticipated 0.4-per-cent pace in November and that the U.S. economy expanded at an impressive 5.7-per-cent annual pace in the final three months of 2009. Still, although both numbers caused some forecasters to increase their estimates of Canada's growth in the fourth quarter, many economists are skeptical the U.S. can keep growing at anywhere near its October-through-December pace, most of which was attributed to companies replenishing depleted inventories.

In any case, growth in both Canada and the U.S. this year will be on the strength of billions in government stimulus measures, not to mention rock-bottom interest rates, so fiscal policy makers face the crucial task of timing their belt-tightening just right because it remains unclear when the private sector will see self-sustaining demand.

Deficit reduction is important, but governments will have to walk a tightrope in the next year, said Jay Myers president and chief executive officer of Canadian Manufacturers & Exporters, which is hosting Mr. Flaherty at a conference later Tuesday in Ottawa.

"The year of recovery is going to be much more challenging for federal and provincial governments than the year of recession," Mr. Myers said. "They basically knew what they had to do in recession. It's much more challenging now, to make the right choices."

The balance hinges on beginning to unwind the extraordinary spending while also encouraging investments in new technology, innovation, skills development and market diversification that help growth over the long haul, he said.

Other topics that might be raised Tuesday range from new housing regulations to learning to live with the strong dollar, said Sheryl King, head of economics at Merrill Lynch (Canada).

The Finance Minister warned last month he will step in if the white-hot home resale market continues to push prices higher by tightening the rules for borrowers, such as increasing minimum down payments and shortening the maximum length of mortgages.