

# Canada & U.S. growing apart (fiscally speaking)

By Warren Lovely & Ethan Currie

President Biden surely has a lot on his plate. Indeed, the Pres was trotted out just this morning in an attempt to soothe markets rattled by the SVB collapse and mounting carnage in the U.S. banking system. Notwithstanding a demanding schedule, we received word last week that Biden is scheduled to head north next week (March 23-24), making his first official visit to Canada since moving into the Oval Office.

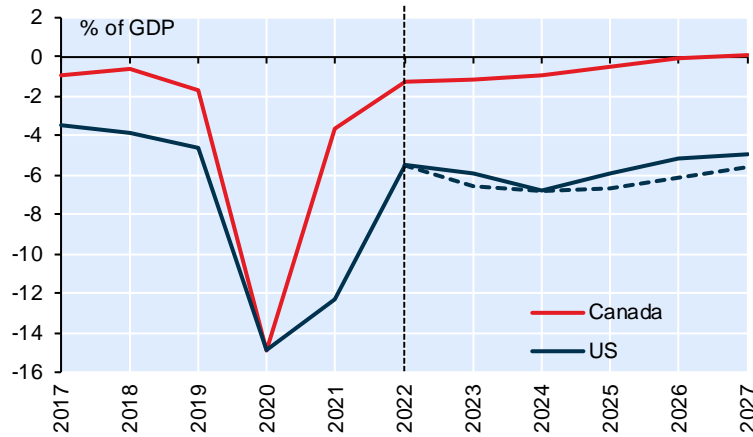
A presidential visit is always a nice photo op. And one can see it now, Biden and PM Trudeau pressing the flesh, trumpeting the vital socio-economic and geopolitical partnership that has long characterized Canada-U.S. relations. But at least when it comes to fiscal policy, the two countries are growing apart... and have been for some time. Two budgets—one from Biden on March 9th and one to come from Deputy PM Freeland on March 28th—highlight the divergence.

The President's fresh budget proposals can be thought of as an opening fiscal volley for a U.S. Congress that is once more engaged in partisan debt-limit negotiations. Biden's budget lauded the fiscal progress made vs. the 'baseline' scenario, with various tax proposals seen chopping nearly US\$3 trillion from the cumulative shortfall to be run from 2024-33. Notwithstanding this apparent or hoped-for fiscal progress, a U.S. federal deficit of 6-7% looks likely in the near term. Canada's fresh budget will provide an opportunity to revise the 2023-24 deficit projection, but as it stands Canada's federal government looks to run a comparatively modest shortfall of 1-2% of GDP.

This budgetary gap of ~5%-pts of GDP means an already striking divergence in debt burdens will become ever more pronounced. Now, just to be clear, the relationship between relative fiscal metrics (budget or debt gaps) and Canada-US yield differentials is hardly iron clad. There's more than pure fiscal fundamentals going into a cross-market rate call, as recent days have made abundantly clear. But over the long(er) term, relative fiscal fundamentals have exerted some influence on rates... this relationship, not surprisingly, appearing to be more relevant out the curve. So, while we're always hesitant to overplay the importance of relative budget proposals, here are two countries, two leaders, two budget proposals that are growing apart fiscally speaking. And all else equal, that lends some non-trivial support to Canada-US yield differentials.

### Chart 1: There's a path to balance in Canada... not in the U.S.

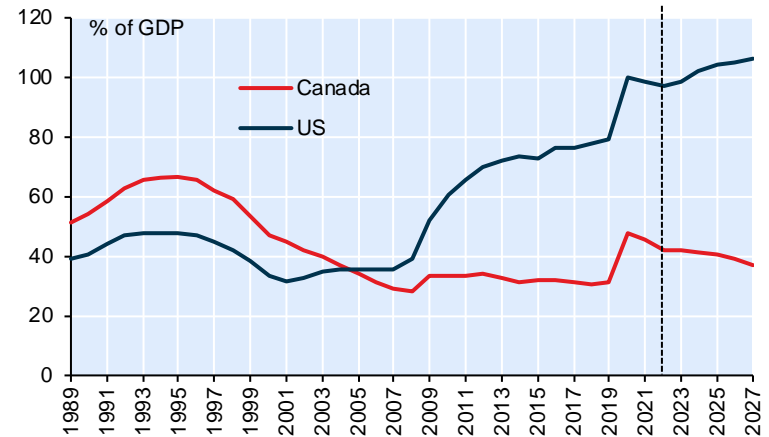
Budget balance (as a % of GDP): Canada vs. U.S.



Source: NBF, OMB, GoC | Note: Dotted line denotes "baseline" deficit while solid line represents Biden 2024 budget

### Chart 2: Debt loads trending in opposite directions

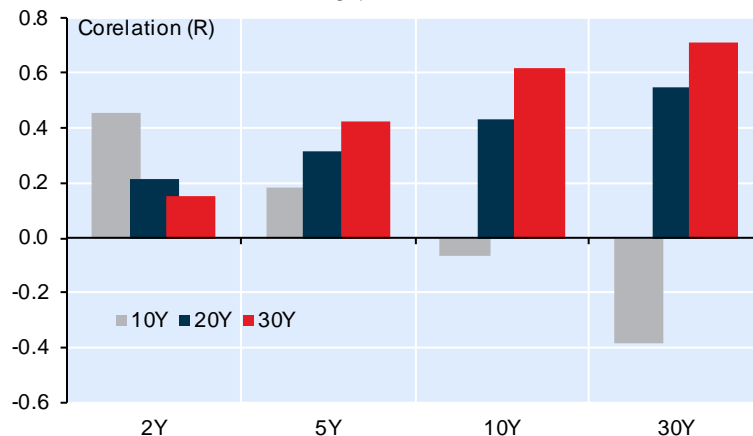
Publicly held debt (as a % of GDP): Canada vs. U.S.



Source: NBF, OMB, GoC

### Chart 3: Relative debt load, rates more correlated in long-end

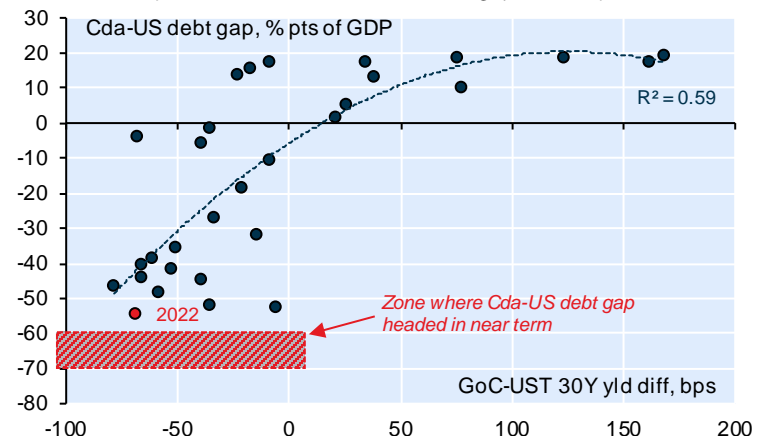
Correlation in Canada-U.S. debt gap & rate differentials: last 10Y, 20Y & 30Y



Source: NBF, OMB, GoC, Bloomberg | Note: Debt gap refers to diff. in debt-to-GDP

### Chart 4: ...suggesting a wide differential can remain (& widen?)

GoC-UST 30Y yield differential & Cda-US debt gap, last 30 years



Source: NBF, OMB, GoC, Bloomberg | Note: Debt gap refers to difference in debt-to-GDP

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