# TD Economics

# 2024 Ontario Budget
## Building a Better Ontario Delays Return to Balance

Leslie Preston, Managing Director | 416-983-7053
Marc Ercolao, Economist

March 26, 2024

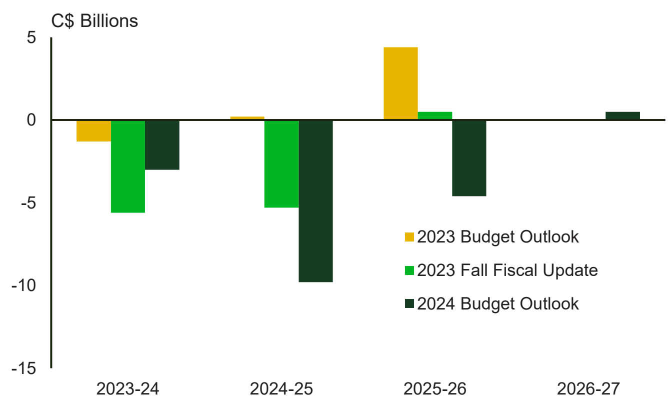
### Highlights

- Like many of its provincial peers, Ontario is expecting a much larger deficit in the current fiscal year and delays a return to a balanced budget until 2026/27.
- Even with a slightly smaller deficit in the current fiscal year ending March 31st, weaker revenues and new spending contribute to a cumulative $7 billion deterioration in the fiscal position through 2025-26, with much of it hitting in the upcoming fiscal year.
- New measures in the budget are focused on growth-enabling infrastructure and health care. Many measures had been pre-announced, including extending the gas tax holiday.
- Given larger deficits and significant infrastructure investments, net debt-to-GDP is set to rise in the near term, but remain just shy of the government's debt sustainability target of less than 40% of GDP.

After downwardly-revising this past year's estimated deficit, Ontario's FY 2024/25 deficit is expected to triple this year to nearly $10 billion, or about 1% of GDP. Ontario is not alone in reporting a wider deficit in the current provincial budget season, and is no stranger to deficits, having run one almost every year for the past 16 years. The government has delayed its return to balanced books by one year relative to the November 2023 fiscal update, getting back to black in FY 2026/27.

The budget maintains a Contingency Fund within program spending of $0.5 billion in the outgoing fiscal year and $1.5 billion in the year ahead, and "increases" it through the medium term, which could be used to ultimately report smaller deficits. If these contingencies are added to the reserves shown in the fiscal table, the budget could return to balance a bit earlier than currently projected. Thus far, however, the government has favoured raising spending to deal with a host of pressures and infrastructure spending to help "build a better Ontario".

**Chart 1: Kicking the Budget Surplus Can Down the Road**




Source: Ontario Budget 2023 and 2024, Ontario Ministry of Finance, TD Economics.

### Slowing revenue growth has some room for upside

After recording a 1.2% gain 2023, growth in real GDP is seen slipping to only 0.3% this year, weighed down by a softer global growth backdrop and elevated interest rates. After which, real GDP growth is expected to bounce back to 1.9% in 2025. These projections underpin modest gains in nominal GDP (the broadest measure of the tax base) as shown in the table on page 3.

The government's growth projections are prudent, and generally align with TD Economics' view. Our forecast for slightly stronger growth on average over the next two years, suggests some potential upside to their revenue projections. Using the government's elasticities, cumulative revenues in 2024 and 2025 could be $750 million higher. Of note, the impact of the federal cap on international students and temporary foreign workers disproportionately impacts Ontario, where the intake in both categories has been relatively robust in recent years. The government appears to have already built in the effects of the former.

In line with a softer economic performance and a weaker job market, revenue growth is forecast to ease to under 1% in FY 2024/25 – well below the long-term average. However, revenues are expected to bounce back in the outer years, growing at 5.0% on average. Personal income and corporate tax revenues are expected to advance modestly in FY 2024/25, though a 2.5% decline in sales taxes unwinds part of the total taxation revenue gain. A 4.5% increase from federal transfers is largely based on existing federal-provincial funding agreements.

The Budget is largely void of any major tax measures though emphasis has been placed on ongoing tax system reviews intended to support greater productivity in the economy. The government is also undertaking a review of the property assessment and taxation system.

Prior to the Budget release, The Ontario government announced extension of the temporary gas and fuel tax rate cut until the end of 2024, estimated to total $620 million in foregone revenues in FY 2024/25. A new computer animation and special effects tax credit along with tax relief on wine and beer will only carry minor impacts on total revenues. We believe some of this hit could be recouped via land transfer tax revenues, where our more optimistic hosing resales forecasts implies a $250 million boost to revenues, given government sensitivities.

