The Canadian Experience in Reducing Budget Deficits and Debt

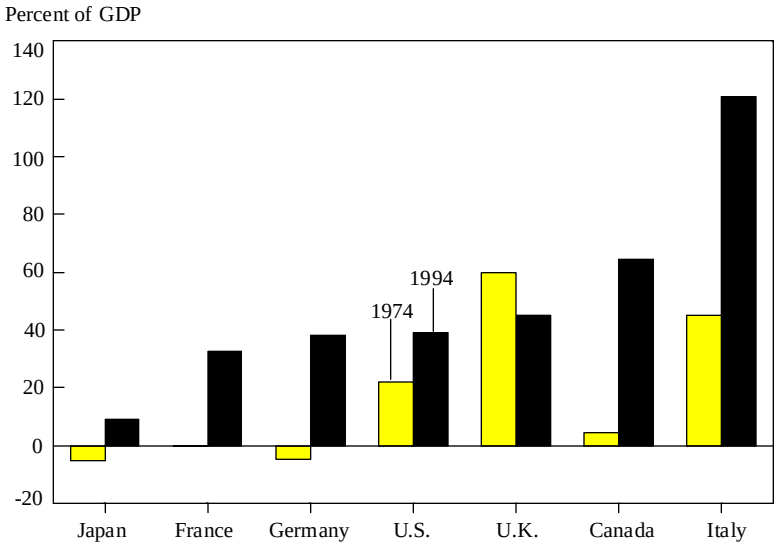
Paul Martin

My objective in these remarks is to describe what we in Canada are doing to improve the fiscal health of the federal government. I will focus particularly on the political dimensions of the process, since obviously there is little I can teach this audience about the economic dimensions. That said, we should begin with some background as to the origins and magnitude of Canada's fiscal problem.

Our general pattern of deficits and debt has much in common with that of many other Organization for Economic Cooperation and Development (OECD) countries, including the United States—that is, a very high ratio of debt to GDP coming out of the Second World War, followed by a rapid decline of the debt ratio as the military was demobilized, as economic growth took off, and as the effective interest rate on government debt remained low.

In Canada's case, the ratio of total government debt—federal and provincial combined—fell from slightly more than 100 percent of GDP in 1945, to bottom out at about 20 percent in 1974. Since then, the debt ratio has risen in virtually every year and is now once again back to approximately 100 percent of GDP.[1] But unfortunately, the contemporary circumstances do not compare with the situation fifty years ago. Today, there is no potential for massive spending cuts from military demobilization, and interest rates exceed the rate of economic growth—precisely the reverse of the postwar conditions.

Chart 1
Total Government Net Fiscal Debt - G-7 Countries
(National Accounts Basis)



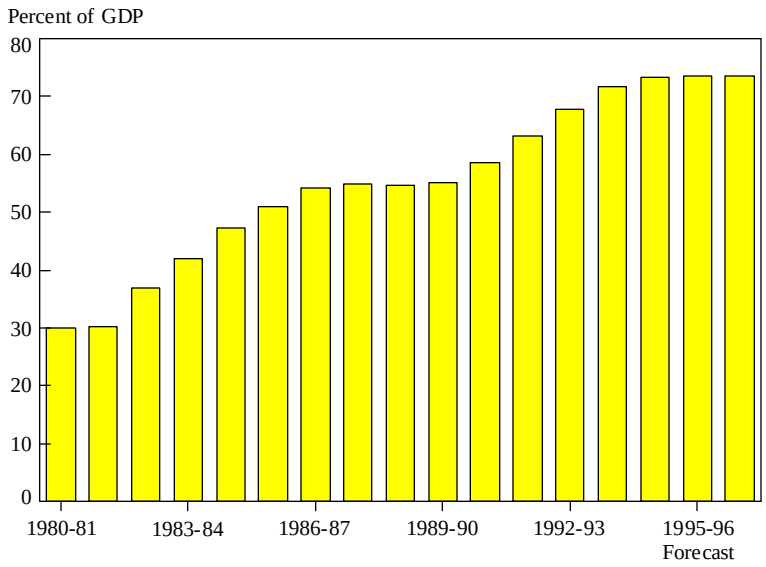
Source: *Statistics Canada* for Canada. *OECD* estimates for other countries.

The growth of debt since the mid-1970s has coincided not only with the maturation of the modern welfare state, but also with the great productivity slowdown in all of the advanced economies. In this regard, Canada's situation has much in common with most G-7 countries.

In what follows I will restrict attention to the situation of the federal government.[2] There, as we headed into the 1981-82 recession, debt was a manageable 30 percent of GDP. Five years later, the ratio had climbed over 50 percent and warning lights had begun to flash. With the last recession, it jumped again, from about 55 percent of GDP in 1989-90 to approximately 73 percent today.

