

March 12, 2018

Staying the course of fiscal responsibility

Highlights

- For fiscal 2017-18, the Third Quarter Report forecasts a summary deficit of \$726 million (1.0% of GDP), an improvement of \$114 million from the \$840 million budgeted last spring.
- For fiscal 2018-19, Budget 2018 projects a \$205-million reduction of the summary deficit to \$521 million. Of this improvement, \$40 million comes from excess of revenue growth over expenditure growth, \$50 million from the non-repeat of a contingency for writedown and \$115 million from yet-to-be-identified revenue increases and/or expense reductions, termed “in year adjustments/lapse.”
- The summary deficit is projected to shrink over the four-year planning period to \$142 million in 2021/22. While a balanced budget is not projected in any of those four years, the government remains committed to returning the budget to balance in its second term, that is by 2024.
- As previously telegraphed, Budget 2018 introduces a carbon tax of \$25 per tonne of greenhouse gas emissions effective September 1. The tax will apply to gas, liquid, and solid fuel products intended for combustion. It is projected to generate \$248 million in revenue during its first 12 months.
- The budget also announces the largest-ever enhancement of the Basic Personal Amount (BPA) in the 2019 and 2020 taxation years. In 2019 the BPA will rise to \$10,392 from \$9,382. In 2020 it will rise to \$11,402 from \$10,392. This measure is projected to remove more than 31,000 people from the tax rolls and reduce Manitobans’ income taxes by more than \$77 million in 2019 and another \$78 million in 2020, for a cumulative reduction of \$156 million in full-year revenue.
- The budget increases the income threshold for the small-business tax deduction to \$500,000 from \$450,000 effective January 1, 2019. Canadian-controlled private corporations that qualify for the small-business deduction pay no Manitoba corporation income tax. This enhancement will save companies up to \$6,000 per year. The estimated full-year cost is \$7 million.
- Effective midnight March 12, the tax rate for fine cut tobacco increases to 45¢ per gram from 28.5¢. The full-year revenue increase is budgeted at \$7 million. The tax rate on cigarettes, cigars and raw leaf tobacco is unchanged.
- The special tax deduction that currently allows credit unions and caisses populaires to pay a lower rate of tax on a portion of their income is to be phased out over five years beginning January 1, 2019. Credit unions will continue to have access to the small-business deduction. The full-year increase in government revenue is estimated at \$15 million upon full implementation in 2023.
- The budget assumes that Manitoba’s real GDP growth, estimated at 2.2% in 2017, will slow this year and next like that of Canada as a whole. The Manitoba Finance Survey of Economic Forecasts projects growth of 2.0% in 2018 and 1.6% in 2019. Nominal GDP is projected to increase 3.8% in 2018 and 3.5% in 2019. Employment growth, 1.7% in 2017, is forecast to slow to 0.8% in 2018 and 0.5% in 2019.
- Summary net debt is estimated at 34.0% of GDP at the end of the current fiscal year. This ratio is projected to grow to 34.3% in the coming fiscal year. Borrowing requirements for fiscal 2018-19 are pegged at \$6.4 billion, of which \$4.2 billion for Manitoba Hydro.

The Third Quarter Report for 2017-18

The summary deficit for the year ending March 31 is now estimated at \$726 million (1.0% of GDP), an improvement of \$114 million from the \$840 million projected in Budget 2017. The improvement comes despite a \$254-million shortfall in income tax revenue attributable to changes in federal income taxes announced in 2015. Stronger-than-expected revenue from corporate and retail sales taxes and from fees, other own-source revenue, federal transfers, net income of Government Business Enterprises, sinking funds and other earnings have offset this storm. At the end of the day, summary total revenue is assumed to be up \$27 million from last year's budget, though Core Government revenue is \$71 million below budget.

Expenditures are estimated at \$252 million below budget, thanks mainly to a strong crop year now expected to result in less payout than anticipated. The forecast in the Third Quarter Report includes a \$50-million contingency for write-down, not incorporated in last year's budget, of assets whose book value is expected to exceed actual value. Taking into account the \$115 million "in-year adjustment/lapse" incorporated in the budget, we arrive at a \$114-million improvement over budget in the estimated summary deficit.