## Spending growth higher than expected, but restraint still promised

Program spending in the outgoing fiscal year was just shy of a billion dollars higher than at the time of the fall fiscal update, and up 4.3% from the prior fiscal year. Program spending growth does continue to slow in the current fiscal year to 3.1%, but less than planned in the fall economic

**Government of Ontario Fiscal Plan**

[ C$ billions unless otherwise noted ]

| Fiscal Year | 2024 Budget Plan | | | | |
|---|---|---|---|---|---|
| | 22-23 | 23-24 | 24-25 | 25-26 | 26-27 |
| **Revenues** | **192.9** | **204.3** | **205.7** | **217.4** | **226.6** |
| % change | 4.2 | 10.4 | 0.7 | 5.7 | 4.2 |
| **Expenditures** | **198.8** | **207.3** | **214.5** | **220.6** | **224.1** |
| % change | 8.6 | 4.3 | 3.5 | 2.8 | 1.6 |
| **Program Spending** | **186.4** | **194.5** | **200.6** | **205.8** | **208.9** |
| % change | 9.4 | 4.3 | 3.1 | 2.6 | 1.5 |
| **Interest Charges** | **12.4** | **12.8** | **13.9** | **14.7** | **15.2** |
| % change | -1.6 | 3.2 | 8.6 | 5.8 | 3.4 |
| **Reserve** | 0.0 | 0.0 | 1.0 | 1.5 | 2.0 |
| **Budget Balance** | **-5.9** | **-3.0** | **-9.8** | **-4.7** | **0.5** |
| % of GDP | -0.6 | -0.3 | -0.9 | -0.4 | 0.0 |
| **Net Debt** | **400.5** | **414.8** | **439.1** | **459.8** | **474.5** |
| % of GDP | 38.2 | 38.0 | 39.2 | 39.5 | 39.1 |

Note : Numbers may not add up due to rounding.
Source: Ontario 2024 Budget.

| Ontario Economic Assumptions | | | | |
|---|---|---|---|---|
| Annual Percent Change (Unless Otherwise Indicated) | | | | |
| Calendar Year | 2023 | 2024 | 2025 | 2026 |
| **Real GDP** | | | | |
| **Budget 2024** | **1.2** | **0.3** | **1.9** | **2.2** |
| TD Economics Forecast | 1.3 | 0.6 | 1.5 | 1.9 |
| **Nominal GDP** | | | | |
| **Budget 2024** | **4.1** | **2.7** | **3.9** | **4.3** |
| TD Economics Forecast | 4.3 | 3.9 | 3.4 | 3.9 |
| **3-Month Treasury Bill Yield** | | | | |
| **Budget 2024** | **4.8** | **4.4** | **3.0** | **2.6** |
| TD Economics Forecast | 4.7 | 4.6 | 2.8 | 2.3 |
| **10-Year Gov't Bond Yield** | | | | |
| **Budget 2024** | **3.3** | **3.2** | **3.1** | **3.3** |
| TD Economics Forecast | 3.4 | 3.3 | 2.9 | 2.9 |
| Source: Ontario Ministry of Finance, as at March 2024. | | | | |

update (1.7%). But, the government resolves to tighten its belt in the coming fiscal years holding spending growth to 2.6% next year and only 1.5% in FY 2026/27.

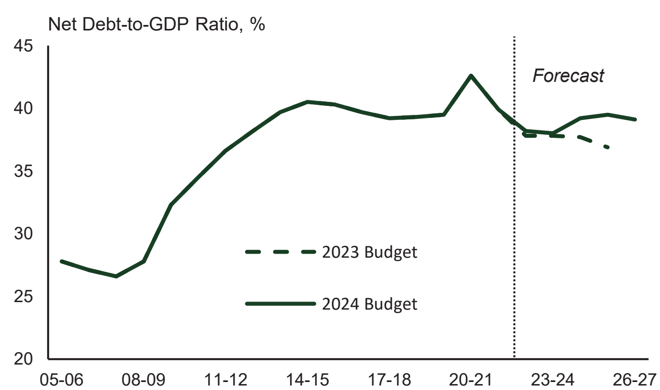
One big ticket pressure was the $6 billion in backpay for public sector workers last year and this year due to the repeal of Bill 124 (which had capped salary increases for public sector workers). Other "new" spending worked into the fiscal framework include $190 billion over ten years in infrastructure and more specifically support for municipalities to enable more housing supply, money for health care and numerous other priorities (much previously announced) including the following big-ticket items:

- $1.8 billion in two funds for municipalities to build "housing enabled" infrastructure.
- $1.2 billion in Building Faster Fund to reward municipalities to achieve their housing targets.
- $2 billion over three years to expand home cares access and increase compensation for personal support workers and nurses.
- $1 billion for hospitals.