This extremely large stock of debt, when combined with interest rates that exceed Canada's rate of economic growth by 3 to 4 percentage points, means that simply to stabilize the federal government's debt

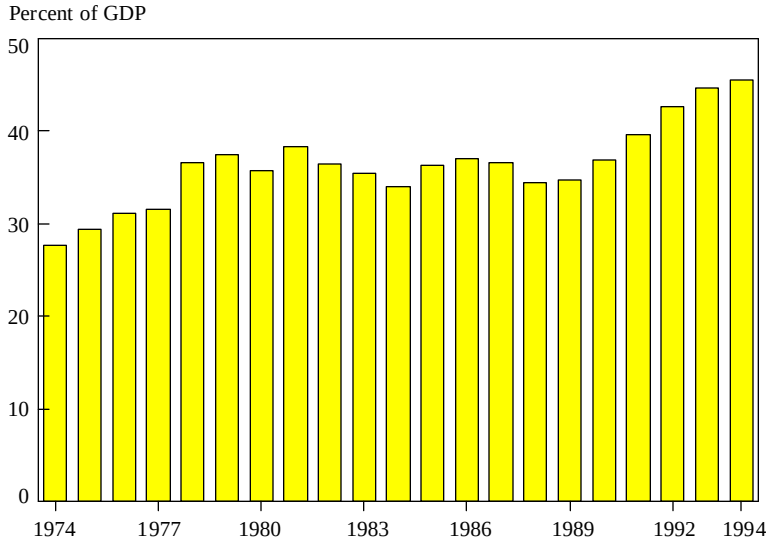
Chart 2
Federal Net Debt
(Public Accounts Basis)



ratio, our revenue intake must now exceed program spending by about 3.5 percent of GDP or close to C$30 billion.

Coming into office in the fall of 1993, we fully expected to find a nasty fiscal situation—the combination of misplaced priorities, which is the stuff of politics, and compound interest, the stuff of the inexorable laws of arithmetic. Indeed, the federal deficit in 1992-93 reached almost 6 percent of GDP. But the much more fundamental problem was the apparent intractability of the sheer arithmetic of debt when the interest rate is higher than the economic growth rate. It became clear that a very long period of restraint would have to be endured to turn the debt momentum around. As part of that, we also needed to fundamentally re-think the role of the national government and the structure of its spending. But there was no ducking the issue.

Chart 3
Canada's Net Foreign Debt



The economic warning flags were everywhere. Despite Canada's having one of the world's best inflation records since 1989, the currency was under constant pressure and real interest rates were increasing, putting a drag on growth and obviously exacerbating the fiscal problem.[3]

Meanwhile, the country was not generating sufficient domestic savings to finance both the investment needs of the private sector as well as huge and chronic public sector deficits. Canada was therefore borrowing increasingly abroad. The result has been an accumulated net foreign debt—owed by the public and private sectors combined—that now exceeds 45 percent of GDP.

Despite these warning signs, the debt and deficit were slow to become top-of-mind issues with the Canadian public. Then, rather suddenly, all that changed. People came to understand that the

problem had reached a genuinely critical juncture; that endless deficits really did have something to do with Canada's high real interest rates; and that higher government spending really did translate into higher taxes, the tolerance for which had reached its limit.

All of this amounted to a crucial turning point in national psychology. Without some such shift in the public mindset, it would seem to me that democratic societies cannot come fully to grips with what needs to be done to solve a debt problem.

In Canada's case, the philosophical chasm that had always divided the deficit hawks and doves began to close. The fact was that no one could deny the stark arithmetic of compound interest. For example, interest charges, which had consumed only 11 cents of every federal revenue dollar in the mid-1970s, now consume almost 34 cents or about 6 percent of GDP.

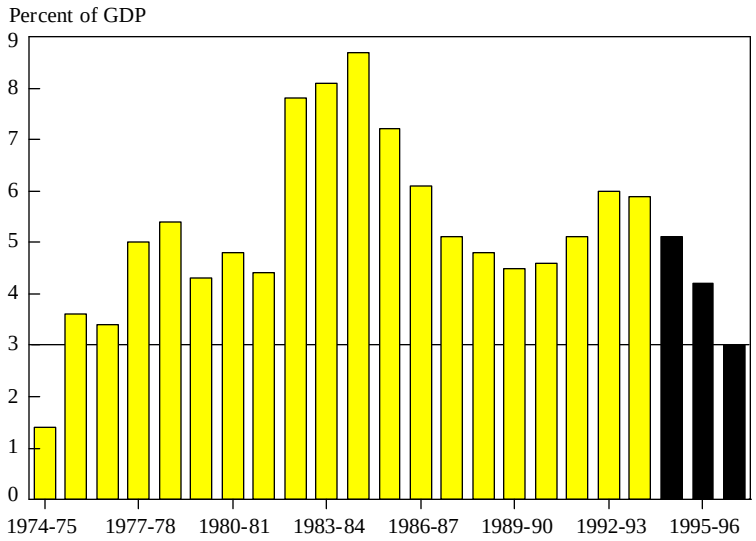
And while some economists may argue about the extent to which deficits crowd out private investment, those of us who believe in a socially progressive and pro-active role for government understand clearly how debt charges crowd out spending on valued public programs such as health care and old age security. Indeed, from the perspective of the political philosophy of the Liberal Party of Canada, the debt burden has become an even more serious threat to the social conscience of government than to our bond ratings.

