

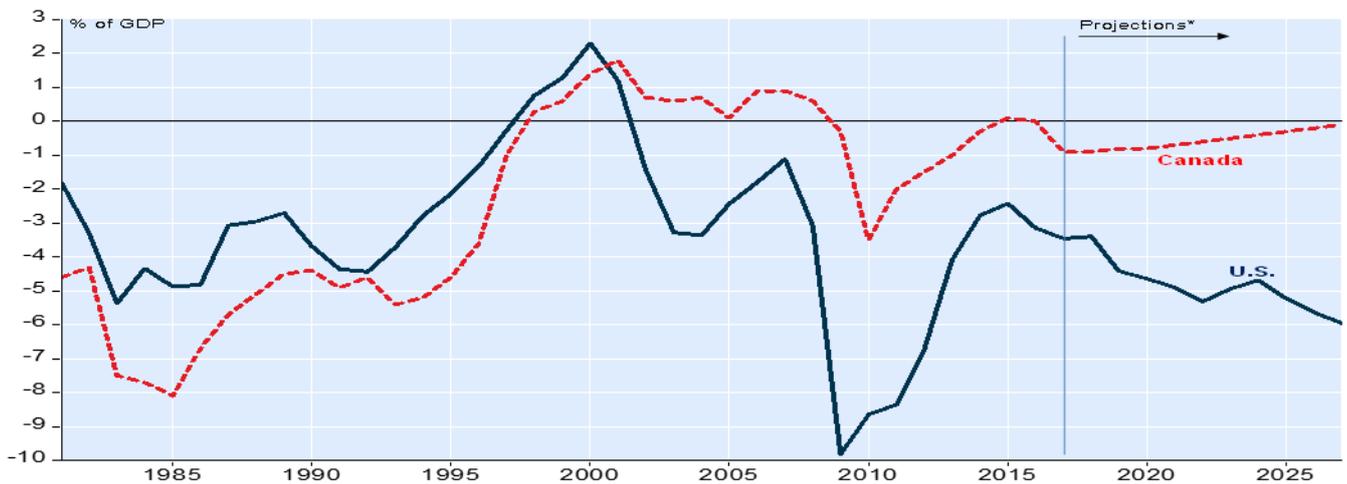
Quick Hit – Fiscal fundamentals matter after all

My colleague Krishen Rangasamy banged out his latest in a long series of very interesting *Hot Charts* earlier today, the focus of which was the stream... you might say river, or better yet, tidal wave... of red ink running through the US federal budget outlook should President Trump's tax proposals come to fruition (as currently set down). In traditional Canadian fashion, it's worth exploring how *our* federal budget outlook stacks up vis-à-vis the path being proposed stateside. Well, the Government of Canada presented a fall update only a couple weeks back, complete with fiscal projections out to 2022-23. Yes, Ottawa's bottom line is printed in red ink too, but from any objective/relative perspective, we're talking about fairly modest and manageable budget shortfalls. (If you're seeking further, independent verification, we'd direct you to the Canada's Parliamentary Budget Officer.) Quite simply, Canada's federal deficit is a fraction of that being run in the US, and seemingly destined to stay that way (Chart 1). That means relatively lighter net funding needs, which statistically hold sway over longer-term Canada-US yield differentials. We won't pretend that fiscal differentials are the be all and end all; individual debt management strategies, investor demand dynamics and global risk sentiment exert a lot of influence too. Nonetheless, Canada's more favourable/sustainable budgetary path supports tighter yields to the US, all else equal (Chart 2). Turns out, fiscal fundamentals matter after all. [Special thanks to NBF Economics for the following two charts.]

Chart 1

Canada's budget deficit smaller than that of the U.S.

Budget balance

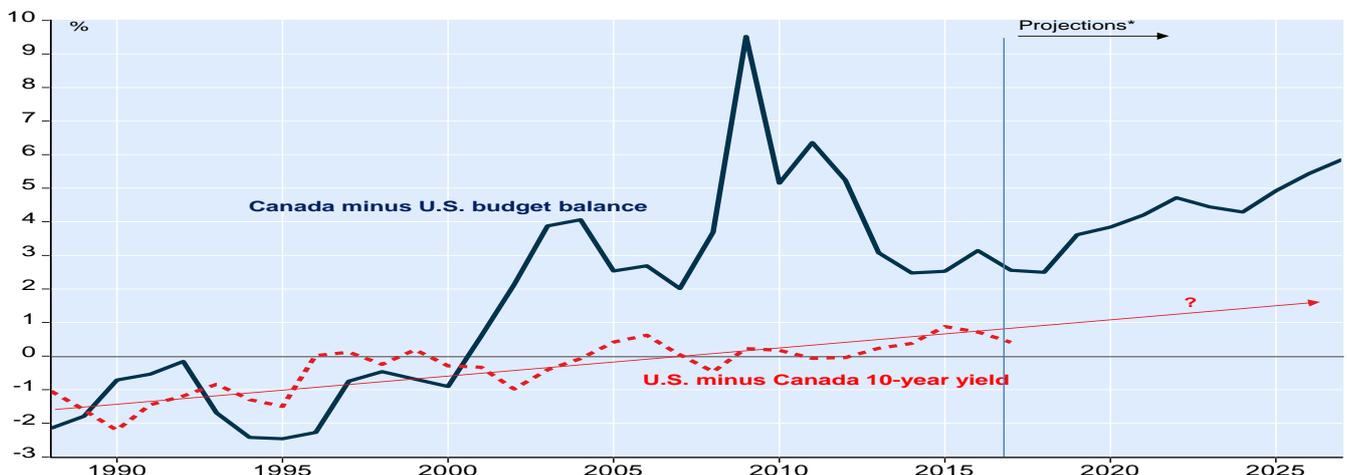


* U.S. projections come from Congressional Budget Office; Canadian projections come from Department of Finance (up to 2023), 2024-2027 projections based on trend NBF Economics and Strategy (data via Congressional Budget Office, Department of Finance)

Chart 2

Are spreads about to get tighter?

Gap between Canada-U.S. budget balance versus 10-year government yield spread



* U.S. projections come from Congressional Budget Office; Canadian projections come from Department of Finance (up to 2023), 2024-2027 projections based on trend NBF Economics and Strategy (data via Congressional Budget Office, Department of Finance)

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