MANITOBA BUDGET 2015

May 1, 2015

Return to surplus delayed until 2018/19

Manitoba Finance Minister Greg Dewar confirmed earlier reports yesterday that the government will fall short of balancing its books in 2016/17 with the latest fiscal plan indicating a balanced budget is not expected until 2018/19. The revision to the target date accompanied a cumulative decline in the budget projections including a whopping $204 million tacked on to the deficit in 2015/16. The government is now facing an estimated shortfall of $422 million in 2015/16 which represents significant deterioration from the $218 million projected in Budget 2014, primarily reflecting a poorer starting point due to last year's overall weak performance. The fiscal plan today adjusted the presentation of the fiscal outlook with projections now encompassing only core government operations. Now the plan shows a gradual improvement to the province's bottom line with deficits of $328 million in 2016/17 and $185 million in 2017/18 preceding a return to a slim surplus of $24 million in 2018/19.

In an attempt to tackle the persistent budget deficits, the government announced a series of tax measures aimed at boosting revenues in Budget 2015. The government is also continuing to rely on cost saving initiatives although the previous $150 million annual allocation for yet-to-be seen department savings and/or upward revenue surprises was reduced to $70 million in each year of the plan after falling well short of $150 million in 2014/15. (It is likely the case, however, based on the summary presentation of 2015/16, that the $80 million savings was derived from other reporting entities that are not included in the core presentation of the budget). To further buttress the path to surplus, the government will transfer $45 million from the Fiscal Stabilization Account to fund government operations over the next three years. In the absence of these adjustments and savings, the government would be at risk of failing to achieve its projected return to surplus in 2018/19.

Savings fall short in FY2014/15

Deterioration in the province's bottom line in 2015/16 was partly attributed to a weaker starting point. The deficit for the 2014/15 fiscal year is estimated to come in at $424 million, a $67 million increase from the initial Budget 2014 projection of $357 million. With higher-than-expected expenditures tempering an overall revenue improvement, the bulk of the revision reflects an underachievement for the government's in-year savings projection. The $150 million allotted annually to yet-to-be determined savings and/or revenue surprises fell short and is now projected to come in at $38 million. On a core operations basis (comparable to the outer-years of the plan), the deficit is higher, estimated at $451 million with only $17 million of the savings objective reached.

Modest improvement projected in FY2015/16

A modest improvement in the budget deficit in 2015/16 entirely reflects anticipated upside revenue surprises and/or yet-to-be determined fiscal savings ($70 million) as well as a lift from a transfer of funds from the Fiscal Stabilization Account ($20 million). Otherwise, the growth planned for total expenditures (2.5%) is expected to outpace that of revenues (2.3%) in 2015/16. This, despite the introduction of new tax initiatives that are projected to support a lift in total revenues to $12.4 billion in 2015/16. These include a 1pp increase to 6% in the Corporation Capital Tax and a 0.5 cent increase per unit in tobacco taxes, which

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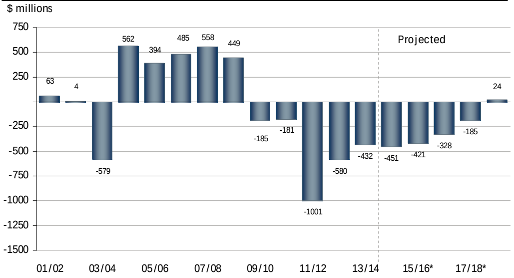

Source: Manitoba Ministry of Finance, RBC Economics Research
*Reflects core operation presentation; not directly comparable to previous years

Budget assumptions

	2014	2015	2016
Real GDP growth (%)			
Budget 2015 planning assumption	2.4	2.5	2.3
RBC	1.8	2.8	2.8
Nominal GDP growth (%)			
Budget 2015 planning assumption	3.9	3.8	4.6
RBC	3.3	4.1	5.5

Source: Manitoba Finance, RBC Economics Research

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are set to boost revenues by $26 million and $2 million, respectively, in the current fiscal year. Additional revenue support is slated to come from a 4.9% projected increase in taxation revenues more than offsetting a 0.8% dip in Federal Transfers.

