



DEFENCE AFTER THE RECESSION

Defence After the Recession

By

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EXECUTIVE SUMMARY

With unfortunate timing, the Harper government released a well-intended plan pledging “predictable, long-term funding”¹ for the Department of National Defence (DND), mere months before the collapse of Lehman Brothers signalled the onset of a global recession. The Canada First Defence Strategy (CFDS) built on the defence budgetary renaissance begun under Paul Martin’s tenure as Prime Minister and promised the Canadian Forces the resources to project leadership abroad over the next twenty years. Economic circumstances quickly intervened, however, and in 2011 the government launched a Strategic and Operating Review (SOR) to reign in government programs. As a result, defence spending has peaked in 2011/2012 and will decline for the next three years.

For DND, this fiscal retrenchment presents a significant problem. Although defence funding increased 54 percent nominally between 2003/2004 and 2010/2011, the CFDS was never adequately funded. While its capital investment plan was long rumored to be insufficient, the *Report on Transformation 2011*, led by Lieutenant General Andrew Leslie, acknowledged this openly.² As a result, DND faces a perfect fiscal storm as its already inadequate funding is battered by deficit fighting measures and the results of the departmental Strategic Review announced in Budget 2011, which both take effect April 1, 2012.³ This combination of factors means the CFDS is likely no longer viable, at least in its original twenty year timeframe. Although a lack of detail makes the full impact of Budgets 2011 and 2012 difficult to discern, enough information is available to provide a preliminary assessment of the probable impact on the Canadian military.

¹ Canada, *Canada First Defence Strategy* (Ottawa: Department of National Defence,[2008]).

² Lieutenant General Andrew Leslie, *Report on Transformation 2011* (Ottawa: Department of National Defence,[2011]).

³ There are other factors that will constrain defence spending, including a wage freeze, but for the sake of simplicity, their impacts are not adressed.

Budget 2012: The Strategic and Operating Review

Budget 2011 required DND (and other departments) to submit deficit reduction plans that would cut direct program spending by between 5 and 10 percent. The results of this process, announced in Budget 2012, will see DND's operating budget reduced by \$1.12 billion a year, or 7.4 percent, by 2014/2015. DND will make the largest departmental contribution to the deficit reduction plan in absolute terms, but its cutback is proportional to its share of overall spending. Despite the Harper government's vocal support for the military, defence received no favouritism in this round of fiscal restructuring.

However, certain components of the defence budget did receive special treatment. Both military personnel numbers and capital equipment purchases survived unscathed. As a result, the Canadian Forces will retain 68,000 regular forces and 27,000 reservists and "the Government will continue to replace key equipment"⁴ including naval vessels and the CF-18s, specifically. The capital program will proceed on an adjusted schedule, as the funding profile of \$3.54 billion worth of major capital equipment projects was re-profiled. It is impossible to determine whether this move is intended to help fight the deficit or simply to acknowledge major delays in the procurement process. Since 2006/2007, a cumulative \$2.9 billion in capital funding has already been re-profiled because DND was unable to spend the money allocated by Parliament on schedule. Either way, the move means the equipment will still be acquired, just more slowly. However, given the impact of inflationary pressures and potential requirement changes as technologies evolve, these procurements will take longer than planned and their existing underfunding will grow worse.

Although military personnel are protected from any cuts in the Budget, the document makes no mention of defence civil servants, suggesting some of these 28,558 positions will be eliminated as part of a government-wide civil service workforce reduction of 4.8 percent. Applied proportionally, this would see 1,400 positions eliminated at DND, fewer cuts than existing departmental plans to eliminate 2,000 jobs.⁵ Similarly, while the Budget retains 27,000 reservists, it does not specify how many will be full-time and how many part-time. As DND conducted a study of full-time reserve employment in 2011 with the intent of eliminating some of these positions, a conversion of some full-time reservists to part-time status is likely.

Budget 2012 focuses its defence reductions on "the efficiency and effectiveness of the organization,"⁶ although it provides few details of how these reductions will be apportioned. While a centralization of real property management targets infrastructure spending, the other initiatives concentrate on DND's operations and maintenance, or readiness, budget. Improving contracting practices and human resources management will presumably try to reduce spending through efficiency improvements. Streamlining the procurement of support equipment and spare parts, however, suggests that the department's National Procurement budget will be reduced as well. This item encapsulates the acquisition of spare parts, contracts for maintenance, repair and overhaul, technical support, and the ammunition used on training. In essence, it is the money used to produce equipment in an "operationally ready state."⁷ Reductions in this area are therefore consistent with the Budget's acknowledgment that with the end of the combat mission in Afghanistan, the CF will "transition to a lower pace of operations."⁸

Budget 2011: The Strategic Review

⁴ Canada, *Economic Action Plan 2012* (Ottawa: Department of Finance Canada,[2012]).