The governments of most of Canada's provinces—regardless of their political ideology—have come to essentially the same conclusion. Within the last couple of years, most have moved to put their fiscal houses in order. Undoubtedly, this helped to create a widespread public expectation that the federal government would do likewise—that it would finally stop talking about the deficit problem and really buckle down to do something about it.

Let me turn next to what we have done.

We entered the 1993 election campaign with a commitment to ultimately balance the budget and a very specific interim target to

Chart 4
Federal Government Deficit



reduce the deficit to 3 percent of GDP by 1996-97.[4] While some have considered this to be an insufficiently ambitious target, the reality is that Canada's federal deficit has exceeded 4.5 percent of GDP virtually every year since 1976 and the resulting accumulation of debt made hitting the 3 percent target in 1996-97—down from about 6 percent in 1993-94—a really significant challenge.

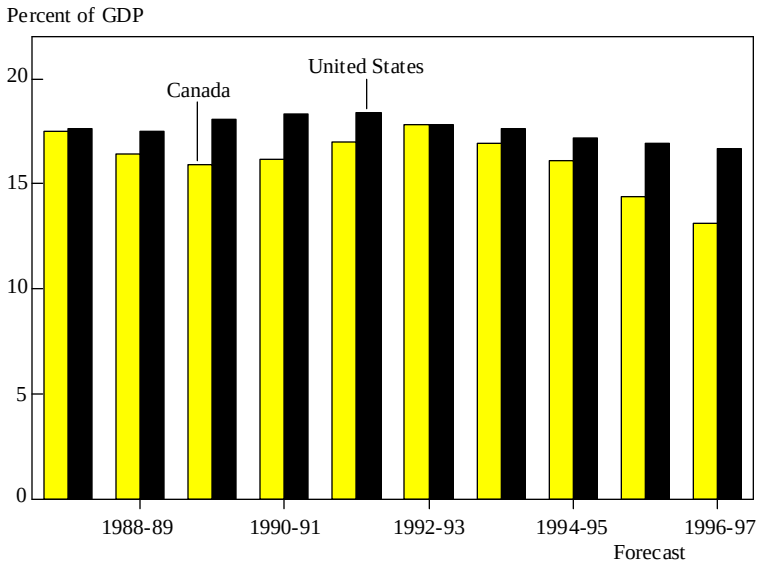
I would emphasize that 3 percent is an interim target on the way to a balanced budget. A zero deficit is not only of fiscal significance—it is of great symbolic significance, a benchmark of fiscal responsibility that has been adopted as well by provincial governments and embraced by the Canadian public. Deficit elimination is thus a goal that will continue to discipline our budget choices. But it can be argued that an even more fundamental objective in strictly economic terms is to put the debt-to-GDP ratio on a steady downtrend. This is the key to fiscal stability and assured sustainability

and thus to a stronger economy. A much lower debt ratio must be a legacy of this government.

We have already made a great deal of fiscal progress—more, in fact, than is generally recognized. We began to turn the corner with our first budget in February, 1994, which secured significant savings, especially in the Department of Defense and in the Unemployment Insurance program. That was followed a year later by what many regard as the most significant federal budget of the postwar era. As a result:

> Fiscal actions—that is, spending cuts and some very limited revenue measures—will total C$29 billion over the three years through fiscal 1997-98. To put that figure in a U.S. context, it would be equivalent to roughly US$210 billion of action over the same period.
>
> The fiscal savings will come overwhelmingly from spending cuts—they will outweigh tax increases by a ratio of 7 to 1. While we took some action to tighten up the corporate tax system and generally to improve tax fairness, we held the line—as we also had in the 1994 budget—on sales taxes and on personal income tax rates.
>
> Program spending by 1996-97 will be 10 percent lower than in 1993-94. In fact, Canada is the only member of the G-7 to budget an absolute decline in program spending. For a comparative perspective, consider that federal program spending in both Canada and the United States was an identical 17.5 percent of GDP in 1992-93. Looking to 1996-97, the U.S. budget forecasts a reduction to 16.3 percent of GDP while Canada's ratio will have fallen to just over 13 percent, the lowest level since the early 1950s.
>
> By 1996-97, the 3 percent deficit target will be met and our market borrowing requirement—equivalent to the Unified Budget Basis deficit in the United States—will be down to 1.7 percent of GDP, projected to be the lowest among central governments of G-7 countries.

