BUDGET ANALYSIS

# Ontario: Budget 2024

## Spending Pressures Delay Plans to Balance by One More Year

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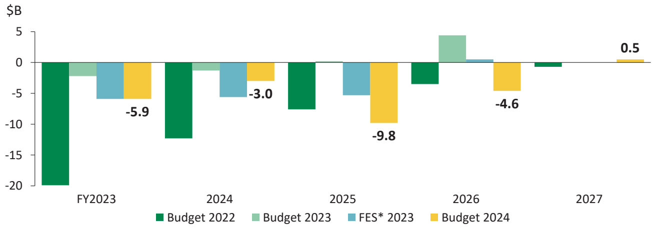
### HIGHLIGHTS

- The province of Ontario's fiscal year 2024–25 (FY2025) forecasts a return to budget surplus in FY2027—one year later than anticipated in the 2023 Fall Economic Statement (FES) (graph 1). Table 1 on page 2 summarizes updated economic and financial projections.
- Higher spending projections—largely attributable to public sector wage increases following the repeal of Bill 124—were responsible for much of the deterioration in the bottom line. The federal government's announcement that it will cap international student permit applications for two years also played a role. The extension of gas and fuel tax cuts headlined new policy.

**Graph 1**
**Return to Balance Delayed Again**
Budget balance projections




* *Fall Economic Statement*
Ontario Ministry of Finance and Desjardins Economic Studies

- Borrowing requirements are now expected to total $38.2B in FY2025, $37.7B in FY2026, and $32.8B in FY2027. The projections for the first two years represent a combined rise of just $1.6B versus FES forecasts, as pre-borrowing activity and more short-term financing are expected to partially offset the effects of larger deficits.
- Risks to the plan include weaker-than-anticipated headcount gains following Ottawa's move to reduce the temporary resident population and further tax base adjustments. Fortunately, Budget 2024 also (characteristically) includes multiple layers of prudence.
- Budget 2024 shows a deterioration in Ontario's financial position, but that deterioration likely would have been worse absent prudent choices in prior plans. Nonetheless, the road ahead will be challenging as the province seeks to balance expenditure control and debt sustainability with the needs of a fast-growing and rapidly aging population.

### Main Takeaways

There's no denying that Budget 2024 shows a deterioration in the province of Ontario's financial position (as we've seen in other provinces this spring). The timeline to balance was once again delayed by one year, and deficit forecasts were increased by nearly $10B combined for the FY2025 to FY2026 period relative to the 2023 FES. Ontario's debt trajectory was also increased versus the previous forecast. As expected, this comes amid modest downgrades to the economic outlook since November 2023 and costly public sector wage increases that the government had signalled were on the table. The [financial hit from reduced international student admissions](), which Desjardins Economics identified as a risk last year, also contributed.

But the fiscal deterioration was arguably not as significant as it could have been, and that's in part because of decisions made in prior plans. Relative to many other provinces, Ontario kept its



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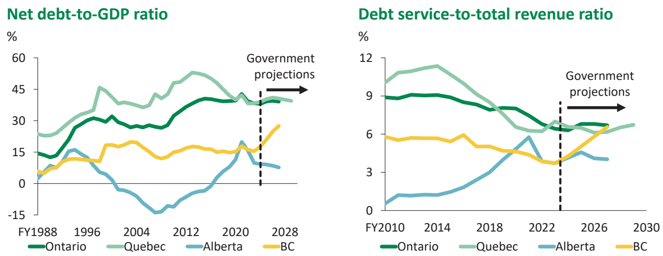
spending in check during the pandemic. That allowed it to push its key debt metrics lower before the pandemic, and it's now poised to avoid hitting record highs in the years ahead (graph 2). Beefing up the contingencies last fall—an approach taken by some but not all other provinces—also helped Ontario absorb a significant chunk of the compensation costs.

Restraining spending growth is still key to returning to the black. Although spending projections were increased relative to forecasts laid out in the FES, the province continues to assume that it will keep advances in program expenditures below the rate of population growth plus inflation (graph 3). That is challenging for any government, let alone one grappling with decades-high population growth and a housing affordability crisis. Keep in mind as well that population aging will only put further upward pressure on healthcare spending in the years ahead.

