



April 30, 2015

### **BALANCED BUDGET TARGET PUSHED BACK**

#### **Highlights**

- The Manitoba government has estimated a budget deficit of \$424 million (0.7% of GDP) in fiscal 2014-15, \$67 million lower than projected in its 2014 budget.
- The balanced budget target has been pushed back to fiscal 2018-19. The budget shortfall is forecast to remain essentially unchanged in fiscal 2015-16 (-\$422 million or 0.6% of GDP). In its medium term core fiscal plan, revenues (+3.7%) are expected to outpace expenditures (+2.4%) over the final three years of the forecast until the Province is back in the black.
- The government's net debt to GDP ratio is projected to move higher in the upcoming year, to an estimated 30.9%. The recent upward trajectory of the Province's debt burden partially reflects borrowing tied to the government's \$5.5 billion capital plan introduced in Budget 2014. The government highlighted its commitment to its 5-year infrastructure plan, with \$1.1 billion in capital outlays slated for fiscal 2015-16.
- The budget contained a slew of new initiatives that were generally modest in nature. The corporation capital tax on banks, trust corporations and loan corporations has been increased from 5% to 6%. The tobacco tax has also been raised by half a cent per cigarette. The minimum wage will be increased to \$11.00 per hour effective October 2015.

The government has pushed back the budget balance target to fiscal 2018-19, marking the second time a delay in the deficit elimination timetable has been announced within the past two years. While stronger economic growth over the next few years will support government coffers, core revenue gains (+3.3% annually) are projected to only modestly surpass those of spending (+2.4% annually), translating into a more extended path to balance. In the meantime, the combination of an ongoing budget shortfall and borrowing associated with the \$5.5 billion infrastructure plan will continue to put upward pressure on the debt burden.

The deficit for fiscal 2014-15 is estimated at \$424 million (0.7% of GDP), overshooting 2014 Budget expectations by \$67 million. While revenues came in ahead of expectations; higher spending in the health, community, economic resource development and justice sectors more than offset this windfall. What's more, the Q3 report highlighted that heavy summer rains and flooding led to a surge in disaster relief funding.

#### **Improved economic outlook to grow budget to balance**

The government estimates real GDP growth at 2.4% in 2014. This is significantly stronger than the preliminary estimate of 1.1% released by Statistics Canada earlier this week. Indeed, the Manitoba Bureau of Statistics is challenging the Statistics Canada estimate, citing differences in methodology as the reason for the differing estimates. Statistics Canada will release revised estimates in November. For the purposes of the fiscal plan, the 2014 GDP reading does have implications for measuring the debt/deficit burden as a share of the size of the economy. If a downward adjustment to the GDP estimate is ultimately

**TABLE 1: MANITOBA GOVERNMENT FISCAL POSITION**

[ C\$ millions, unless otherwise indicated ]

Fiscal Year	Actual				Est.	Forecast
	10-11	11-12	12-13	13-14*	14-15	15-16
<b>Revenues</b>	13,069	13,688	13,614	14,214	14,784	14,963
% change	3.3	4.7	-0.5	4.4	4.0	1.2
<b>Expenditures</b>	13,250	14,689	14,174	14,736	15,246	15,535
% change	3.1	10.9	-3.5	4.0	3.5	1.9
<b>In-Year Adjustments/Lapse*</b>	-	-	-	-	-38	-150
<b>Summary Net Income</b>	-181	-1,001	-560	-522	-424	-422
% of GDP	-0.3	-1.8	-1.0	-0.9	-0.7	-0.6
<b>Summary Net Debt</b>	12,562	14,550	15,893	17,344	18,775	20,426
% of GDP	23.7	26.1	27.0	28.3	29.5	30.9

\* Increase in revenue and/or decrease in expenditures.

Source: Manitoba Finance, Budget 2015.

required, it would (all things equal) raise these key fiscal metrics relative to what is shown in today's budget.

Looking ahead, the government projects real GDP in Manitoba to average growth of 2.4% over the 2015-16 period – outperforming the national average. Manufacturing activity is assumed to accelerate over the forecast period, reflecting a lower Canadian dollar and steady U.S. demand. What's more, mining activity is assumed to increase partly on account of two new mines in Northern Manitoba, while the government's large capital plan provides some economic stimulus. The province is also counting on continued solid population gains (+1.3%). Over the past five years, population growth has averaged 1.2%, slightly ahead of the national average. Nominal GDP growth – a good proxy for revenue-intake – is forecast to run at 4.2% over the 2015-16 period. These projections are reasonable in our view.

In fiscal 2015-16, revenue growth is estimated at a tepid 1.2%. On the surface this appears to be out of line with the government's healthy nominal GDP forecast. However, this largely reflects a 0.8% estimated drop in federal transfers (which account for more than 25% of revenues). Net income from Government Business Enterprises (GBEs) are also forecast to move lower (-11.2%). Beyond these two revenue streams, strong gains are expected to be recorded in personal and corporate income tax receipts (+4.8%). Other taxes (+3.6%) are also projected to post a notable advance, reflecting increased growth in retail sales and fuel taxes as well as a rise in capital tax earnings. On the other side of the ledger, total expenditure growth is forecast at 1.9% in fiscal 2015-16, a marked slowdown from the 3.7% average increases recorded over the previous two fiscal years. Growth in spending dedicated to health (+3.2%) and education (+2.1%) is forecast to decelerate for a third consecutive

year. In order to control headline spending, outlays in other areas including justice will decline by 6.1% this fiscal year. Debt servicing costs (-0.4%) are also forecast to move lower.

Budget 2015 also draws down on the Fiscal Stabilization Fund to the tune of \$105 million in fiscal 2015-16 to retire a portion of core government borrowings and help offset the impact of investment in capital spending.