Chart 5
Federal Government Program Expenditure



Notes: 1. Total expenditure minus gross debt service charges for Canada and the U.S.
2. Fiscal years ending March 31 and September 30 of the same year for Canada and the U.S., respectively.

Sources: Canada: Department of Finance Canada: United States: Department of Commerce and Budget of the United States Government, Fiscal Year 1996.

> The operating surplus is forecast to be 3.6 percent of GDP (C$30 billion) by 1996-97. Most significantly, this will be sufficient to finally begin cutting the debt ratio. Increasing operating surpluses in the future will ensure an accelerating reduction of that ratio.

These facts and figures tell only part of the story—in fact, the lesser part in our view. More fundamentally, we have sought to change permanently the structure of federal government spending. Since our fiscal problem is structural, our remedies must be structural as well.

Our overarching objective is to promote jobs and growth, a particularly resonant theme in Canada given the nation's unusually weak recovery from the 1990-91 recession. For us, deficit cutting is not an end in itself, but rather an urgent and necessary means to achieve our fundamental jobs and growth objective.

We have developed a comprehensive game plan to address the underlying issues, focusing primarily on promoting productivity growth while working to correct aspects of the labor market that have caused Canada's core unemployment rate to roughly double over the past 20 years.[5] That game plan guides our budget choices which, beyond their purely fiscal purpose, are designed to help achieve the structural changes that lie at the heart of our jobs and growth strategy.

For example, it was clear to us that many long-standing business subsidies were, in fact, hurting our productivity and competitiveness. So in last February's budget we cut total subsidies to business by 60 percent over the next three years. This included ending a more than one-half-billion-dollar-a-year subsidy for grain transportation in the west that had been in place since the last century.

We realized that many features of Canada's unemployment insurance system were impeding rather than promoting the efficient function of our labor market. So we are taking significant steps to transform unemployment insurance—with emphasis on getting the incentives right and on active measures to help the long-term jobless.

We also took a hard look at federal transfer payments to the provinces, which this year will account for almost 23 percent of program spending. Clearly, the fiscal problem could never be tamed without some reduction of these transfers. We were nevertheless determined not to cut back our support to the provinces by any greater percentage than we were hitting programs in our own back yard. Furthermore, it would not have made sense simply to off-load the problem onto another level of government.

So to give the provinces greater flexibility, we will convert the present cost sharing of social assistance payments into part of a larger block grant. This will also increase the incentive to develop more innovative and cost-efficient ways of delivering social assistance. That said, the new block-funded transfer will still require provinces to respect certain nationwide principles, particularly in respect to health care delivery but also in the social assistance domain.

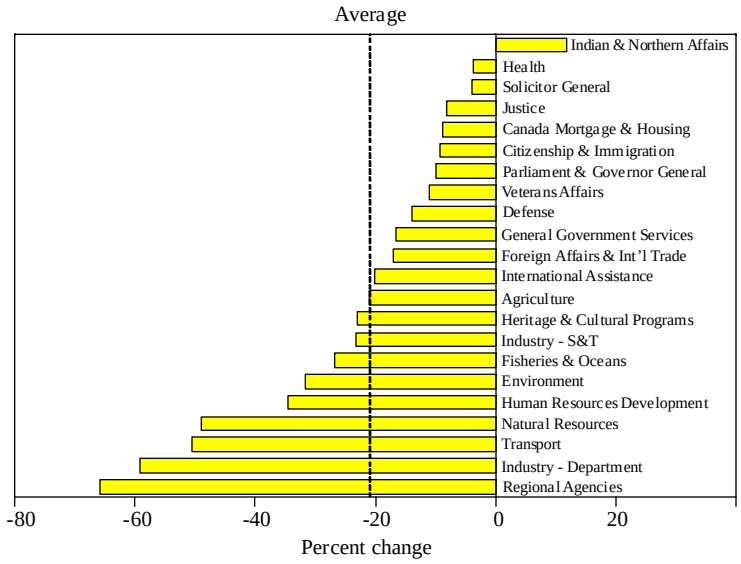
There can be no questioning the commitment of the government of Canada, and of Canadians themselves, to our publicly-funded national Medicare program. We view this as a joint responsibility of the federal and provincial governments. As such, one of the imperatives of getting our fiscal house in order is to be able to have continuing, stable federal funding for health care.

The 1995 budget also announced significant reductions in spending by federal departments and agencies. As a result, departmental outlays by 1997-98 will be close to 20 percent lower (in absolute dollar terms) than last fiscal year; the public service will be reduced by about 15 percent or roughly 45,000 positions; and several activities, notably in the transport sector, will be privatized or commercialized.

