

Erin O'Toole's Conservatives prepare to return Canada to austerity

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Conservative Party leader Erin O'Toole in front of the party's slogan, "Secure the Future." Image: Erin O'Toole/Flickr

During the COVID-19 pandemic, most of the sacred and long-standing precepts of neoliberal macroeconomics were thrown out the window, and for good reason. Dramatic interventions in both fiscal and monetary policy in Canada and other countries helped economies get through the pandemic and resulting recession. Erin O'Toole's Conservatives, however, are now signaling they will quickly reverse course and resuscitate those neoliberal principles if they form the next government.

Governments around the world racked up eye-watering deficits as they opened the fiscal taps to support personal incomes, subsidize businesses, and finance public health responses. Canada was no exception. The federal deficit exceeded \$350 billion for 2020-21, or around 15 per cent of national GDP - the biggest (in relative terms) since World War II, and unimaginable in conventional economic discourse.

Canada's deficit was among the largest of OECD countries, indicating a relatively ambitious response to the pandemic. But most industrial countries also incurred very large deficits: across the whole OECD, they averaged around 12 per cent of GDP.

Meanwhile, provincial governments also incurred record-breaking deficits due to reduced revenues and increased health and other program costs. Every province except New Brunswick (whose COVID-insulated economy traversed the pandemic better than any other) incurred large deficits; Alberta's (at close to 7 per cent of GDP) was by far the biggest.

In monetary policy, too, the conventional obsession with inflation control and monetary rectitude -- already shaken by the global financial crisis (GFC) 12 years earlier -- was abandoned in most countries, in favour of extraordinary interventions to support spending.

Until COVID-19, the Bank of Canada had refused to join other leading central banks in a practice called "quantitative easing" (QE): using the Bank's money-creation powers to buy assets (largely but not solely government bonds) in hopes of boosting money supply, bank lending, and spending. That practice was routinely practiced by other central banks in recent years (in Japan's case, for over 25 years), but the Bank of Canada had refused to use that tool. Given the magnitude of the economic shock caused by COVID-19, the Bank of Canada [finally jumped into the QE fray](#).

Beginning in March 2020, the Bank purchased some \$335 billion in federal bonds -- and about \$20 billion of provincial bonds, to boot. Those purchases (some made directly in new bond auctions, some bought second-hand in commercial markets) kept interest rates super-low, despite the financial uncertainty associated with the pandemic. They also made it easier for the federal and provincial governments to finance their unprecedented deficits.

The combination of these two dramatic shifts in macroeconomic policy exposed the lie of austerity upon which neoliberal economic and social policies have been based for decades. Harsh government cutbacks were always explained on grounds that government just "can't afford" to spend more. This lie was critical to the formulation and legitimation of austerity. Why would populations accept endless belt-tightening, cuts in public services, and privatization of public assets, without this spectre of a binding budget constraint tying the hands of even progressive governments?

The pandemic proved something progressives argued for years: there is virtually no financial constraint to the ability of governments (especially national governments, which possess independent currencies and financial regulatory powers) to mobilize resources in the interests of social and environmental well-being -- *if they choose to do so*.

Canadian governments raised hundreds of billions of dollars to support extensive income supports (through measures not dissimilar from the "basic income" vision advanced by many progressives), subsidize wages and protect employment (in the face of macroeconomic chaos), and invest in expanded physical and social infrastructure -- even stretching to the introduction of whole new programs (like national child care).

The ultimate limit on the capacity to deliver these reforms and supports is the real productive capacity of the economy, not the government's budget. As long as the economy languishes far below that capacity limit, government can and should use its capacity to raise money (including creating it, through a publicly regulated and partly publicly owned banking system), and spend it to stimulate more work, output, and income -- preferably in socially useful undertakings.

The dawning reality that government can do amazing things when it chooses to, poses an existential threat to the narrative that underpins neoliberal fiscal and monetary policy.

Even mainstream economists have been generally supportive of the extraordinary measures taken during the pandemic. Most recognized that adherence to traditional strict doctrines (of deficit-reduction and inflation control) would have turned the COVID recession into an outright depression. Neoliberal purists were always uncomfortable, however, with the idea that large fiscal and monetary interventions to support public health, public services, employment, and infrastructure could be seen as anything more than short-term emergency measures. Conservative politicians went along with these interventions, to an extent (and in many countries, it was conservatives who oversaw them) -- but always with an eye to cramming the genie back into the bottle as soon as possible.

