Ontario Fall Economic Statement: Delayed Path to Balanced Books

Marc Ercolao, Economist

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Highlights

- The Ontario government's budget balance nearly quadrupled in FY 2023/24 to $5.6 billion. Relative to GDP, this figure remains relatively modest at 0.5%. Most of the fiscal deterioration was due to starting point shocks.
- Although debt servicing costs have been marked lower this year, interest costs will continue to climb over the forecast horizon. Meanwhile, net debt-to-GDP shows little improvement over the next three years.
- The marquee spending measure is the $3 billion investment of a new Ontario Infrastructure Bank. Other spending was modest and the update was void of any new major inflation-relief spending.

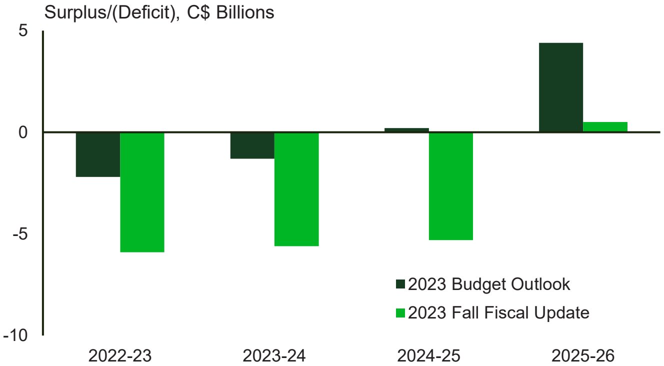
In its Fall Economic Outlook and Fiscal Review, the Ontario government is now anticipating a budget deficit of $5.6 billion in 2023-24, larger than the $1.3 billion deficit projected in Budget 2023 but still a relatively modest 0.5% of GDP. Cumulatively, roughly $14 billion in red ink has been added to the deficit tally between FY 2022/23 and FY 2024/25, with the government opting to delay its return to a surplus by one year, to FY 2025/26.

The main culprit behind the fiscal deterioration is a weaker starting point. Notably, in its recently released FY 2023/23 Public Accounts, revenues were marked down by a hefty $8 billion relative to previous estimates. Much of that shortfall (owing to a downgrade in personal income taxes) is expected to carry over through the medium-term forecast period. This masks a continued moderate expansion in the overall revenue take over the next 3 years in line with nominal GDP gains.

A portion of the higher deficit in the current year can be chalked up to an upgrade in spending plans. In particular, the total expense outlook in FY 2023/24 has been raised $1.7 billion above the 2023 budget assumption, bringing the total increase to $9 billion. Part of that growth could reflect the timing of expenditures, as last year's final outlays were revised down by around $4 billion in the Public Accounts. Moreover, the government has booked $2.5 billion in contingency funds this year, bringing up the balance to $5.4 billion (these spending contingencies are distinct from the government's customary reserve allowance that grows over time). Beyond this year, the government has left its total spending targets largely intact from last year's budget.

What may come as a surprise to some, debt service costs have been marked down relative to Budget 2023, by roughly $1 billion, as the government benefits from a lower-than-expected hand-off from FY 2022/23. Still, interest costs are expected to rise by almost $3 billion over the forecast horizon.