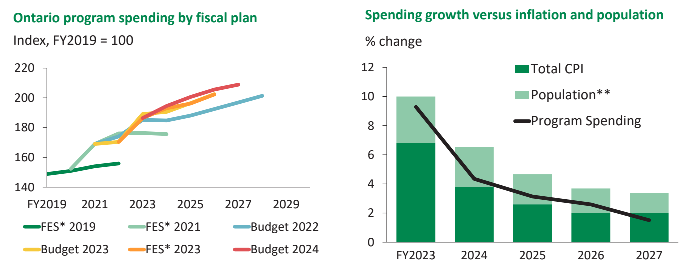
Weaker-than-anticipated population growth would presumably ease the spending pressures described above, but also presents downside potential to the economy and government revenues. Just a few months ago, we might have talked about how skyrocketing non-permanent resident landings meant that risk was tilted to the upside on demographic gains. Not so for Budget 2024 projections, which were completed before Ottawa's announcement that it would take steps to reduce the national temporary resident by 20% over the next three years. Ontario's last set of demographic projections still guide the forecasts published today, and they assumed that temporary migration

### Graph 2
**Ontario's Debt Metrics Are Set to Remain Below Record Highs**




Provincial budget documents and Desjardins Economic Studies

### Graph 3
**Spending Plans Increased, But Remain Restrained**




* *Fall Economic Statement*. ** Outer-year population growth numbers based on 2023 Ontario demographic projections
Statistics Canada, Ontario Ministry of Finance and Desjardins Economic Studies

### TABLE 1
**Updated Ontario Fiscal and Economic Forecasts**

| IN $B (UNLESS OTHERWISE INDICATED) | 2023–24 | | 2024–25 | | 2025–26 | | 2026–27 |
|---|---|---|---|---|---|---|---|
| | **FES* 2023** | **Bud. 2024** | **FES* 2023** | **Bud. 2024** | **FES* 2023** | **Bud. 2024** | **Bud. 2024** |
| Total Revenues | 201.8 | 204.34 | 206.7 | 205.7 | 220.0 | 217.4 | 226.6 |
| *% change* | *4.6* | *5.9* | *2.4* | *0.7* | *6.4* | *5.7* | *4.2* |
| Own-Source Revenues | 166.7 | 169.6 | 171.3 | 169.4 | 183.0 | 179.9 | 187.9 |
| *% change* | *3.2* | *4.9* | *2.8* | *-0.1* | *6.8* | *6.2* | *4.4* |
| Federal Transfers | 35.1 | 34.8 | 35.4 | 36.3 | 37.0 | 37.5 | 38.7 |
| Total Spending | 206.4 | 207.3 | 210.5 | 214.5 | 217.5 | 220.6 | 224.1 |
| *% change* | *3.8* | *4.3* | *2.0* | *3.5* | *3.3* | *2.8* | *1.6* |
| Program Spending** | 193 | 194.5 | 196.2 | 200.6 | 202.3 | 205.9 | 208.9 |
| *% change* | *3.5* | *4.3* | *1.7* | *3.1* | *3.1* | *2.6* | *1.5* |
| Debt Servicing | 13.4 | 12.8 | 14.3 | 13.9 | 15.2 | 14.7 | 15.2 |
| *% of revenues* | *6.6* | *6.3* | *6.9* | *6.8* | *6.9* | *6.8* | *6.7* |
| Reserve | 1.0 | 0.0 | 1.5 | 1.00 | 2.0 | 1.5 | 2.0 |
| **Budget Balance** | **-5.6** | **-3.0** | **-5.3** | **-9.8** | **0.5** | **-4.6** | **0.5** |
| *% of GDP* | *-0.5* | *-0.3* | *-0.5* | *-0.9* | *0.04* | *-0.4* | *0.0* |
| *Net Debt (% of GDP)* | *38.4* | *38.0* | *39.1* | *39.2* | *38.7* | *39.5* | *39.1* |
| *Nominal GDP (% change)* | *3.6* | *4.1* | *2.9* | *2.7* | *4.2* | *3.9* | *4.3* |
| *Real GDP (% change)* | *1.1* | *1.2* | *0.5* | *0.3* | *2.0* | *1.9* | *2.2* |
| Infrastructure Spending | 20.7 | 20.9 | 26.0 | 26.2 | 27.1 | 29.5 | 26.7 |

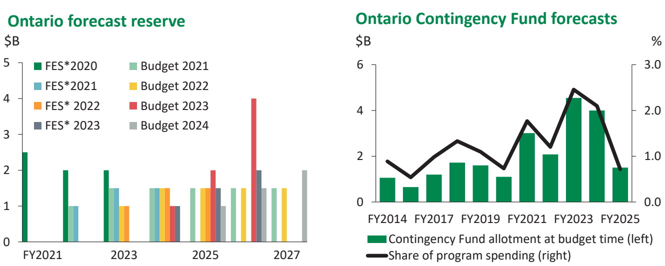
* *Fall Economic Statement*

** Includes COVID-19 funding and one-time expenses

Ontario Ministry of Finance and Desjardins Economic Studies would contribute nearly 500k people (over 40%) to population growth from July 1, 2023, to July 1, 2026. We also highlighted here and here that there's an outsized risk to Ontario's economy from a reduction in temporary worker inflows, which builds on the potential financial hit to the province from lower international student admissions.