The improvement in the Core Government deficit is marginal – from \$779 million to \$775 million. This is because Core Government revenue is forecast to be down \$71 million from budget, since the aforementioned decline in income taxes has not been fully offset by revenue from other sources. Core Government expenditure is forecast to come in \$160 million under budget, primarily in health care including lower costs due to previously announced delays. Add to these numbers the aforementioned \$50-million contingency for writedown and a \$35-million in-year adjustment/lapse, and the Core Government deficit is forecast to edge down \$4 million.

Budget 2018: The path forward

In 2018-19, revenue is budgeted to grow \$659 million (+4.1%) over the 2017-18 forecast and expenditure \$619 million (+3.7%). The fiscal framework embeds \$115 million in revenue increases and/or expenditure decreases yet to be identified. With that item (called "in-year adjustments/lapse") included and assuming the \$50-million contingency for writedown will not be repeated, the summary deficit for the coming fiscal year is budgeted at \$521 million (0.7% of GDP), a \$205-million improvement over the forecast for fiscal 2017-18.

That deficit is \$177 million less than was forecast in last year's budget (which did not take into account the one-time contingency for writedown).

The forecast deficit for the following year, 2019-20, is reduced by \$133 million from the budgeted deficit for the

coming year, to \$388 million, or \$161 million less than was projected last year.

The deficit is projected to fall gradually to \$142 million in 2021-22, the last year of the forecast period. Over that period, \$115 million in yet-to-be-identified revenue increases and/or expense decreases are projected for each year. In the four years 2018-19 through 2021-22, revenue is projected to grow an average 2.2% annually and expenditure an average 1.5% annually. While a balanced budget is not projected in any of those four years, the government remains committed to returning the budget to balance in its second term, that is by 2024.

Tax measures

As previously telegraphed, today's budget introduces a carbon tax of \$25 per tonne of greenhouse gas emissions effective September 1. This tax will apply to gas, liquid, and solid fuel products intended for combustion. It is projected to generate \$248 million in revenue during its first 12 months.

The budget announces the largest-ever enhancement of the Basic Personal Amount (BPA) in the 2019 and 2020 taxation years. In 2019 the BPA will rise to \$10,392 from \$9,382, a \$1010 increase that will translate into a \$109 tax saving for an individual. In 2020 it will rise the same amount to \$11,402. This measure is projected to remove more than 31,000 people from the tax rolls and reduce Manitobans' income taxes by more than \$77 million in 2019 and another \$78 million in 2020, for a cumulative reduction of \$156 million in full-year revenue.

The budget increases the taxable-income threshold for the small-business tax deduction to \$500,000 from \$450,000 next January 1. Canadian-controlled private corporations that qualify for the small-business deduction pay no Manitoba corporation income tax. This enhancement will save companies up to \$6,000 per year in taxes. The estimated full-year cost is \$7 million.

The special tax deduction that currently allows credit unions and caisses populaires to pay a lower rate of tax on a portion of their income is to be phased out over five years beginning next January 1. Credit unions will continue to have access to the small-business deduction. The full-year increase in government revenue is estimated at \$15 million upon full implementation in 2023.

Effective midnight March 12, the tax rate for fine cut tobacco increases to 45¢ per gram from 28.5¢. The full-year revenue increase is budgeted at \$7 million. The tax rate on cigarettes, cigars and raw leaf tobacco is unchanged.

These measures and others of smaller effect are projected to increase government revenue by a net \$105 million once fully implemented.

Fiscal responsibility

Over the 13 years before 2016-17, core expenditure budgets were continuously overspent. If the forecast for the fiscal year about to end is on the mark, it will be the second year in a row of below-budget spending. The province's credit rating was downgraded three times in three years; demonstrating fiscal responsibility is a way to arrest that trend.

Manitoba's Fiscal Responsibility and Taxpayer Protection Act requires governments to show progress toward a balanced summary budget. The government is promising amendments to strengthen the Act by holding governments accountable for steady reduction from a "Base Line Deficit" defined as summary deficit less net income from Manitoba Hydro and the Fiscal Stabilization Fund transfer. An improvement of \$100 million per year will be required every year in order for ministers to receive all their pay. The amendments to the Act are intended to create greater incentives for the difficult work of restoring finances and remove disincentives to early progress or achievement beyond \$100 million per year. Measuring progress from the 2017/18 budget, the Act will also allow for reinstatement of ministerial salaries withheld once a surplus is achieved.

