

The contents of this document are preliminary and subject to change.

GRAY/21/643

March 10, 2021

**Statement by Mr. Buissé, Mr. Rozan, and Mr. Roman on Canada
(Preliminary)
Executive Board Meeting
March 12, 2021**

We thank staff for a very comprehensive set of reports and Ms. Levonian, Ms. Vasishtha, and Mr. Weil for their insightful Buff statement. The Covid-19 pandemic has taken a significant toll on the Canadian economy, and we commend the authorities for their swift, strong and multi-pronged policy responses to meet the challenges of the crisis. **As the authorities intend to detail their recovery plan this spring, we concur that such a plan will be essential to ensure a a strong, sustainable, and inclusive economic recovery, and we welcome the authorities' intention in this regard, as they flesh this plan out.** We share the thrust of staff's appraisal and we wish to make the following comments.

We broadly agree with staff's projections for the near-term economic outlook and we take note of staff and authorities converging views regarding downside and upside risks. Like in many other countries, there is still months to wait before a sufficient vaccination coverage is reached. Therefore we welcome from the Buff statement that vaccination is the top health priority, with the goal of ensuring that anyone who wants to be vaccinated will be by September of 2021 – a timeline which is broadly in line with many advanced economies. In the meantime, mitigation efforts will help minimize economic disruptions. We do note that since the report was written, a significant upside risk has materialized, with the vote of the US Covid-19 relief bill. *We would be interested to have staff's indication regarding the upside this represents on Canada's macroeconomic outlook.*

We welcome the authorities' intention to maintain their support until the recovery is well entrenched, basing their decision on data-driven triggers. The unprecedented fiscal support, amounting to 20% of GDP, provided a much-needed support to households and businesses. We also wish to underscore staff's assessment that it helped to avert an even sharper fall in output. While initial support measures showed some weaknesses in their design, the authorities appropriately revamped the mechanisms to minimize potential disincentives to activity. We positively see that the crisis has already prompted changes to the employment insurance system and that the authorities will continue to review it, along with the broader social safety net. This could go a long way to achieve a more systematic

framework for cyclical stabilization, for which we see a strong economic and social case. More broadly, as the authorities are fleshing out their medium term recovery package, we agree with the authorities that they have the fiscal space to sustain their policy approach. We look forward to have more information on the design of the recovery plans as they become available. Going forward, it will be useful for the authorities to initiate a debate on their medium-term fiscal strategy, and we note in that regard that they have committed to outlining a long-term fiscal anchor when the economy is more stable. Given the emerging demands on new expenditures (also discussed below), it seems likely that such anchor would imply to increase revenues.

The monetary policy has been appropriately accommodative. The Bank of Canada acted quickly to support financial markets by lowering interest rates, providing liquidity, and purchasing government and corporate bonds. We positively note that significant progress has been made towards implementing recommendations from the 2019 FSAP and we encourage the authorities to address the remaining gaps. We particularly encourage the authorities to continue to closely monitor the macroprudential policy stance to ensure it remains appropriate in light of household debt and housing market risks.

We look forward to the federal government’s intention to release a “Build Back Better” plan in the course of the spring. *We note that this commitment to spend between 3 to 4 percent of GDP over the next 3 years to help jumpstart the recovery “needs further justification” in staff’s views, and we would be interested to hear more from staff on the type of justification that is expected.* On some likely areas of focus of the recovery plan, we wish to offer the following comments:

- (i) We welcome the strong focus of the Canadian authorities on supporting the **green economy and the climate transition**. The Canadian Net-Zero Emissions Accountability Act combined with the carbon pricing scheme - which is dubbed by staff as a prototype for other countries - are important steps towards achieving the ambitious targets to mitigate GHG emissions. We note that the pricing requirement of CAN \$40 per ton (CO₂) for 2021 will make Canada, along with the EU, the frontrunner on carbon pricing. We positively note staff’s mention that policymakers might consider a transition away from the output-based performance standard to a border carbon adjustment, and an international carbon price floor (ICPF) arrangement.
- (ii) We also see very positively the recent announcement to develop a Canada-wide **early learning and childcare system**, in a context where Canada has one of the lowest enrolment rates in early childhood education and care in the OECD. *Could staff detail the authorities plans in that regard and the likely positive effects on female labor force participation?*
- (iii) **Structural reforms** to increase competition, trade integration between provinces, and shift taxes from production to consumption would also help address the productivity gap.

We welcome the selected issues report on income inequalities, which have been rising in many advanced economies over recent decades, albeit to a lesser extent in Canada. Canada indeed has the lowest Gini coefficient in the G7 in terms of market income. However, after redistributive policies, the coefficient based on disposable income ranks third,

as redistributive policies seem less effective than in other countries with stronger social safety nets and more progressive tax systems.

Finally, we are of the view that external trade issues could have warranted a more thorough analysis, given its importance for the Canadian economy. In addition, we agree with staff's recommendations aimed at boosting Canada's non-energy exports, especially considering the medium-term perspective of increasing global carbon prices and exit from fossil fuels. More generally, the consequences of climate change on the medium-term outlook for Canada, which heavily depends on oil exports, could be further developed in future article IV.