

THE 2013 ONTARIO ECONOMIC AND FISCAL REVIEW

November 7, 2013

Budget projections remain on track

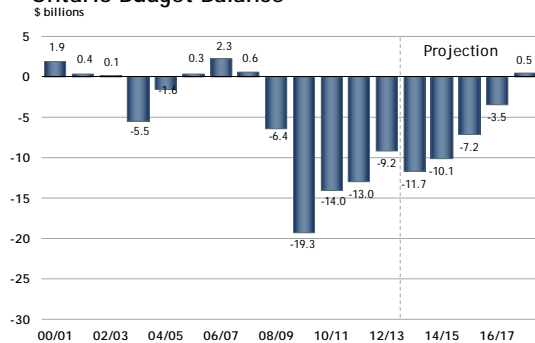
Ontario Finance Minister Charles Sousa today delivered his mid-year update on the provincial budget situation which showed that his government remains on track to post a \$11.7 billion deficit this fiscal year (2013-14), as projected in the May budget. The updated projections for revenues and expenses for 2013-14 are virtually unchanged from budget, at \$116.8 billion and \$127.6 billion, respectively. There were modest variations in some of the components of revenues and expenses but these were almost fully offsetting.

Because this mid-year review exercise strictly focuses on developments in the current fiscal year, projections for the remainder of the fiscal plan were unchanged. The government's target, therefore, remains to balance the books by 2017-18, and the path to get there outlined in the May budget is still the same. The government indicated, however, that if economic conditions were to be significantly weaker than expected, it would err in favour of supporting economic growth, rather than sticking with "short-term targets".

On the surface, this budget update is largely a steady-as-she-goes story. It must be noted, however, that it comes on the heels of better-than-expected audited results in 2012-13 as the final tally of the provincial deficit (released in September) came in at \$9.2 billion, or \$600 million lower than estimated this past May and fully \$5.6 billion below the projection in the 2012 budget. This 'beating target' was in keeping with the government's tendency to 'over-deliver' on deficit goals over the past four years.

The lower deficit last year was achieved in large part through spending restraint. In fact, program spending fell (by 0.3%) for the first time since 1998-99. This is testament to the serious efforts to redress the fiscal situation of the province taken by the government. Those efforts more than compensated for weaker-than-estimated revenue growth in 2012-13. That being said, the savings generated by the spending restraint last year set a favourable starting point in realigning expenditures with revenues this year. By maintaining the projected expenditures for 2013-14 at the Budget 2013 levels in this budget update, the government effectively raises this year's forecasted growth in program expenditures from 3.0% to 4.2%. This does not jeopardize the \$11.7 billion deficit projection given that stronger growth also occurs on the revenue side; however, the government misses an opportunity to 'bank' those savings and work from a lower expenditure path going forward. Had the government stuck to the revenue and expense growth rates for 2013-14 that it projected in the 2013 budget, it would have been able to show a slightly lower deficit of \$11.2 billion this year, relative to a retained target of \$11.7 billion. While this may not look like a significant reduction, the point is that it would have signaled an unwavering commitment not to let opportunities go by on the road to balancing the books. As we have indicated in past budget commentaries, the task of taming expenditures will not get any easier in the years ahead.

Ontario Budget Balance



Source: Ontario Ministry of Finance, RBC Economics Research

Laura Cooper
Economist
(416) 974-8593
laura.cooper@rbc.co

Robert Hogue
Senior Economist
(416) 974-6192
robert.hogue@rbc.com

The point on maintaining focus on spending growth is unlikely to be lost on debt rating agencies. For instance, Standard and Poor's put the province on negative outlook since April 2012 because, among other things, of concerns about the ability to maintain aggressive cost containment targets. Letting program expenditures grow faster this year may be interpreted as slippage in the government's cost containment efforts.

At least, rating agencies will take comfort in the government's continued stated commitment to hold the line on public sector compensation, as reiterated in today's mid-year review. Additionally, rating agencies will see last year's lower-than-expected deficit and its effect on the province's debt positively. The lower deficit helped to reduce net debt by \$700 million to \$272.1 billion, and the net-to-GDP ratio marginally by 0.1% to 37.4% at March 31, 2013, relative to the estimates in Budget 2013 in May.

The documents stated that the government continues to expect long-term borrowing requirements of \$33.4 billion in 2013-14, and that \$21.9 billion (or 65%) of which was completed by October 23, 2013.

The Ministry of Finance today also updated its economic forecasts, which were downwardly revised slightly with real GDP growth now projected at 1.3% in 2013 and 2.1% in 2014 (compared to 1.5% and 2.3%, respectively, in the May budget). These revisions – reflecting similar changes to private sector forecasts made since budget – were too small to affect revenue and spending assumptions materially. The Ministry's forecasts continue to be more conservative than those of the private sector, representing an element of prudence embedded in the budget projections. The other main element of prudence — the \$1 billion reserve — was also maintained.

The 2013 Ontario Economic and Fiscal Review document was also the vehicle for a number of policy intentions and initiatives, most of which had already been announced in recent weeks and months. Among them were proposals to:

- issue so-called 'green bonds' to raise capital to fund "projects with specific environmental benefits";
- introduce of a new trust fund (the Trillium Trust) to be financed by the proceeds of government asset sales and aimed at supporting infrastructure spending;
- establish a Financial Accountability Officer (a provincial equivalent to the Parliamentary Budget Office at the federal level) to keep the Ontario legislature abreast of fiscal developments;
- exempt pension plans from the rule prohibiting them from owning more than 30% of voting shares for certain Ontario public infrastructure projects;
- introduce a 10-year infrastructure plan; and
- change the dividend tax credits to address fairness issues across income levels.

Some of these proposals will require new legislation and, therefore, will be debated in the coming months.

Ontario's fiscal plan

(\$ billions)	Actual	May	November	Projected Outlook (May Budget)			
		Budget	Update	2014/15	2015/16	2016/17	2017/18
	2012/13	2013/14	2013/14				
Total revenues	113.4	116.8	116.8	120.5	124.9	130.1	134.4
Total expenditures	122.6	127.6	127.6	129.5	131.0	132.1	132.4
Program spending	112.3	117.0	117.0	118.3	118.8	118.8	118.0
Interest on public debt	10.3	10.6	10.6	11.1	12.2	13.4	14.5
Reserve	-	1.0	1.0	1.2	1.2	1.5	1.5
Surplus/(Deficit)	(9.2)	(11.7)	(11.7)	(10.1)	(7.2)	(3.5)	0.5

Source: Ontario Ministry of Finance, RBC Economics Research

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