The current federal election campaign has confirmed the Conservative Party of Canada's desire to quickly restore traditional neoliberal goals; smaller government, balanced budgets, and an overarching commitment to inflation control (which is always the most important priority for owners of financial wealth, given the impact of higher inflation on their accumulated holdings).

If they form government, Canadians should expect a whiplash-inducing reversal of the extraordinary measures that were implemented during the pandemic. The consequences for macroeconomic recovery, employment, and social policy (the new national child care program would be the first, but not only, casualty of a return to fiscal rectitude) would be enormous.

For months during the pandemic, Pierre Poilievre -- then the party's finance critic, still a prominent spokesperson, and likely front-runner for party leader in the event O'Toole falters -- was the most outspoken critic of fiscal and monetary supports.

He lambasted both the government's large deficits and the Bank of Canada's money creation. In the Bank's case, Poilievre's attacks were extraordinary and aggressive: accusing the Bank of becoming an ideological tool, [serving as "an ATM" for the Trudeau government's rampant spending](#). Given the accepted mainstream consensus for the last generation in Canada that the Bank should be politically independent from the government, this attack was like throwing a grenade into the polite company of Canada's political and economic elite.

Shortly afterward, Poilievre was demoted from his critic post; shuffled to critic for jobs and industry. He has remained an outspoken and (in some circles) effective advocate of a quick return to neoliberal fundamentals; balancing the budget, refocusing monetary policy on inflation control, and simultaneously (and contradictorily) blaming the Trudeau government for inflation, deficits, and unemployment at the same time.

O'Toole has walked a more nuanced line in attacking the Trudeau government's deficits -- knowing that the lifesaving policies that caused those deficits (like CERB and wage subsidies) were very popular with the public. After all, some nine million Canadians received government income support at some time during the pandemic. So the old political logic of welfare-bashing is no longer as effective for Conservatives as it once was.

Nevertheless, O'Toole has attacked the federal deficit (without saying what programs he would have eliminated to reduce it), blamed Trudeau for the increase in inflation that has accompanied the re-

opening of the economy, and pledged to balance the budget within a decade if elected. That pledge would require years of deep austerity in federal spending, and would almost certainly throw ice water on the economy's rebound from the COVID recession. The experience of Europe after the GFC is painful evidence of the self-inflicted harm caused by fiscal restraint during periods of macroeconomic crisis.

Mind you, we should have already learned that same lesson back in the 1930s.

The modest increase in inflation in recent months (the year-over-year rate hit 3.7 per cent in July) has provided fuel for loud Conservative warnings about the menace of fiscal and monetary laxity. Those arguments are not credible.

The uptick in inflation has been driven mostly by gasoline prices (excluding gasoline, the rate was 2.8 per cent) and a few other volatile commodities. The "core" inflation rate (with volatile items stripped out) was just 1.7 per cent -- still below the Bank of Canada's target. Short-run price pressures resulting from the sudden re-opening of large segments of the economy (such as hospitality) after the lockdowns should be expected, even welcomed. Indeed, for years the Bank of Canada has missed its two per cent target from below; over the last decade, inflation has fallen below the target twice as often as above. A period of above-target inflation would only help to offset the Bank's previous errors in keeping inflation too low (an error on which the Tories were deathly silent). None of that stops O'Toole from using the inflation data to stoke his broader campaign of fear about the consequences of Canada's recent monetary and fiscal policies.

The Tories' lift in public opinion polls during the campaign indicates that these traditional tough-love tropes (of fiscal discipline, the threat of inflation, and the consequences of income supports for the "work ethic" of Canadians) still have political legs, even though few economists, even mainstream ones, endorse their call for fiscal and monetary restraint.

The fact that their commitment to balancing the budget and controlling inflation is completely at odds with their long list of potentially expensive spending promises (including an expansion of EI benefits, business subsidies, and even taxpayer-supported restaurant meals three days a week) should not fool Canadians. When push comes to shove, if they hold the reins of fiscal and monetary policy, Canada will undoubtedly be heading back to an unforgiving and austere brand of neoliberalism -- and fast.

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