Chart 1: Ontario's Road to a Balanced Budget Will Take an Extra Year



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

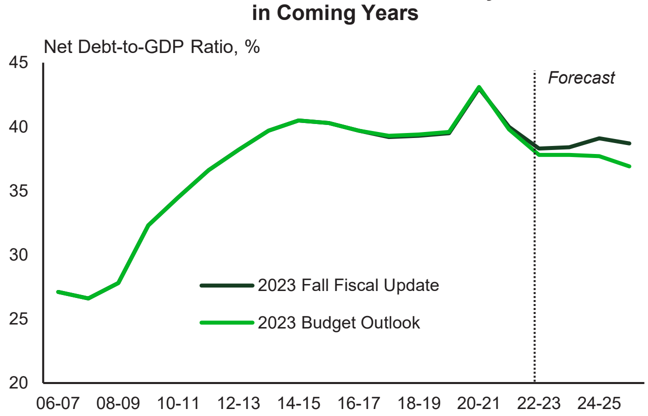
Government of Ontario Fiscal Plan [C$ billions unless otherwise noted]				
Fiscal Year	2023 Fall Fiscal Update			
	22-23	23-24	24-25	25-26
Revenues	**192.9**	**201.8**	**206.7**	**220**
% change	4.2	4.6	2.4	6.4
Expenditures	**198.8**	**206.4**	**210.5**	**217.5**
% change	8.6	3.8	2.0	3.3
Program Spending	**186.4**	**193.0**	**196.2**	**202.3**
% change	9.3	3.5	1.7	3.1
Interest Charges	**12.4**	**13.4**	**14.3**	**15.2**
% change	-1.6	8.1	6.7	6.3
Reserve	**-**	**1.0**	**1.5**	**2.0**
Budget Balance	**-5.9**	**-5.6**	**-5.3**	**0.5**
% of GDP	-0.6	-0.5	-0.5	0.0
Net Debt	**400.5**	**416.1**	**435.4**	**449.1**
% of GDP	38.3	38.4	39.1	38.7

Note : Numbers may not add up due to rounding.
Source: 2023 Ontario Economic Outlook and Fiscal Review.

As to economic assumptions, the government coffers will continue to benefit in the near term from decent nominal economic growth tied to higher inflation. Nominal GDP for 2023 is forecast to expand by 3.6% in 2023 compared to Budget projection of 2.8%. The Province expects a moderate slowdown in its planning scenario in 2024 and 2025, which will lean against revenue gains somewhat in the outer years. Furthermore, the government is assuming a 10-year Government of Canada yield at around 3.25% on average over the next years. These projections are in line with our own.

Consistent with a higher deficit, Ontario's net debt-to-GDP ratio is now forecast to be 38.4 per cent in FY 2023/24, compared with its Budget 2023 projection of 37.8 per cent. Looking ahead, little improvement is now expected in the debt ratio over the next 3 years. Ontario is currently the 2nd most indebted province.

Chart 2: Debt-to-GDP Ratio To Gradually Worsen in Coming Years



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

Total long-term borrowing requirements total $34.7 billion in FY 2023/24, $7.2 billion more than the 2023 Budget forecast. Requirements are then slated to increase to $37.0 billion next year, before falling slightly to $37.0 billion in FY 2025/26, roughly mirroring the flat net-debt profile.

Infrastructure Bank Tops The List Of New Measures

In the document, the government cited a scattershot of measures, many of which were previously announced. In terms of the more significant initiatives announced today, the most notable was $3 billion for the creation of an arms-length infrastructure bank, with a mandate to help build major projects in affordable housing, health care and transportation. The idea is to reduce the risk of large-scale infrastructure projects while also attracting private capital from pension and insurance funds.

Also in the vein of infrastructure, an additional $200 million over 3 years will be targeted to a new Housing-Enabling Water Systems Fund for the repair, rehabilitation and expansion of municipal water infrastructure projects.

The government has proposed an additional $12 million per year in tax credit support to the critical minerals mining industry via expanding eligibility of the Ontario Focused Flow-Through Share Tax Credit.

On the household side, it followed through with a previously-announced extension of the 5.7 cents/litre gas tax cut until June 2024– saving consumers an average of $260–and eliminating the provincial portion of the HST on purpose-built rentals.

The government also announced an additional $100 million for Invest Ontario, an agency tasked with attracting business investment in the province

Bottom Line

Although the government's budget balance has deteriorated since the spring budget, much of that reflected a weaker starting point rather than significant new measures incorporated on a go-forward basis.

The narrative around Ontario finances is unchanged, notably an elevated debt burden that is projected to show little progress amid a looming economic slowdown and spending pressures partly tied to a strongly rising population.

On the plus side, the government did refrain from introducing significant new inflation-relief measures for households that would probably only exacerbate near-term price pressures and thus be counterproductive.

The sizeable contingencies incorporated in the budget plan will provide a cushion in the even that economic conditions deteriorate more than expected. Given the government's still-elevated debt burden, our hope would be that any unused funds be deployed towards debt reduction.