Some departments—for example, our Departments of Industry and of Transport—will cut their spending in half. In fact, only one department of the federal government—Indian and Northern Affairs—will be spending more in three years' time than it is today. And that one exceptional case reflects the extraordinary circumstances of Canada's native people. Every other branch of government will be required to get by with less.

We believe, nevertheless, that because of the nature of our spending decisions—which reflect a commitment to get government right and to promote the structural changes that lead to higher productivity and more jobs—we can restore fiscal health while greatly improving the micro-foundations of Canada's economy. Let me emphasize that the measures I have been describing are not merely a budget wish

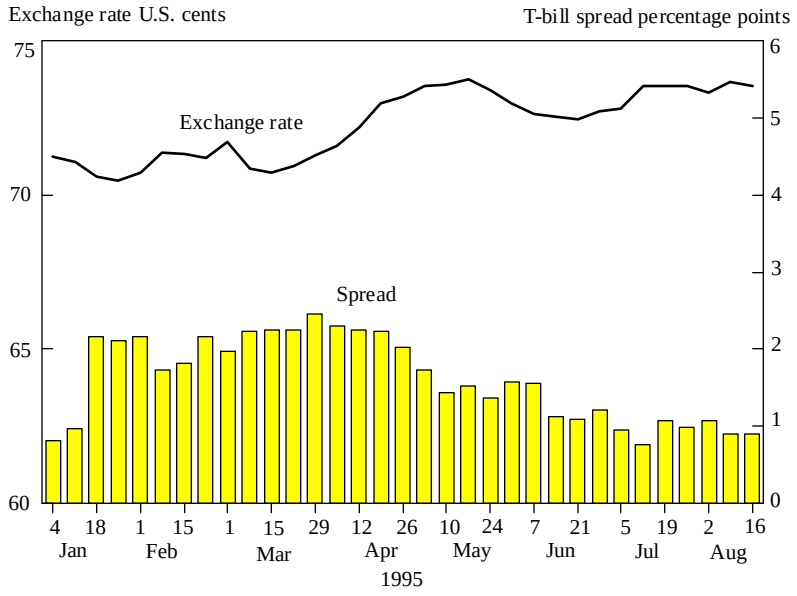
Chart 6
Changes in Federal Department Spending
1997-98 Relative to 1994-95



list. In this case, one of the advantages of Canada's parliamentary system—where the executive and legislative branches are one in the same—is that the budget that is announced is also the budget that is enacted (provided the government holds a majority of seats in the House of Commons). In fact, our February budget was completely passed into law by June of this year.

The public reaction to the 1995 budget has been favorable on the whole, especially given that few recipients of federal spending were left untouched. In particular, the reaction of affected interest groups was muted, perhaps reflecting the fact that the measures were carefully balanced and apparently considered to be equitable by the great majority of Canadians. As for the financial markets, their verdict was generally positive. Indeed, the 1995 budget probably met or exceeded most expectations of what we would actually deliver.

Chart 7
Canada-U.S. Comparison



Given the history of federal governments, some in the financial community remain skeptical that the government will stay the course for as long as it takes. I can assure you, their skepticism is misplaced. In fact, we believe that, overall, markets have been reassured by the scope and nature of our actions. And while one must be wary of attributing too much cause and effect, it may be indicative that the Canada-U.S. Treasury bill spread has narrowed from the vicinity of 200 basis points last February to about 100 basis points now (mid-August 1995) while the exchange rate has remained quite stable.

Let me turn now to *how* we managed to do all this—our strategy, the politics, and some of the lessons that might be more broadly applicable.

Our theme in the 1993 election was “Jobs and Growth,” and reflecting our conviction that sound finances and a sound economy go hand in hand, a key element of that platform was the 3 percent

interim deficit target for 1996-97.[6] This proved to be an essential *political anchor* for our budget strategy. Without some fixed and quantified target, any finance minister risks ending up on a slippery slope. But with the unequivocal support of the prime minister, and that target as a foothold, we were able to combine an economic forecast with our fiscal model so as to quantify, in relatively unassailable terms, the total amount of fiscal action required.

That made the politics manageable. Without a target to which we were all irrevocably committed, the natural reluctance of ministers—myself included—to accept cuts in their own domains would likely have caused things to unravel. But once the fiscal target was set, tradeoffs became inevitable and the only question was precisely what those tradeoffs would be.

The budget strategy

Our broad budget strategy rested on three principal elements—that is, setting our targets and assumptions; allocating the spending cuts; and consulting with the public.

Short-term targets; prudent assumptions

We began by confirming the 3 percent deficit target for 1996-97, sticking with our campaign commitment despite a fiscal mess that turned out to be even worse than we had anticipated. For us, the importance of maintaining that political anchor was uppermost. We were also not content simply to state the 3 percent target for 1996-97. So we committed to interim annual targets that would lead us there. In fact, we have bettered the target for last fiscal year.