### Core plan targets balance in fiscal 2018-19

The government presented a core fiscal forecast beyond fiscal 2015-16 (see Table 3). This does not include activities related to GBEs such as Manitoba Hydro, Manitoba Public Insurance and all health authorities. The core fiscal plan projects that revenues will rise at an average annual rate of 3.7% from fiscal 2016-17 through fiscal 2018-19. Core expenditures are forecast to increase at an average rate of 2.4%, which still translates to a decline in real per capita terms. All told, the government expects to bring the budget back to a balanced position in fiscal 2018-19.

The government intends to control spending through securing additional efficiencies. For example, the government has targeted \$50 million in savings in health care services over the next four years after reaching a deal with doctor's

**TABLE 2: MANITOBA ECONOMIC ASSUMPTIONS**

[ Per cent change, unless otherwise noted ]

	2014E	2015F	2015F
Real GDP	2.4	2.5	2.3
Nominal GDP	3.9	3.8	4.6
CPI Inflation	1.9	0.9	2.3
Employment	0.1	1.2	1.1
Unemployment rate (%)	5.4	5.4	5.4
Population	1.3	1.3	1.3

2014: actual (except GDP).

2015-16F: forecast courtesy of Manitoba Finance.

**TABLE 3: MANITOBA GOVERNMENT CORE FISCAL POSITION**

[ C\$ millions, unless otherwise indicated ]

Fiscal Year	Est.	2015 Budget			
	14-15	15-16	16-17	17-18	18-19
<b>Core Revenues</b>	12,078	12,354	12,768	13,231	13,770
% change	-	2.3	3.4	3.6	4.1
<b>Core Expenditures</b>	12,546	12,865	13,181	13,496	13,816
% change	-	2.5	2.5	2.4	2.4
<b>In-Year Adjustments/Lapse</b>	-17	-70	-70	-70	-70
<b>Net Result</b>	-451	-441	-343	-195	24
<b>Fiscal Stabilization Account Draw</b>	-	-20	-15	-10	-
<b>Surplus (+)/Deficit (-)</b>	-451	-421	-328	-185	24

Source: Manitoba Finance, Budget 2015.

to enhance the sustainability of the health-care system. Despite an overall focus on containing spending growth to a rate more or less in line with inflation, there were a number of new modest spending announcements. These include:

- As announced in mid-March, the Senior School Rebate has been increased to \$470 from \$235 for the 2015 property tax year. This is projected to lead to a \$15 million increase in tax expenditures this fiscal year.
- The primary caregiver tax credit has been increased by 10% from a maximum annual amount of \$1,275 to \$1,400, beginning in 2015.
- The income limit for the small business deduction has been raised from \$425K to \$450K – effective January 1, 2016. Small businesses that qualify for the small business deduction pay a 0% corporation income tax.
- The minimum wage will increase to \$11.00 from \$10.70 per hour, effective October 2015.

In an effort to boost revenues and offset these spending announcements, the corporation capital tax on banks, trust corporations and loan corporations will be raised from 5% to 6% beginning April 30, 2015. This is expected to generate \$25.5 million in additional revenues in fiscal 2015-16. The tobacco tax has also increased by half a cent per cigarette – generating \$2 million in additional revenues this fiscal year.

### Infrastructure plan heading into year 2

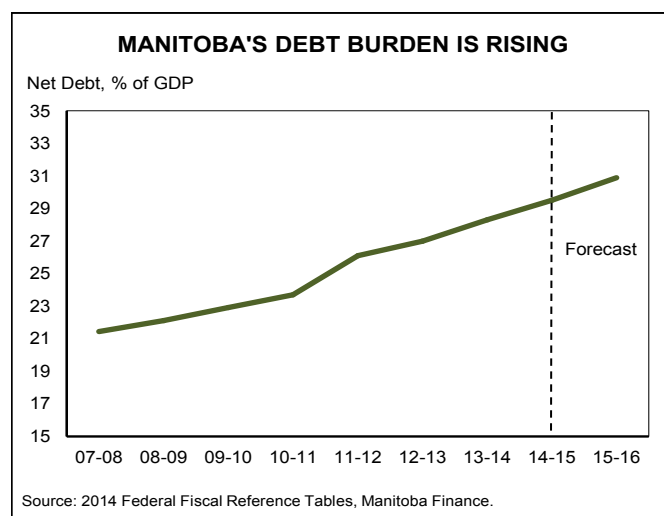
Recall in Budget 2014 the government introduced its core infrastructure plan. The 5-year plan commits to \$5.5 billion in capital spending outlays targeted towards transportation and municipal infrastructure as well as flood protection. In an effort to address these infrastructure spending needs, the government raised the PST by one point in 2013 but still requires additional funding to meet its capital plan targets. In year 2 of the plan, \$1.1 billion of planned investment

spending has been earmarked.

As a result, the Province's debt profile is forecast to rise. Net debt is forecast to climb above \$20 billion in fiscal 2015-16, or 30.9% of GDP. Gross borrowing requirements in the year ahead are estimated at \$4.7 billion of which \$3.1 billion are new cash requirements.

### Bottom Line

Budget 2015 contained very few surprises, reading more as an update on the economy and fiscal situation following the unveiling of the ambitious infrastructure plan last year. The delay in the deficit-elimination timetable is noteworthy but was announced ahead of today's budget. An important part of the government's strategy is taking advantage of current low interest rates and large investor appetite for its debt to address the province's large capital spending needs. Avoiding further delays in balancing the budget would help to limit further upward pressure on the province's debt burden, which has grown by about one third since fiscal 2007-08.





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