

May 18, 2016

The FAO's Spring 2016 Economic and Fiscal Outlook Statement by the Financial Accountability Officer

Good morning. Welcome.

Today I provided to the Speaker, for tabling, a report assessing the economic and fiscal outlook of the Province of Ontario.

The Economic Outlook

The outlook for the Ontario economy is a fundamental building block of the FAO's fiscal projections.

And on this there is positive news. The Financial Accountability Office is forecasting solid economic growth for Ontario with real GDP increasing by two and a half (2.5) per cent in each of the next two years.

This continued steady growth builds on healthy gains in real GDP over the past two years.

This forecast is consistent with the consensus view among economists and reflects the expectation of a robust U.S. economy and a competitively valued Canadian dollar.

Most significantly, from the perspective of the Province's fiscal outlook, the FAO is forecasting nominal GDP – the broadest single measure of the tax base – to grow at an average annual rate of four (4.0) per cent over the next five years. This compares to actual growth of just three and a half (3.5) per cent on average over the past five years.

The Fiscal Outlook

Since our economic and fiscal report last fall, the province's fiscal position has improved.

The improvement reflects stronger economic growth but also, more importantly, new revenues from the government's cap and trade program as well as new federal funding.

Despite the stronger growth outlook and the new revenues, we are still projecting budget deficits over the next two years.

In 2017-18, the fiscal year that the government has committed to achieving a balanced budget, our analysis indicates a small deficit of six hundred (600) million dollars.

Compared to a one hundred and thirty (130) billion dollar Provincial budget or a seven hundred and fifty (750) billion dollar economy, a deficit of six hundred (600) million is manageable given the flexibility built into the fiscal plan.

My report acknowledges that the Province should be able to achieve its commitment of balancing the budget in 2017-18.

However, maintaining balanced budgets in Ontario will be an on-going challenge for the Province as revenue growth remains moderate and spending pressures build.

The FAO is projecting a gradual deterioration in the Province's budget balance leading to a deficit of one point seven (1.7) billion dollars within five years.

Ontario's Debt Outlook

Turning to the debt outlook for the province – Over the next five years, Ontario's net debt is projected to rise by almost fifty-four (54) billion dollars to three-hundred and fifty (350) billion dollars.

This continued growth in Ontario's debt reflects projected deficits over the next five years plus forty-five (45) billion dollars in additional borrowing, mostly to finance new capital spending for the government's large infrastructure program.

Combining Ontario's rising debt with the expected growth in the economy, the FAO projects that the province's debt-to-GDP ratio will decline by approximately one percentage point over five years.

At this pace, it would take more than fifty (50) years to achieve the government's commitment of a debt-to-GDP ratio of twenty-seven (27) per cent.

The Government should provide a plan and a realistic timeframe, for the achievement of this goal.

Risks to the Fiscal Outlook

Our report summarizes what we believe are the most likely outcomes for Ontario's fiscal position. However, there are significant risks.

If the economy were to maintain the average pace of growth of the past five years, growing somewhat more slowly than forecast in the Budget, revenues would be lower.

This would increase the budget deficit to one point four (1.4) billion dollars in 2017-18, with a further deterioration to three and a half (3.5) billion by 2020-21.

On the expenditure side, the FAO outlook adopts the government's own projections for program spending from the 2016 Budget.

However we remain concerned that the government will not be able to maintain its current expenditure restraint program. But without adequate information to assess the government's expenditures plans and given the government's control over its discretionary spending, we have adopted the government's projections to 2018-19.

For the two years beyond 2018-19, we have expenditures growing in line with cost pressures.

However, if the Province were to maintain existing services and allow spending to grow in-line with underlying demographic and cost pressures, program expenses would be four (4.0) billion dollars higher by 2018-19 than projected in the 2016 Budget.

The FAO outlook also adopts several critical policy assumptions built into the government's fiscal plan.

In particular, the government's fiscal outlook includes specific assumptions regarding three major sources of revenue: Equalization payments; new federal transfers and; new cap-and-trade revenues.

These three sources of revenue – totaling over five (5) billion dollars in 2017-18 – are subject to significant uncertainty. Differences in the timing, duration or net fiscal benefit of these revenue sources could have a material impact on the government's fiscal position.

A fiscal plan should balance risks. However we see most of the risks tilted to the downside.

In its determination to meet its fiscal target of a balanced budget in 2017-18, government has built a fiscal plan that is heavily exposed to factors outside its control.

This is concerning given the current level of debt and importance the government has given to maintaining high levels of capital spending to support the economy.

There is little fiscal room to deal with unexpected events.

Thank you.

I am happy to take questions.