On the expenditure side of the ledger, a 2.5% rise in program spending predominantly reflects planned expenditure increases in the two largest departments, health (up 4.3%) and education (up 3.1%). The extension of a number of existing tax credits further adds to the fiscal costs in 2015/16, the largest of which is an increase in the Seniors School Tax rebate (to increase expenditures by $15.1 million). Accompanying these measures were several initiatives smaller in scope aimed at alleviating poverty in the province. Higher debt charges (rising 2.3%) on account of a boost to the province's debt balances further contribute to the estimated increase in total expenditures, which are slated to rise 2.5% to $12.9 billion in 2015/16.

Medium-term plan: A return to surplus in 2018/19

Amidst weaker-than-expected fiscal results in 2014/15, the government is facing its seventh consecutive deficit in 2015/16. Despite a focus on 'building instead of cutting', the government is still projecting a return to surplus, albeit two years later than planned in Budget 2014. (Moreover, the deficit profile is likely lower than what would have otherwise been the case should the old framework been carried forward given the earlier projected deficits for other reporting entities that are no longer included). The revised path to balance that includes planned deficits of $328 million and $185 million in 2016/17 and 2017/18, respectively, reflects revenues growing at an annual average of 3.7%, exceeding the 2.4% average projected spending increases. Significant downside risks to the projections are evident should built-in cumulative savings of $280 million not be achieved, which essentially act as a reverse contingency fund; however, there is potential upside risk to the fiscal plan as well. A positive revenue surprise could materialize from stronger-than-expected economic growth. The government's forecasts for real GDP growth of 2.5% and 2.3% in 2015 and 2016, respectively, are, in our view, conservative relative to RBC's current forecast for a 2.8% advance in each of the years. Moreover, nominal GDP, the broadest indicator of the tax base, is forecast by the government to rise on average by 4.2% over the two-year period, which is a slower pace than RBC's forecast for an average 4.8% advance.

Capital spending

As part of the ongoing 5-year $5.5 billion core infrastructure plan announced in last year's budget, $1.08 billion in capital investment is planned for 2015/16, up from $1.035 in the previous fiscal year. To fund the infrastructure spending, distributed amongst roads, highways and bridges, flood protection and municipalities, $286 million will come from the one percentage point increase in the provincial sales tax (came into effect July 2013), $729 million from base funding and $35 million from federal cost-sharing. This will leave a gap of $30 million in 2015/16. Gaps over the projection period total $354 million and the government plan will be reviewed and adjusted each year to reflect variances in PST revenues and updated investment plans.

Net debt to rise

Higher capital spending is contributing to a projected increase in the province's net debt, which is set to jump by $1.7 billion to $20.4 billion by March 31, 2016. Part of this increase ($502 million) is attributed to an accounting change with the Manitoba Hydro-Electric Board adopting International Financial Reporting Standards in the current fiscal year. The increase in net debt is expected to outpace growth in nominal output, leaving the net debt-to-GDP ratio set to rise to 30.9% in 2015/16 from 29.5% in 2014/15.

Financing requirements:

Total borrowing requirements are expected to be $4.7 billion with $2.0 billion needed for refinancing in 2015/16.

Fiscal Stabilization Account

The province's Fiscal Stabilization Account is meant to cover core government operating shortfalls and as a result, withdrawals from the account will continue in 2015/16 with a planned $105 million payment. Of this, $85 million will be used to retire a portion of provincial borrowings with the remainder set to be directed towards funding core operations. This builds upon disbursements of $55 million in 2014/15 and $100 million in 2013/14 to leave the remaining account balance at $115 million at the end of the 2015/16 fiscal year.

Manitoba's fiscal plan

$ millions	Forecast	Budget	Projection		
	2014-15	2015-16	2016-17	2017-18	2018-19
Revenue	12,078	12,354	12,768	13,231	13,770
Expense	12,546	12,865	13,181	13,496	13,816
In-year adjustments/lapse	(17)	(70)	(70)	(70)	(70)
Fiscal Stabilization Account Draw	-	(20)	(15)	(10)	-
Surplus/ (deficit)	(451)	(421)	(328)	(185)	24