The better news is that some prudence remains in Budget 2024, and that provides some wiggle room. Characteristically, that prudence is threefold. First, Ontario budgets are based on economic projections that are slightly weaker than the private sector average. Second, forecast reserves, at $4.5B over the next three fiscal years, are available to cover unexpected shortfalls. Finally, the Operating and Capital Contingency Funds—booked as expenses—total $1.5B in FY2025. That said, it's a small allocation relative to recent plans in dollar terms and as a share of spending projections (graph 4).

**Graph 4**
**Budget 2024 Still Contains Some Contingencies**

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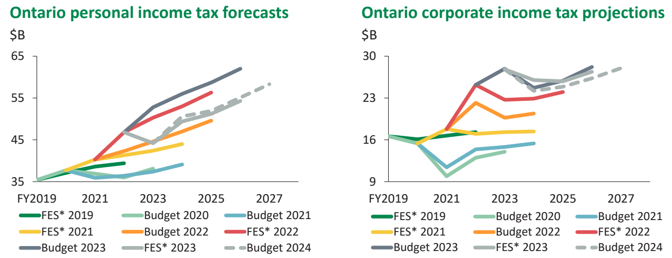
The bottom line: Ontario's 2024 budget shows a fiscal deterioration similar to what we've seen in other provinces, but cautious planning in prior fiscal blueprints has helped it avoid worse outcomes. Still, the road ahead may not be easy as the government grapples with a still-high debt burden, potentially higher-for-longer interest rates, and myriad implications surrounding population growth.

## Revenue and Expenditure Details

Budget 2024 included downward revisions to revenue expectations and boosts to spending projections. Relative to last year's FES, forecasts for government own-source receipts were reduced by a combined $5B from FY2025 to FY2026. Program expenditure projections were increased by about $8B over the same two-year period.

Federal tax assessments—which we discussed in our Budget 2024 preview and helped accelerate the timeline to balance in last year's fiscal plan—once again impacted the fiscal outlook. Following a big upward revision in Ontario's third quarter fiscal update for FY2024, personal income tax forecasts were lowered by $1.3B for the fiscal year ending March 31st. By contrast, corporate income tax expectations were increased by $2.4B following a big reduction at Q3. Net of the Q3 FY2024 and Budget 2024 revisions, personal income taxes are now on track to roughly hit the FES projections in the outer years of the plan. The trajectory for corporate income taxes is weaker relative to the prior target (graph 5), though less so than we would have anticipated following the third quarter forecast revision. Meanwhile, the government now expects sales tax revenues to fall in FY2025 following a Q3 upward adjustment to FY2024 projections.

**Graph 5**
**Further Base Adjustments Bring Tax Revenues Closer to November 2023 Projections**

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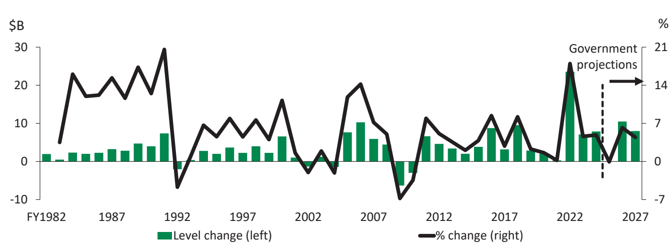
The risk of further revisions remains. This is what occurred in last year's Public Accounts, which noted that final 2023 corporate and personal tax assessments wouldn't be finalized until December of this year.

Against that backdrop, revenues continue to rely on strong growth in the final two years of the plan. The combined $18.5B gain in own-source receipts penciled in for the FY2026 to FY2027 period would be—in dollar terms—the largest two-year increase recorded outside the pandemic recovery period (graph 6). At 11%, the two-year increase is less of an outlier in growth rate terms, but the forecast of two successive annual

**Graph 6**
**Ontario's Fiscal Plan Still Relies on Solid and Persistent Outer-Year Revenue Growth**




Finance Canada, Ontario Ministry of Finance and Desjardins Economic Studies gains exceeding 4% isn't something we've tended to see outside of post-recessionary periods. Near-term economic forecasts were revised lower, but (a still-positive) 0.3% real GDP growth anticipated in calendar year 2024 suggests a slowdown rather than a moderate-to-deep downturn.