Foremost in our thinking was the need to restore the severely damaged credibility of the government, which for years had been over-promising and under-achieving its fiscal targets. Without credibility, any positive market effects of a budget will be delayed as skeptics adopt a wait-and-see attitude. So when planning the 1995 budget, we used forecasts of growth and interest rates that were considerably more cautious than the private sector average.

We also include in our deficit projections a "contingency reserve" equal to about 1 percent of combined revenue and spending to buffer nasty surprises arising in the economy. And significantly, if the reserve is not required to hit our target, it will not be spent. It will contribute instead to an even lower deficit.

We have also decided to adopt a two-year budget horizon—rolling the second year's target forward one year at a time. This is central to our overall strategy. We have rejected the traditional approach where typically a balanced budget would be projected five or more years down the line. Frankly, that is political never-never land for the simple reason that elections intervene before the magic date arrives. Political accountability is lost and the bureaucracy can safely put off the day when they really have to buckle down and find the savings. The result, as we saw in Canada during at least the last ten years, is a progression of missed targets, looming fiscal crisis, and growing public cynicism.

With our two-year rolling targets—and our promise to hit them "come hell or high water," the situation is very different. Since the targets are always staring us straight in the face, our feet are held to the political fire. This keeps the goal uppermost in the cabinet's mind and puts maximum pressure on the program managers in the public service to deliver promised savings.

The result is that we have been able to meet all of our targets to date—something of a novelty for federal fiscal managers in recent times—and we are totally committed to meeting them in the future.

We nevertheless still face pressure to abandon the strategy of two-year rolling deficit targets and announce a firm date when the budget will be balanced. We will resist that pressure and stick to our game plan. Next February's budget will include a deficit target for 1997-98 (that is, one year beyond the announced 3 percent target for 1996-97) together with the measures needed to achieve it. The balanced budget target will be announced once we are confidently within two years of its achievement.

A frequently advocated alternative to the approach we have adopted is to use "balanced budget" legislation—or even a constitutional provision—to guarantee the fiscal responsibility of legislatures. In our view, that is not the way to go. Apart from limiting the choices of duly elected governments, this legalistic approach simply encourages ingenious politicians and bureaucrats to spend time looking for ways to get around the rules through accounting hocus-pocus and subterfuges of various kinds. It seems to us that a simple ironclad commitment to credible short-term targets is more democratic, and given every politician's desire to avoid public opprobrium, more effective.

Program review—allocating the cuts

The second principal element of our fiscal strategy is a practical procedure to address the seemingly intractable problem of allocating spending cuts among departments and agencies. Even with a strong collective commitment to a fiscal target, it is inherently difficult for a large group of ministers to accept spending cuts that differ significantly from ministry to ministry. The reason is that such variations put the spotlight on differences in government priorities and put individual ministers at risk of looking like losers to their constituencies, their perceived losses being the stuff of headlines.

That is why all governments are tempted to resort to uniform cuts across all programs. And while this can sometimes be justified in the early stages of fiscal consolidation, it eventually becomes a cop-out. Moreover, it is fraught with moral hazard since a policy of uniform cuts destroys the incentive for individual departments to become as lean and efficient as possible—that is, in the next round of cuts, the keener would risk hitting bone while their lax counterparts would still have fat to slice.

We therefore rejected a uniform, across-the-board approach to meeting our deficit targets. Instead, we launched a comprehensive review of virtually all programs to identify those where a continuing federal role was still justified and to find ways to deliver our services more efficiently. The prime minister appointed a special committee

of ministers to consider proposed departmental spending cuts. This involved my colleagues directly in the tough job of examining spending, line by line, and thus fostered an even stronger buy-in to our budget goals. The process was disciplined by a firm requirement that the individual spending cuts had to add up to a predetermined level of savings needed to meet our budget targets. Once the departmental amounts were ratified, it was left to individual ministers to establish priorities within their own areas of responsibility so as to achieve their sub-targets.

The program review exercise was completed in about six months and produced agreement on departmental spending reductions totaling almost 20 percent from 1994-95 levels, spread over three years. This represents an unprecedented, and in many ways revolutionary, change in the way the Government of Canada operates. It is forcing the government to focus sharply on those things—and only on those things—it is in the best position to do.

The incentive to choose carefully is particularly powerful since under our Expenditure Management System there are no longer any "policy reserves" set aside to finance new initiatives. A new proposal must therefore find funds from re-allocation of existing spending.

All of this is part of a process that we call "getting government right" and, like the analogous process in the private sector, it is a job that is really never finished. What is needed therefore is to inculcate in government a culture of continuous improvement and continuous assessment of priorities.