⁵ Canada, *Departmental Performance Report 2010-11* (Ottawa: Department of National Defence,[2011]); Canada, *Report on Plans and Priorities 2011-12* (Ottawa: Department of National Defence,[2011]).

⁶ Canada, *Economic Action Plan 2012*, 274.

⁷ Lieutenant-Colonel Michael Rostek, "Managing Change within DND," in *The Public Management of Defence in Canada*, ed. Craig Stone (Toronto: Breakout Education Network, 2009), 64.

⁸ Canada, *Economic Action Plan 2012*, 274.

Beyond Budget 2012, the simultaneous implementation of the Strategic Review will see another \$1 billion annual reduction by 2014/2015. Budget 2011 also provided scant details regarding how this will be achieved, beyond outlining savings of \$58 million by eliminating outdated equipment, \$10 million through rationalized procurement processes, and \$43 million by optimizing infrastructure. The Budget also mandated that the department save: \$321 million by increasing efficiency and effectiveness; \$313 million by focussing on core roles; and \$164 million by meeting the priorities of Canadians. Given the vague phrasing, it is impossible to know exactly where most of the required savings will be found.⁹

Table 1. ¹⁰	\$(millions)	2012-2013	2013-2014	2014-2015
Total Budget Base		20,000	20,000	20,000
Strategic Review (5% of total)		-525	-1,000	-1,000
Strategic and Operating Review (7.4% of the \$15B Operating Base)		-327	-706	-1,120
Total Cut		-852	-1,706	-2,120
Total Cut as % of Total Budget Base		-4%	-9%	-10.5%

The full impact of Budget 2011 and 2012 is displayed in Table 1. By 2014/2015 the required reduction will be \$2.1 billion, or 10.5 percent of the budget base. This cut will be significant because of its magnitude and the manner in which it appears the government intends to apply it. Budget 2012 exempts regular force military and capital equipment spending from the budget reductions. Furthermore, from public documents, we can estimate that civilian job losses will not greatly exceed 2,000 and, at most, 5,000 full-time reserve positions will be eliminated.¹¹ Overall, this would mean between \$1.5 and \$1.9 billion will need to be eliminated from the infrastructure, and operations and maintenance spending categories; a reduction that could exceed 20 percent of previous spending in these areas.

Furthermore, in reality, operations and maintenance will be impacted disproportionately relative to infrastructure. While DND owns 21,000 buildings, one for every five soldiers in uniform, little money is spent on infrastructure annually. DND devoted only \$660 million to

⁹ Another \$90 million is listed as “to be identified.” Canada, *Budget Plan 2011* (Ottawa: Department of Finance Canada, [2011]).

¹⁰ No total “base” reference level is provided in Budget 2012 and Department of Finance Canada officials in the budget lock-up would not provide one when asked. The SOR review base of \$15 billion does not include all capital funds, so does not, therefore, represent the department’s total base budget. The Strategic Review’s total base budget of \$20 billion is, therefore, used as a rough proxy for the base reference level. This is equivalent to total departmental spending in 2010/2011.

¹¹ The 2012/2013 Main Estimates are used to make these calculations. While different accounting practices do not allow for direct comparisons between the Budget and the Estimates, without other data sources, the Estimates are used to make indicative calculations. This recognizes that the 2012/2013 Estimates includes the first tranche of SR reductions, but uses the estimates for spending on personnel and equipment on the assumption that the SR’s impact on these areas is negligible, thus allowing for rough order of magnitude calculations. The Estimates allocates \$9.3 billion for military and civilian pay and benefits and \$2.9 billion for equipment acquisition, roughly \$12 billion. Data from the Report on Transformation 2011 (ROT), suggests eliminating 2,000 defence civilians would save the department approximately \$140 million (excluding possible compensation). Budget 2011 indicates a \$58 million reduction in outdated equipment. These two measures would see only \$200 million of the required \$2.1 billion cut taken from personnel and equipment spending, leaving \$1.9 billion to come from the remaining budget share. The ROT recommended eliminating up to 5,000 full-time reservists, at a savings of \$350 million annually. Taking this as a reasonable upper limit for reserve reductions, this would lower the remaining needed reduction from \$1.9 billion to \$1.55 billion. Thus, depending on the size of defence civilians and full-time reserve cuts, DND will need to find a further \$1.5 and \$1.9 billion in savings in the operations and maintenance and infrastructure budgets. This would see these combined categories, roughly \$8 billion, cut 19 to 24 percent.

this area in 2011/2012 and the CFDS allocated just eight percent of overall spending to infrastructure, so unless infrastructure cuts are severe, they will not realize large savings.¹² Base closures are always politically sensitive, making aggressive reductions unlikely. Furthermore, base closures can actually be costly in the short term, given the expenses associated with environmental remediation and work force adjustments. As a result, while many scholars advocate that DND rationalize its infrastructure holdings, and doing so may be prudent in the long term, it is unlikely that much will be saved by scaling back in this area over the next three years.¹³

Consequently, the bulk of these cuts will fall to the operations and maintenance, or readiness, budget, which provides the “resources needed to maintain equipment, conduct training, and prepare units for operations.”¹⁴ As a result, these budget reductions are unique in post-WWII Canadian history. Previously, when defence spending declined in real terms, military capabilities were reduced. Regular force personnel levels fell and so did the share of defence spending allocated to capital.¹⁵ The Harper government is breaking new ground by devolving a majority of its defence spending reduction to the operations and maintenance pillar.