For spending, the bulk of the increase versus the FES appeared to stem from public sector wage increases implemented following the repeal of Bill 124. The bill would have restrained salary boosts in the health and education sectors. The government attributed FY2024 upward revisions of $1.6B and $1.8B to expenses in the health and education sectors, respectively, to compensation costs. The province expects the post-secondary education spending to come in below FES projections because of the federal government's announcement that it will cap international student permit applications for two years. That said, it also lowered the "other non-tax revenue" stream by $1–1.5B per year versus FES projections in response to this effect.

The extension of gas and fuel tax cuts—about which we have mixed feelings—headlined new policy. We argued in 2022 that the potential savings would accrue primarily to higher-income households at a time when policy should target the lowest-income individuals most impacted by inflation. And the risk of re-stimulating inflation remains, though it's diminished relative to last year. This extension is also more costly than prior ones, estimated to result in foregone revenues of $620M in FY2025. That said, commodity price volatility is a source of reduced affordability and increased anxiety for many Ontarians and this measure should help to alleviate that. The province will also review the property assessment and taxation systems beginning this year. It remains focused on workforce skills development, supporting the skilled trades, and keeping electricity costs low.

Infrastructure spending plans were largely unchanged from the prior plan. The most meaningful difference—a $2B increase versus the FES—is expected to come in FY2026. Health and transit remain the principal focus of the government's ambitions on this front.

## Borrowing and Financial Market Developments

Total long-term borrowing is now expected to reach $41.8B in FY2024, $38.2B in FY2025, $37.7B in FY2026, and $32.8B in FY2027. The FY2025 and FY2026 projections represent a combined $1.6B rise versus FES forecasts. Increases to finding requirements are almost entirely a result of larger projected deficits. However, pre-borrowing activity conducted earlier this year—which was booked as a boost to fiscal year-end cash levels—will mitigate the higher funding requirements in outer years. The province will also increase short-term borrowing in FY2025 to take advantage of investor demand for Ontario debt. Table 2 updates borrowing program projections. Almost 90% of the borrowing completed in FY2024 has been in Canadian dollars, via 36 syndicated issues, one floating note and two Green Bonds. The target range for domestic borrowing remains 75 to 90% for FY2025. The weighted average borrowing term for outstanding debt in FY2024 was estimated at 15.2 years, long enough to help mitigate risks related to refinancing at higher interest rates. Ontario once again committed to "monitor the market and adjust the debt term strategy in the future, if necessary, in response to further changes to interest rates and the yield curve."

**TABLE 2**
**Updated Ontario Borrowing Program**

| | 2023–24 | | 2024–25 | | 2025–26 | | 2026–27 |
|---|---|---|---|---|---|---|---|
| IN $B (UNLESS OTHERWISE INDICATED) | FES* 2023 | Bud. 2024 | FES* 2023 | Bud. 2024 | FES* 2023 | Bud. 2024 | Bud. 2024 |
| Deficit/(Surplus) | 5.6 | 3.0 | 5.3 | 9.8 | (0.5) | 4.6 | -0.5 |
| Investment in Capital Assets | 13.6 | 14.7 | 18.7 | 17.7 | 19.0 | 20.2 | 20.4 |
| Non-Cash and Cash Timing Adjustments | (1.3) | (1.6) | (11.2) | (11.0) | (12.0) | (12.0) | -13.9 |
| Net Loans and Investments | 0.2 | (0.2) | (0.9) | (0.3) | (0.1) | 0.1 | — |
| Debt Maturities/Redemptions | 31.2 | 31.2 | 28.0 | 28.0 | 33.1 | 33.1 | 26.9 |
| Total Funding Requirement | 49.2 | 47.1 | 39.8 | 44.2 | 39.4 | 46.0 | 32.8 |
| Decrease/(Increase) in Short-Term Borrowing | — | | (2.5) | (5.0) | (2.5) | — | — |
| Increase/(Decrease) in Cash and Cash Equivalents | — | 9.3 | — | (1.0) | — | (8.3) | — |
| Pre-borrowing for 2023–24 | (14.5) | (14.5) | — | — | — | — | — |
| **Total Long-Term Borrowing** | **34.7** | **41.8** | **37.3** | **38.2** | **36.9** | **37.7** | **32.8** |

* *Fall Economic Statement*

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The Budget's release close to the end of the trading day precludes a deeper analysis, but Ontario bond spreads did not move meaningfully versus those of other Canadian governments immediately after the plan was tabled. That suggests investors had—to some extent—anticipated the deterioration in fiscal balances following a spike in pre-financing and early signs that wage increases would come with a meaningful price tag. Going forward, overall risk sentiment should be the primary driver of spreads in Canada's largest province—and indeed those of other governments given Ontario's role as the provincial benchmark.