Budget Analysis
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ONTARIO: 2016 BUDGET

A balanced budget is within arm's reach

HIGHLIGHTS

- The return to a balanced budget is still planned for 2017–2018.
- Program spending growth will be slightly higher than previously expected.
- The province's debt will continue to climb, in particular to fund the major infrastructure program.
- A significant reduction in tuition fees for children from families with income below $83,000.
- Ontario is continuing its efforts to introduce a cap-and-trade program for greenhouse gas emissions.
- Introduction of a surtax on tobacco, increases in some other taxes and insurance deductibles, and elimination of the tax credit for children's activities.

Table 1
Summary statement of transactions

	Actual	*Projections*			
In $B	**2014–2015**	**2015–2016**	**2016–2017**	**2017–2018**	**2018–2019**
Total revenues	**118.5**	**126.5**	**130.6**	**137.7**	**141.9**
- Variation (%)	2.2	6.8	3.2	5.4	3.1
Program spending	**-118.2**	**-120.9**	**-122.1**	**-124.2**	**-127.6**
- Variation (%)	2.1	2.3	1.0	1.7	2.7
Debt charges	**-10.6**	**-11.2**	**-11.8**	**-12.5**	**-13.1**
- Variation (%)	0.0	5.7	5.4	5.9	4.8
Debt charges	**-128.9**	**-132.1**	**-133.9**	**-136.6**	**-140.7**
- Variation (%)	2.0	2.5	1.4	2.0	3.0
Reserve	---	-0.2	-1.0	-1.1	-1.2
Budgetary balance	**-10.3**	**-5.7**	**-4.3**	**0.0**	**0.0**
Net debt	**284.6**	**296.1**	**308.3**	**316.9**	**326.8**
- In % of GDP	38.4	39.4	39.8	39.8	39.2

Sources: Ontario Ministry of Finances and Desjardins, Economic Studies

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THE RETURN TO A BALANCED BUDGET IS STILL PLANNED FOR 2017–2018

Ontario's budget forecasts have raised many doubts in recent years and a return to a balanced budget has often been considered doubtful. However, we must recognize that the Ontario government is not only still on course with the 2016 budget that it tabled today, but that the budget numbers are a little better than was initially expected. For example, the budget deficit for the fiscal year ending March 31 of this year will be only $5.7B, which is $2.8B less than what was predicted in last year's budget. For the fiscal year ending March 31, 2017, the deficit could turn out to be just $4.3B, i.e. $500M less than the budget projections of 2015. Thus, the return to a balanced budget is still planned for the 2017–2018 fiscal year. We would point out that the Ontario government's budget forecasts still include a contingency fund amounting to nearly $1B for future fiscal years, giving the government some financial leeway.

We would also mention that the scope of the deficits expected for future fiscal years could have been reduced further, if the Ontario government had held onto the very weak growth target that it had set for its program spending last year. But with a balanced budget now within arm's reach, the Ontario government decided to accelerate its program spending a little. While a cumulative cut of 0.4% was planned last year for the 2016–2017 and 2017–2018 fiscal years, the latest projections show a cumulative increase of 2.7%. This represents an average annual increase of 1.4% for the next two fiscal years—this is still quite low from a historical perspective. Among other things, this will make it possible to increase hospital funding for the first time in five years.

Despite the gradual return to a balanced budget, Ontario's net debt will keep expanding in future fiscal years. It could reach $326.8B as at March 31, 2019, mainly to fund the province's major infrastructure program. That said, debt growth should eventually reach a pace below nominal GDP growth, so that the debt-to-GDP ratio should not exceed the 40% mark. By comparison, Quebec's net debt-to-GDP ratio is expected to reach 49.9% as at March 31, 2016.

SEVERAL NEW MEASURES HAVE BEEN PROPOSED

The increase in program spending in future fiscal years will enable the Ontario government to introduce several new measures. That said, the total cost of most of these new measures is fairly limited, and is partly offset by some increases in tax revenues, such as the introduction of a $3 surtax per carton of 200 cigarettes, an increase in the price of, and taxes on, wine, an increase in the prescription drug insurance deductible for the majority of seniors, and the elimination of the tax credit for children's activities. Here is a summary of the main measures proposed in the 2016 budget:

- Almost free tuition for postsecondary students from families with income below $50,000. A little over half of all students from families with income of up to $83,000 will also benefit from substantial financial aid.
- In its 2016 budget, the Ontario government also revealed more details about the climate change strategy that it announced last November, in particular with a cap-and-trade system for greenhouse gas emissions. This system could result in a price increase of around ¢4.3 per litre of gasoline.
- Ontario will also continue its vast infrastructure program. Between now and March 31, 2025, over $137B should be invested. This should enable Ontario to take full advantage of the infrastructure program that will be unveiled as part of the federal government's upcoming budget.
- The 2016 budget also reiterates the Ontario government's intention to enhance the Canada Pension Plan (CPP) and to adopt the Ontario Retirement Pension Plan (ORPP). By 2020, all eligible Ontario workers would be covered by the ORPP or by a comparable plan from their employer. A bill to that end should be introduced next spring.

The Ontario economy faces fewer challenges

Even if Ontario's real GDP growth were to slow a little in 2016 and 2017, Ontario will still maintain growth above the national average. Furthermore, the manufacturing industry is enjoying favourable conditions, with the depreciation of the Canadian dollar and growing demand from the United States.

The effects of low energy prices are also far less pronounced on Ontario's GDP deflator. The province's nominal GDP could grow by 4.0% in 2016 after an estimated gain of 3.6% in 2015. By comparison, the nominal GDP of Canada as a whole probably rose by a mere 0.7% in 2015, and an increase of just 2.1% is expected for 2016. This gap should, among other things, produce higher tax revenue growth in Ontario than in most of the other provinces.

Table 2
Economic and financial forecasts

	2015		2016f		2017f	
Variation in %	2015 Budget	2016 Budget	2015 Budget	2016 Budget	2015 Budget	2016 Budget
Real GDP	2.7	2.5	2.4	2.2	2.2	2.4
Nominal GDP	4.2	3.6	4.2	4.0	4.2	4.6
Employment	1.1	0.7	1.3	1.1	1.4	1.2
U.S. real GDP	3.1	2.4	2.9	2.1	2.7	2.4
Canadian dollar (US¢)	79.5	78.2	80.0	72.0	85.0	75.5
Treasury bills – 3-month	0.6	0.5	1.1	0.5	2.5	0.8
Federal bonds – 10-year	1.8	1.5	2.7	1.6	3.8	2.3

f: forecasts
Source: Ontario Ministry of Finances

THERE IS NO GUARANTEE

While the Ontario government appears to be in a good position to achieve its goal of returning to a balanced budget, many uncertainties remain. For one thing, global economic conditions are still fragile, and Ontario's economic growth may turn out to be below expectations. In fact, the province's economic forecasts have been downgraded somewhat since last year's budget. For another, the faster-than-expected improvement in the province's public finances was possible in part thanks to higher-than-expected revenues stemming from the partial sale of Hydro One and to larger tax revenues derived from new home sales. Obviously, future fiscal years will not be able to benefit from those one-time contributions. That said, the existence of a contingency fund is reassuring. It should enable the Ontario government to cope with possible difficulties without compromising its return to a balanced budget.