Public consultation—the open budget process

The third major element of our budget strategy has been to engage the public—the experts, the interest groups, and the average citizen—in dialogue as to the adequacy of our targets, the prudence of our assumptions, and the potential fiscal measures themselves. In Canada, by contrast with the practice in the United States, budget secrecy has been very much the tradition. My predecessors began to change that, and we have built on their efforts.

Although the details of last February's budget were kept confidential right up to budget day, we initiated the consultation process more than four months in advance. It was kicked off with the release of major background papers that launched an extensive round of public hearings by the Finance Committee of the House of Commons.[7]

This proved to be a remarkably effective public education process, both for the public and for us. Among other things, it stimulated an out-pouring of detailed mock budgets by various interest groups, media columnists, and individual citizens. Although there was no clear consensus—except perhaps that our economic assumptions should be prudent and that personal tax rates should not be increased—the open budget process unearthed virtually every feasible option.

Overall, we believe that the consultation contributed importantly to creating reasonable expectations as to the magnitude and the general nature of the budget actions that were needed. This is surely of great importance in building public understanding and support for any ambitious program of fiscal consolidation.

We also took care to ensure that the budget was understood abroad. Senior economic ministers traveled to the financial capitals—New York, London, Tokyo—and were available on budget day to deliver briefings and to answer questions directly on the economic and political significance of what we were announcing simultaneously in Ottawa.

To summarize—the principal elements of our budget strategy were:

> First, to set two-year rolling deficit targets backed up by an ironclad political commitment to hit the targets and to base fiscal forecasts on prudent economic assumptions further supported by substantial contingency reserves;
>
> Second, to establish an internal process with the authority to allocate spending reductions among departments, reflecting overall government priorities; and

Third, to engage in wide-ranging pre-budget public consultations.

Frankly, this neat ordering suggests a degree of logic and strategic coherence that is more apparent in retrospect than it was as events were unfolding in all of their uncertainty. For while it is true that we tried to guide ourselves pretty much as I have just described, external factors also played a key, and in some respects determinative role.

The most important of these factors arose from the macroeconomic climate during the pre-budget period from about September 1994 through budget day on February 27th of this year. Successive bouts of currency volatility—particularly marked during the Mexican peso crisis—put unexpected upward pressure on Canadian interest rates. We had to deal with this just weeks before the budget to ensure we had a credible plan to hit our upcoming target. It also underlined our fiscal vulnerability and the loss of control that comes from too much debt.

Mexico's difficulties last winter were something of a wake-up call. There we saw a concrete demonstration of a nation's vulnerability to global financial markets. It was the kind of object lesson that politicians find more compelling than hypothetical scenarios from business economists, media pundits, and rating agencies.

The Mexican episode did influence the budget because it directly affected something that had the potential to throw us off target—like an unanticipated hike in Canada's interest rates or a downbeat change in the growth forecast. So, while the Mexican crisis clearly fell into the category of real perturbations in the economy, Moody's pre-budget signal of a potential downgrade of our debt did not.

Once we set our fiscal target, the thing that matters above all else is our absolute political commitment to hit that target. And the fact that the targets are near-term means that we have had to react immediately to events like Mexico. Had the deficit target instead been several years off, we could easily have rationalized doing nothing to correct our course. Over time, however, the consequences

of such complacency tend to accumulate—one more reason why targets end up being missed. Our approach avoids that risk.

What lessons might be drawn from all this? Looking back in summary on last February's budget, I believe it succeeded despite the tough medicine, for basically the following reasons:

First and most fundamentally, the majority of Canadians were already on-side with our general objective—in fact, on the fiscal issue, the public was out in front of most governments, a message many in our caucus brought home to us loud and clear.

Second was the fact that the budget immediately won the approval of opinion leaders thanks to the prudence of its overall set of assumptions and to the structural quality of the measures themselves.

Third, the actions in the budget were broadly seen to be balanced and fair and to be generally responsive to the public's overall sense of priorities. Most of the credit for this has to go to my cabinet colleagues who not only had to make the sacrifices in their own ministries, but then had to sell the overall justification to their constituencies.

Fourth, we achieved substantial fiscal savings while keeping new taxes to a minimum and especially by ruling out any personal income tax rate increases. The fact that we cut back so heavily on our own activities, rather than putting the burden of deficit reduction on the backs of taxpayers, was a key plus. The biggest hits, as they would say in Washington, were "inside the Beltway."

Finally, we have had reasonable success in communicating why action to deal with deficits and debt had to be the government's immediate priority and why this was not inconsistent with our jobs and growth agenda—in fact, quite the contrary.

The 1995 budget is, of course, not the end of the story. The goals of a significantly reduced debt ratio and a balanced budget are that much closer, but still not achieved. There will be new interim deficit targets to be set and further structural reforms to be implemented. For example, we are already committed to reform the public pension system to make it fairer and more sustainable. We will shortly be introducing further structural reform of unemployment insurance. Our program review continues.