Interest costs are projected to jump by 8.6% in FY 2024/25. This represents 6.8% of revenues, leaving Ontario's interest bite below its long-term average and shy of the government's target of 7.5%. However, putting Ontario's debt burden in perspective, the $13.9 billion the province will pay to service its debt this year is more than it spends on postsecondary education.

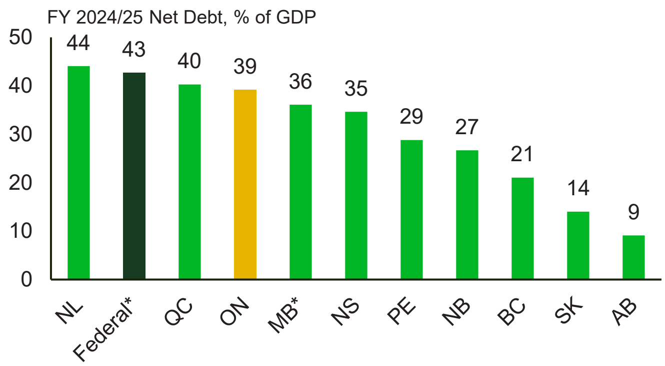
Another key measure that doesn't hit the fiscal plan were planned "reforms" to the auto insurance industry, by making only medical, rehabilitation and attendant care benefits for severely injured people coverage mandatory, and other benefits optional to give drivers the opportunity to lower their premiums.

**Chart 2: Debt- Burden Rises in the Near-Term**




Source: Ontario Budget 2023 and 2024, Ontario Ministry of Finance, TD Economics.

**Chart 3: Ontario Carries Heavy Debt Loads**




*As of 2023 Fall Fiscal updates.
Source: Government Documents, TD Economics.

## Deficits, capital spending drive debt higher

The combination of on-going deficits and robust capital spending plans sees the province's net debt-to-GDP rising from an estimated 38.0% in FY 2023/24 to a peak of 39.5% in FY 2025/26, before retreating to 39.1% by FY 2026/27 (Chart 2). That ratio is just shy of Ontario's prescribed 40% ceiling and doesn't provide much wiggle room in the event that economic growth undershoots or the government runs larger-than-expected deficits. Current debt levels are elevated by historical standards and relative to other provinces (Chart 3). In FY 2024/25, infrastructure investment is forecast to expand solidly this year, consistent with the last survey of capital spending intentions, which is pointing to a 15% gain in spending in 2024. Planned investments totalling $190 billion are built into the Budget over the next ten years.

Total long-term borrowing requirements are estimated at $38.2 billion for FY 2024/25, edging down from the $41.8 billion in long-term borrowing completed last fiscal year. Borrowing remains elevated over the following two years, averaging $35 billion, as rising capital-spending requirements offset a declining deficit. The government will also continue with its Green Bond offerings, with $3 billion in issuances occurring in FY 2023/24, and a new framework for allowing a broader range of potential offerings in the future.

## Bottom Line

Ontario's fiscal situation is expected to deteriorate further over the next few years relative to the government's previous expectations, as continued sub-par growth term in the economy and the revenue take battles up against ongoing pressure in key spending areas, notably big outlays on infrastructure, specifically to enable new housing supply and health care. The government is relying on holding spending increases to a modest rate and a normalization in revenue growth to bring the budget back to balance in two years.

While the government's finances have come a long way from earlier pandemic-era forecasts, the continued uptrend in the already-high debt burden leaves the province more vulnerable to unexpected economic or financial events. Helping to mitigate these risks are the government's practice of building in significant contingency reserves, which it maintained in this budget. Moreover, given the resilience of household spending amid high rates, the prospect that the economy will pull off a soft landing has increased significantly in recent quarters – clearly good news from a fiscal perspective.

Lastly, it's importance to recognize that a chunk of the uptick in the province's debt burden is capital investment. This spending is needed given the demands of a rapidly growing population. More broadly, infrastructure investment can also help boost longer-term productivity, and Ontario has had its issues in in this regard in recent years.