Economic assumptions

By our measurement, Manitoba's economy is the most diversified of any province. For that reason its economy used to grow at a fairly stable rate. Manitoba has attracted a record number of skilled workers, entrepreneurs and their families, mostly because of an immigration policy centred on the

Manitoba Provincial Nominee Program (MPNP). Its population has accordingly grown the fastest of any province's over the last three years. Recent enhancements to the MPNP will make it easier for international students with a Manitoba education to settle and build careers in the province.

The budget assumes that Manitoba's real GDP growth, estimated at 2.2% in 2017, will slow this year and next like that of Canada as a whole. The Manitoba Finance Survey of Economic Forecasts projects growth of 2.0% in 2018 and 1.6% in 2019. Nominal GDP is projected to increase 3.8% in 2018 and 3.5% in 2019. Employment growth, 1.7% in 2017, is forecast to slow to 0.8% in 2018 and 0.5% in 2019. Those are cautious assumptions, but there are many risks in the outlook. A NAFTA outcome significantly affecting trade, rising interest rates and major U.S. tax changes could materially affect the mobility of capital and labour.

Debt and borrowing

Summary net debt is estimated at 34.0% of GDP at the end of the current fiscal year. This ratio is projected to grow to 34.3% in the coming fiscal year. Attention has been drawn to the estimate that debt service cost will top \$1 billion next year. However, the resulting 6.2% bite out of summary revenue is far from the worst among the provinces.

Borrowing requirements for fiscal 2018-19 are pegged at \$6.4 billion, of which \$4.2 billion for Manitoba Hydro.

Marc Pinsonneault

Manitoba • 2018 Budget

Manitoba

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Budget	Forecast	Budget	Projection		
2017/18	2017/18	2018/19	2019/20	2020/21	2021/22

SUMMARY BUDGET

Revenue	16,101	16,128	16,787	17,095	17,243	17,593
Income taxes	4,194	3,940	4,041			
Other taxes	4,497	4,620	4,800			
Fees and other revenues	2,307	2,363	2,333			
Federal transfers	4,163	4,195	4,496			
Net income (loss), government business enterprises	705	758	842			
Sinking funds and other earnings	235	252	275			
Expenditure	17,056	16,804	17,423	17,598	17,638	17,850
Health	6,681	6,633	6,751			
Education	4,410	4,405	4,453			
Family services	2,131	2,128	2,144			
Community, economic and resource development	1,473	1,275	1,441			
Justice and other program expenses	1,370	1,399	1,600			
Debt servicing	991	964	1,034			
Contingency for Writedown	-	50	-			
In-Year Adjustments/Lapse	(115)	-	(115)	(115)	(115)	(115)
Summary net income	(840)	(726)	(521)	(388)	(280)	(142)
Debt servicing as a % of revenues	6.2%	6.0%	6.2%			
Summary net income as a % of GDP	-1.2%	-1.0%	-0.7%	-0.5%		

CORE GOVERNMENT

Revenue	13,016	12,945	13,546	13,898	13,989	14,302
Expenditure	13,820	13,660	14,170	14,306	14,306	14,478
Contingency for Writedown	-	50	-			
Year-end Adjustments/Lapse	(35)	-	(35)	(35)	(35)	(35)
Transfer from Fiscal Stabilization Account	(10)	(10)	(50)	(50)	(50)	(50)
Core government net income	(779)	(775)	(639)	(423)	(332)	(191)

SUMMARY NET DEBT

Provincial Borrowings, guarantees & obligations	45,464	44,986	48,480			
Net pension liability	2,766	2,745	2,924			
Debt repayable by the Manitoba Hydro-Electric Board	(19,267)	(19,249)	(21,855)			
Other debt	874	763	739			
Less: Net financial assets	5,065	5,293	5,225			
=Summary net debt	24,772	23,952	25,063			
Summary net debt as a % of GDP	35.7%	34.0%	34.3%			

BORROWING REQUIREMENTS (\$ million)

Refinancing			2,285
New cash requirements			4,794
Less Repayments			661
Total borrowing requirements			6,418
As of Manitoba Hydro			4,188

Source: Province of Manitoba, *Budget and Supplementary Financial Information*.

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