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ECONOMY

Liberals' upcoming budget worries Canadian businesses

Concerns over potential tax hikes

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ADRIAN WYLD / THE CANADIAN PRESS

Finance Minister Chrystia Freeland will deliver the spring budget on April 16.

Finance Minister Chrystia Freeland's upcoming budget has some in Canada's business community concerned there will be tax increases to offset new government spending.

Freeland and Prime Minister Justin Trudeau will almost certainly bring in a package of tools to boost housing supply in the April 16 budget, according to people familiar with the government's plans, and may commit additional spending to industrial subsidies, defence, university research and drug plans.

So new measures to raise revenue will likely be needed if Freeland is to stick to her promise to keep deficits from growing, unless she opts to cut spending in other places. In November, the government projected annual deficits about $40 billion between 2023 and 2026 — but the country's fiscal watchdog has already raised doubts it will meet this year's target.

Trudeau and Freeland face political constraints, too. They can't afford to produce a budget that's seen as inflationary. The governing Liberal party is far behind Pierre Poilievre's Conservatives in opinion polls, and frustrations about the cost of living are a leading cause of those woes. The government wants interest rates to fall.

Some business leaders are worried Freeland is considering hiking corporate taxes, such as a broad-based tax on profits of large companies. It's a tactic the government has used before: in 2022, Freeland levied a one-time tax on windfall profits by major banks and insurers, and last fall Trudeau threatened grocers with new taxes if they didn't help rein in food inflation.

An excess profits tax would be favoured by the opposition New Democratic Party, which is propping up Trudeau's government in Parliament.

"The latest rumour in Ottawa is the government will try to solve its problem by introducing a new corporate tax — one that targets Canada's most successful companies," Goldy Hyder, chief executive officer of the Business Council of Canada, wrote in an editorial published in The Hub on March 6.

Hyder said large businesses "have become a popular punching bag for politicians," but warned that taxing profits would "further discourage business investment in Canada and force successful Canadian companies to either constrain or cancel any growth plans."

Freeland's office declined to comment on any potential tax measures in the budget.

Still, Trudeau and Freeland may decide a battle with business over taxes is preferable to letting the deficit run higher. A loose fiscal policy risks giving pause to the central bank's rate-setting committee as it debates whether and when to start lowering borrowing costs.

Some economists point out that government spending in recent years — including on COVID-19 emergency programs, which led to a record $328-billion federal deficit in the first year of the pandemic — has already complicated the central bank's job. Last year, Bank of Nova Scotia economists estimated that the combined spending of provincial and federal governments forced the Bank of Canada to add as much as 200 basis points of tightening.

On the other hand, drastically cutting spending now risks weakening an economy that's already struggling.

"Now that rates have gone up this much, I don't think it would be especially constructive to really slam the brakes on the fiscal side," said Doug Porter, chief economist with Bank of Montreal, adding that he'd still "heavily caution against spending a lot more at this stage."

The government will get some help from a spending review recently led by Treasury Board President Anita Anand, which she says "refocused" $10.5 billion in planned travel and consulting expenses over the next three years toward priorities such as housing, health care and the clean economy.

Still, the spending estimates she introduced in Parliament project $449.2 billion in spending in the upcoming fiscal year — on top of anything to be announced in the spring budget. That's an increase of $16.3 billion, or 3.8 per cent, from the main estimates for the current fiscal year, which ends March 31.

Anand rejected calls to cut spending. "We did not want to undermine services to Canadians," she said. "We're reallocating money that can be used for a higher purpose."

Trudeau has taken some steps to reduce inflationary pressures. After a record surge in international students, Immigration Minister Marc Miller set a cap on the number of study permits — cutting them 35 per cent relative to those issued in the previous year. That's expected to ease pressure on rental costs, which rose 6.5 per cent last year.

There's also some inflation risk attached to the budget plans of provincial governments, which are planning to ramp up spending.

"I think there are some question marks about how much fiscal restraint or stimulus there will be at the provincial level," said Avery Shenfeld, chief economist at Canadian Imperial Bank of Commerce.

With assistance from Jay Zhao-Murray. Bloomberg