The bottom line message here is clear. It is that our commitment to stay the course of fiscal recovery is unequivocal, and the foundations for that recovery are already solidly in place.

Reflecting, in conclusion, on the broader significance of what we are going through, the 1994 and 1995 budgets were obviously much more than cost-cutting exercises to get the markets off our back. What we have really launched is a fundamental reappraisal of the appropriate role of the national government.

The context for such a reappraisal is an increasingly interdependent global economy where no nation, however powerful, can really control even so basic a parameter as the exchange value of its currency. The truth is that the limits on the ability of governments everywhere to decree social and economic outcomes have become starkly apparent.

This has created a dissonance between what we have conditioned our citizens to expect from their governments, and what governments are actually able to deliver. Contradictions abound.

For example, the public is increasingly skeptical that government can directly create net new jobs, yet when the unemployment rate rises, government is blamed.

There is a similar public skepticism about the ability of government by itself to cure many of the social ills afflicting individuals and communities. Yet it is in our compassionate nature—as that nature has been conditioned over the past several decades—to still expect government to set things right.

We could go on citing examples like these. But the point is that those of us who are committed to a pro-active role for government, in both the social and economic domains, also have a responsibility to begin distinguishing clearly those things governments can do from those they can not. It's time to come clean and stop creating unrealistic expectations.

In Canada's case—a highly sophisticated, yet relatively small and open economy, heavily indebted to boot—these issues have particular salience and urgency. For us, globalization—whether of financial markets or of economic competition—is simply a fact of life. The real challenge we face is to turn globalization to our favor and to maximize our freedom of action.

The only way to do this, it seems to us, is to put our fiscal house in order, and to do all we can to boost productivity. This last point is crucial because productivity is the foundation of competitiveness, and international competitiveness is the only dependable route to economic independence, growth, and jobs.

Seen in this light, our fiscal strategy is also a strategy to safeguard Canada's independence. But it is also true that the restraint associated with the strategy is leading to a government that is smaller, at least by the measures of head count and spending volume. For some, smaller government is an objective in itself. But for us, it is simply a means to an end. We do believe that government should do only what it can do best—and leave the rest for those who can do better—whether business, labor, or the voluntary sectors.

What we must still achieve at the end of the day is a government that is fully capable of assisting the disadvantaged; a government that is unequivocally committed to our publicly-funded national system of health care; a government that is more adept at providing those things the private marketplace cannot—things such as strategic support for aspects of science and technology; and a government that is focused on getting the incentives right—whether to foster environmental protection, to attract footloose investment, or to spring people from the welfare trade and onto the job ladder.

In broadest outline, the redefined role of government is becoming clearer. In metaphorical terms, it is to be more like the tiller of a sleek, modern sailboat than the paddle wheel of a nineteenth-century steamer.

Yet achieving the transformation still poses a very large challenge. This is because the habits and incentives of bureaucrats and politicians, and the institutions they have created over the past fifty years, have all been adapted to the fiscal growth of government. We have not yet learned how to act as creatively as we must in the new environment of static or shrinking financial resources. That constraint is also forcing us, as never before, to concentrate on the setting of priorities, and on discovering how to do what is genuinely needed without spending a lot of taxpayers' money.

What is called for here is not only a change in attitude; it is a sea change in the nature of politics as it has been practiced in the affluent democracies over the past five decades. The job of getting government right, or re-inventing government, or whatever the phrase is much more than a slogan. Creating a public sector where it can truly be said that "less is more" is the greatest challenge we face.

Endnotes

[1]The debt figures in this paper are stated on a Public Accounts basis to accord with most presentations of fiscal data in Canada. On a National Accounts basis—which corresponds to OECD comparative presentations, and to U.S. budget data—net government debt in Canada is about 64 percent of GDP.

[2]The federal government is currently responsible for approximately 47 percent of the program spending of the federal and provincial governments combined, while the net federal debt is about 73 percent of the combined total.

[3]Upon taking office in 1993, the government agreed formally with the Bank of Canada to a target band for CPI inflation of 1 percent to 3 percent through 1998.

[4]*Creating Opportunity: The Liberal Plan for Canada, 1993*, p. 20.

[5]See *A New Framework for Economic Growth*, Government of Canada, October 1994.

[6]We have also set a deficit target of C$32.7 billion for 1995-96, but this has received much less public attention than the 1996-97 target of 3 percent of GDP (estimated to be C$24.3 billion).

[7]*A New Framework for Economic Growth* and *Creating a Healthy Fiscal Climate: The Economic and Fiscal Update*. The latter publication presented the fiscal implications of a range of economic scenarios and derived from these the amount of fiscal action in each case needed to achieve the designated deficit targets for 1995-96 and 1996-97. The document also contained quite detailed information on departmental spending, tax expenditures, and revenue sources.