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Budgets for Bad Times*

Preparing a budget was a breeze for those of us in Ontario's Finance department in the late 1980s. Every week or so, we would present Bob Nixon (the Finance Minister in David Peterson's Liberal government) with a revised forecast. Another $500 million to add onto the revenue estimate…another billion…one more billion. Nixon jokingly complained about our inability to predict revenue, but as a seasoned Finance veteran quipped: "No one screams when the rollercoaster is going up."

Then the rollercoaster started going down. As it gathered speed, Ontarians began to scream. They kicked out the Peterson government and, to everyone's surprise, elected the NDP under Bob Rae. But Bob Rae was as helpless to stop the rollercoaster's plunge as was Peterson before him.

With a recession hitting the US, the auto sector – which supports about 25 percent of Ontario's economy – went flat. To make matters worse, the Bank of Canada jacked up interest rates, deciding that now was the time to put an end to inflation. High interest rates burst southwest Ontario's bulging real estate bubble, prices collapsed and the construction industry ground to a halt, throwing tens of thousands of construction workers onto the unemployment lines. The remainder of Ontario's manufacturing industry followed the downhill ride as high interest rates forced the Canadian dollar to rise against the US dollar. To add to the melee, the Mulroney government brought in the GST. Suddenly consumer spending ground to a halt along with everything else.

At his inauguration Bob Rae sang "We Ain't Got a Barrel of Money." By the time he got to his first budget, he didn't even have the barrel.

Of course, Ontario was not alone. The rest of Canada, the US and much of Europe was in an economic funk. Yet Ontario seemed to be doing worse than everywhere else. We climbed so high in the 1980s that it felt like a longer way down in the 1990s. So the Rae government began to 'own' the recession despite the continental economic decimation.

The NDP's first budget proudly stated that it was 'fighting the recession, not the

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deficit' as if Ontario could singlehandedly spend its way out of the recession. But the recession continued and deficits piled higher and higher. In the meantime, inflation abruptly fell from just below 10 percent to the 2 to 3 percent range. Yet public service contracts and agencies demanded annual increases of more than 5 percent. The impression was left of a rich government and a poor people, with public sector workers immunized against the recession hammering everyone else.

Within a few years, the deficit was threatening to reach more than $15 billion and the government was forced to pivot. Ontario's budget for internal government operations was slashed by several billion dollars. Funding increases for the broader public sector – consisting of everything from hospitals to children's aid societies – were cut down to reflect current price inflation in the vicinity of 2 percent. And the famous 'Rae days' (compulsory unpaid days off work) were introduced as a way of reducing costs without laying off workers.

A decade and a half later, 'Rae days' are springing up all over the United States. We are once again in an economic downturn. Except this time it is much worse. The 1990s crisis was largely created by central banks as a means of stemming inflation. The financial system remained intact. Outside of North America and Europe, Asian economies were relatively healthy. In today's economic crisis a huge mountain of US debt has collapsed, leading to an abrupt and dramatic contraction of economic activity across the whole world. No one knows exactly what to do.

The current economic downturn is not only more serious than the 1990s, the politics in Ontario are dramatically different. Last time, deep tax cuts and deregulation were the flavour *à la mode* among business leaders and many economists. This time, the conservative agenda is discredited. No one but some die-hard Republicans any longer promulgate the policies that brought us to this dismal juncture. In the 1990s Keynesian stimulus was derided as out of date: Today everyone, including Stephen Harper, is a Keynesian whether they like it or not. Last time, Ontario – and especially Toronto – seemed to be the epicentre of its own mini-depression. This time, the recession clearly began in the US and spiralled outward.

Despite these differences, there are lessons that the current Ontario government can learn from the Rae government's experience in the 1990s.

Queen's Park must try to set reasonable expectations. It neither caused the global economic crisis nor can it cure it. Provincial governments have the most important economic tasks – maintaining an excellent education system, modern infrastructure and vibrant communities. But these are long-run determinants of prosperity. In the short term, the province is not an economic island and cannot catapult itself back to economic health while the rest of the world languishes.

The McGuinty government's next budget should delineate a constrained set of objectives during the recession to help those hardest hit and to put unemployed resources to good use by building for the future. To do this Ontario needs to maintain, even improve, the social safety net. The province can expand educational opportunities for the unemployed. It can take advantage of reduced construction costs to catch up on its backlog of infrastructure, especially looking forward to a greener province. It can do a lot of good, but it cannot buy its way out of the recession.

While huge deficits are today unavoidable and even desirable, the Ontario government must be seen to have a path back to fiscal prudence. Had the Rae government somehow survived the 1995 election, Ontario's budget would have been balanced in a few years followed by large surpluses. But the public was convinced that the NDP government had a love affair with debt, and it proved impossible to shake this perception. Ironically, the succeeding Harris government's tax cuts and spending increases did lead to growing debt even during the boom years, but the Conservatives presented themselves as good fiscal managers.

The McGuinty government does not want to find itself stuck with the label of a profligate spender, ignoring the public debt. It must express regret at the necessity of accumulating debt and show that it has plans to manage the fiscal health of the province over the long run.

When Ontario Finance Minister Dwight Duncan unveils his new budget on March 26, the economic roller coaster will still be racing downhill. No one knows when it will stop. Being Finance Minister at this time of deep economic malaise is no fun, but Duncan has some advantages that the Rae government did not. It should be evident to all that Ontario did not cause the recession and cannot end it. There is no opposition waiting in the wings with a magic solution of tax cuts to solve all pain. Duncan can steer a path for Ontario which will see us through the bad times with as little hurt as possible, and perhaps even put the province onto a path of greater prosperity when this bad trip finally ends. Unlike the Rae government, it is possible for the McGuinty government to survive the recession.

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