In part, the government intends to achieve this by making DND more efficient and effective. The *Report on Transformation 2011* was launched with this goal in mind, receiving direction from the Prime Minister’s office to reduce military overhead.¹⁶ The Report suggested that roughly \$700 million in savings would be made possible by reforming enterprise resource planning, information technology and information management, reducing the use of contractor services and optimizing base support.¹⁷ In October 2011, DND officials stated that many of the Report’s recommendations would be implemented and that such efficiency reforms would be used to make sure “a dollar reduction in input does not necessarily result in a dollar reduction in output.”¹⁸ However, even if a full \$700 million in efficiencies can be found, this still leaves between \$800 million and \$1.2 billion of the needed \$1.5 and \$1.9 billion reduction to come from the only remaining source: readiness.

According to the Chief of the Defence Staff, readiness “is the degree of preparedness and responsiveness of our forces that allows me to deploy them with little notice in response to government direction. It’s the ability to get the right people, with the right skills and the right equipment, into the right place at the right time and to sustain that for as long as government requires.”¹⁹ In essence, by focusing a large portion of the budget reductions in this area, decision makers have opted to reduce the deployability of the military today in favour of preserving its capabilities for the future.

Significantly reducing this funding means the military will have 68,000 regulars and 27,000 reservists in uniform and billions of dollars of capital equipment, but a greatly reduced ability to conduct operations. Fuel budgets will get smaller, less ammunition will be ordered, and repairs will happen less frequently. This means planes will not fly as much, soldiers will train less regularly, and ships will spend less time at sea. As a result, when a future government

¹² Canada, *2012-13 Estimates* (Ottawa: Treasury Board of Canada Secretariat,[2012]).

¹³ Phillipe Lagassé and Paul Robinson, *Revising Realism in the Canadian Defence Debate* (Kingston, ON: Centre for International Relations, Queen’s University, [2008])

¹⁴ Canada, *Canada First Defence Strategy*, 18.

¹⁵ Craig Stone and Binyam Solomon, “Canadian Defence Policy and Spending,” *Defence and Peace Economics* 16, no. 3 (June, 2005): 145-169.; John M. Treddenick, “The Defence Budget,” in *Canada’s International Security Policy*, eds. David Dewitt and David Leyton-Brown (Scarborough: Prentice Hall Canada, Inc., [1995]), 413-454.

¹⁶ CDAI Roundtable, Fall 2011.

¹⁷ Leslie, *Report on Transformation 2011* The Report included a reduction in full-time reserve employment as an efficiency saving, but this was previously addressed.

¹⁸ Vice Admiral Bruce Donaldson, Mathew King and Kevin Lindsey, *Evidence* (Ottawa: The Standing Senate Committee on National Security and Defence,[2011]).

¹⁹ General Walter Natynczyk, *Evidence* (Ottawa: Standing Committee on National Defence,[2011]).

asks the Canadian Forces to deploy on an operation, it will have fewer high readiness troops prepared to do so than are available today.

The government will likely state that efficiency improvements will enable it to do more with less. As Bland argues, however, “in every case since 1962, every government's policy aimed at finding efficiencies to allow the Canadian Forces to do more with less has produced in fact military forces capable only of doing less with less.”²⁰ How long the forces will be less capable is the key question.

Opting to target operations and maintenance spending may indicate that the government intends to restore defence funding once its books are balanced. If so, the current plan makes sense, as it preserves personnel and equipment that would take much longer to regenerate than readiness. The longer it takes for funding to be restored, however, the less prudent this strategy will be. Preserving relatively large numbers of “hollow” forces lacking the requisite operations and maintenance funding to conduct operations will make little sense over the long term. At some point soon, therefore, balance will need to be restored between the personnel, equipment, infrastructure, and readiness pillars. In the meantime, the government needs to set a new “level of ambition”²¹ for the military that better reflects the funding assigned to it. In other words, it is time for a new Canada First Defence Strategy.

²⁰ Douglas Bland, *Evidence* (Ottawa: House of Commons Standing Committee on National Defence,[2012]).

²¹ Canada, *Canada First Defence Strategy*, 2.

ABOUT THE AUTHOR

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