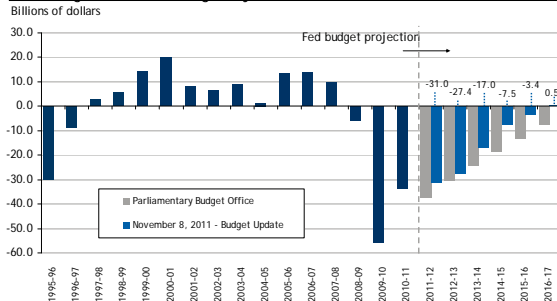


2011 FEDERAL BUDGET UPDATE

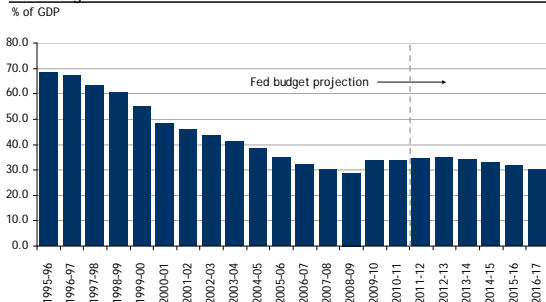
November 9, 2011

Federal government budgetary balance*



*Does not include projected savings from the Strategic and Operating Review
Source: Department of Finance, RBC Economics Research

Federal government debt



Source: Department of Finance, RBC Economics Research

The Federal Government's Economic and Fiscal Update, released today, indicated a delay in balancing the budget by one year. On an "official" basis, which excludes the savings from the Strategic Operating Review, a surplus of \$0.5 billion is achieved in 2016/17. This compares to a \$4.2 billion surplus projected for 2015/16 in the June 2011 Budget. If the strategic operating savings are included, the budget is balanced in 2015/16 with a \$0.6 billion surplus which again is a year later from the \$3.4 billion surplus projected for 2014/15 in the June 2011 Budget. Slower-than-expected economic growth this year, combined with a number of downside risks to the economy that could affect growth in the future, have significantly altered the expected revenue and expenditure profiles.

Higher oil prices, supply chain disruptions from natural disasters and slower US growth have all contributed to weaker-than-expected economic growth in Canada so far this year. At the time of the budget, the average private sector forecasts for Canadian real GDP growth in 2011 and 2012 were 2.9% and 2.8%, respectively. These have now been revised down to 2.2% and 2.1%. Other major changes to the economic forecast include lower-than-expected interest rates, higher inflation and a stronger Canadian dollar; the unemployment projections have remained unchanged. On the whole, the government estimates that changes to the economic forecast will lower revenues by \$46.4 billion over the forecast period, including a \$3.9 billion reduction in 2011/12 and a \$9.0 billion reduction in 2012/13. This is partially offset by reduced interest payments, which will lower debt charges by \$18.8 billion over the forecast period (\$1.5 billion and \$4.6 billion in 2011/12 and 2012/13, respectively.). Adding in changes in expected expenditures (the biggest change is a \$5.6 billion reduction in 2011/12, due to lower-than-expected EI expenses and the repayment of British Columbia's HST payment), the net effect of "economic and fiscal developments" is -\$22.4 billion over the next 5 years. Because of the uncertainty of the economic situation, the government also increased its adjustments for risk. The adjustment was \$3.0 billion in 2011/12 and \$4.5 billion in 2012/13.

The only significant adjustment to the government's budget plan was a reduction in planned EI premium increases. The 2012 increase has been reduced from 10 cents to 5 cents per \$100 for employees and from 14 cents to 7 cents per \$100 for employers. According to the update, this should result in roughly \$600 million in lower revenues. The government also extended an enhancement to the Work-Sharing Program, first enacted in 2009.

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On an “official” basis, the deficit is now expected to be -\$31.0 billion in 2011/12, \$1.3 billion lower than planned in the budget. The deficit for 2012/13 is now expected to come in at -\$27.4 billion, \$8.0 billion higher than expected. The deficit will gradually shrink to \$3.4 billion in 2015/16, before returning to surplus in 2016/17.

Central Bank Mandate

A joint statement released by the Government of Canada and the Bank of Canada today confirmed that the 2% mid-range inflation target was maintained. The agreement will run for another five-year period, ending December 31st, 2016. One noteworthy modification to the announcement is that the word “flexible” was added to modify any reference to the inflation-targeting framework.

Summary statement of transactions (billions of dollars)

	Projection						
	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
Budgetary transactions							
Budgetary Revenues	237.1	243.5	251.8	268.8	285.1	298.4	310.6
Program Expenses	239.6	243.0	247.4	252.5	257.6	265.3	272.4
Public debt charges	30.9	31.5	31.9	33.3	35.0	36.5	37.7
Total Expenses	270.5	274.5	279.2	285.8	292.6	301.8	310.1
Budgetary Balance	-33.4	-31.0	-27.4	-17.0	-7.5	-3.4	0.5
Federal Debt	550.3	585.2	612.7	629.7	637.2	640.6	640.0
Per cent of GDP							
Budgetary revenues	14.6	14.4	14.4	14.6	14.7	14.8	14.7
Program Expenses	14.7	14.4	14.1	13.7	13.3	13.1	12.9
Public Debt Charges	1.9	1.9	1.8	1.8	1.8	1.8	1.8
Budgetary Balance	-2.1	-1.8	-1.6	-0.9	-0.4	-0.2	0.0
Federal Debt	33.9	34.6	35.0	34.2	32.9	31.7	30.3

Economics assumptions (Year-over-year % change)	Budget						Economic and Fiscal Update					
	2011	2012	2013	2014	2015	2016	2011	2012	2013	2014	2015	2016
Real GDP growth	2.9	2.8	2.7	2.5	2.5	n/a	2.2	2.1	2.5	2.5	2.5	2.3
GDP Inflation	2.8	2.1	2.1	2.0	2.0	n/a	3.0	2.0	2.0	2.0	2.0	2.0
Nominal GDP growth	5.8	5.0	4.9	4.5	4.5	n/a	5.3	4.1	4.5	4.5	4.5	4.3
3-month Treasury bill rate*	1.3	2.5	3.4	3.9	4.1	n/a	0.9	1.2	2	2.9	3.5	3.7
Ten-year government bond rate*	3.5	4.0	4.6	4.8	5.0	n/a	2.8	2.7	3.2	3.9	4.5	4.5
Unemployment rate	7.5	7.2	7.0	6.7	6.5	n/a	7.5	7.2	7	6.8	6.6	6.4
U.S. real GDP growth	3.1	3.1	3.2	3.3	3.2	n/a	1.6	2.0	2.4	2.9	2.9	2.8

* %, end of period

Source: Statistics Canada, Bureau of Economic Analysis, RBC Economics Research

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