Media Event: FAO Economic and Fiscal Outlook

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MEDIA EVENT: FAO ECONOMIC AND FISCAL OUTLOOK
December 11, 2017

Time / Location:
10:00 a.m. / Media Studio, Queen's Park

Speakers:
J. David Wake, Temporary Financial Accountability Officer; David West, Financial Accountability Office.

Media Attendance:
Print – 4
TV – 3
Radio – 0

Media Outlets:
Benzie – Star; Smith Cross – QP Briefing; Smith – QP Today; Brule - Radio Canada/CJBC; Reid – TVO.

Statements:
Wake: My name is David Wake, and I'm serving as Ontario's Financial Accountability Officer on a temporary basis. Today, the Financial Accountability Office released an updated economic and fiscal outlook report providing a forecast for Ontario's economy and an assessment of the province's fiscal position over the next four years. Our report incorporates recent economic data as well as updated fiscal information from the province's 2017 Economic Outlook and Fiscal Review. Importantly, the FAO's fiscal projections also reflect the Auditor General's recommended accounting treatment for both the government's Fair Hydro Plan as well as the net pension assets of jointly-sponsored pension plans. In contrast, the government has chosen not to adopt the Auditor General's recommended accounting for both the Fair Hydro Plan and net pension assets. This decision has contributed to a significant and growing gap between the fiscal outcomes projected by the FAO and the province. The disagreement between the Auditor General and the government has increased uncertainty and reduced the transparency and the reliability of the province's fiscal plan for both MPPs and the public. I will ask David West, the FAO's chief economist, to provide an overview of some of the key results from the FAO's economic and fiscal outlook report.

West: Thank you Commissioner Wake. Let me begin with the FAO's economic outlook, which provides the foundation for our fiscal projections. The FAO forecasts continued steady economic growth for the province. In 2017, Ontario will post its fourth consecutive year of solid economic gains. Over the next four years, economic growth is expected to moderate just slightly as household spending and residential investment ease. Strong economic growth is expected to boost revenues this fiscal year. However, despite the revenue gains, the FAO is projecting an Ontario budget deficit of four billion dollars in 2017-18, the result of the Auditor General's recommended accounting for both the Fair Hydro Plan and net pension assets. Over the next four years, the FAO is projecting a steady deterioration in the budget deficit due to the loss of one-time time-limited revenues, more moderate growth in tax revenues, and the growing fiscal impact of the Fair Hydro Plan. In the absence of any change in fiscal policy, the FAO is projecting an Ontario budget deficit of $9.8 billion by fiscal year 2021. This is a significant deterioration in the FAO's deficit projection since our spring report, and is largely the result of the introduction of the Fair Hydro Plan, which will add $3.2 billion to the budget deficit by 2021.

In comparison, under the government's accounting presentation, which does not reflect the full impact of the Fair Hydro Plan, the FAO projects a small budget surplus this fiscal year. However, even under the government's accounting basis, the FAO projects a return to budget deficits next year due to the loss of temporary revenues and more moderate growth in tax revenue growth – and more moderate growth in tax revenues. On the government's basis, the FAO projects a deficit of almost four billion dollars by fiscal year 2021. The FAO's outlook for significant and rising budget deficits leads to higher debt and a rising debt burden for the province. Over the next four years, assuming no change in current fiscal policies, the FAO expects that Ontario's net debt will increase by more than $75 billion to over $400 billion, increasing the province's net-debt-to-GDP ratio to over 41 per cent by 2021. Current and future governments are facing difficult policy choices. As we have concluded in past reports, additional measures to raise revenue or lower spending will be required if the province wants to achieve and maintain a balanced budget and also lower Ontario's debt burden. However, raising tax rates could impact economic growth, while program spending restraint would place greater stress on the current system of public services. Future policy choices need to be both pragmatic and sensitive to these challenges. Thank you. Commissioner Wake and I would be happy to take questions.

Media Questions:
Q. Brule: [in French] Do you speak French, Mr. West?

West: [in French] Not enough, I'm sorry.

Q. Benzie: Just curious. The chair of the Canadian accounting standards association concluded that the government's accounting was okay, but the Auditor General disagreed. You are siding with the Auditor General over the chair of the Canadian actuarial whatever. Why? Why don't you buy into the government's accounting, and why do you side with the Auditor General over them?

West: We view the Auditor General as the authority on the appropriate interpretation of accounting for the provincial financial statements, so we side with her as a –

Q. Benzie: (inaudible) from 2002 to 2015, this Auditor General and her predecessors said that those assets could be booked. So that changed in 2016. Why – why do you think that it suddenly, this U-turn is okay?

West: Well (inaudible) again, I'm going to just defer to the Auditor General on the appropriate accounting. There's two accounting issues too. It's not just pensions. It's also the Fair Hydro Plan.

Q. Benzie: Yeah, but the pensions are the bigger chunk, though.

West: No.

Q. Benzie: No?

West: Bigger chunk's the Fair Hydro Plan. They're roughly equivalent. By 2021, the deficit will be by our accounting, by our estimates, will be nine, roughly ten billion dollars. Six billion to that is accounting, and roughly 3.2 of that is FHP; 2.9 is pensions.

Q. Smith Cross: You don't have a response to – sorry, (inaudible) got a response from the finance minister yet? But he said in the past that the province has often beaten expectations and he just expects that will happen again. What is your feel when – what do you make of that?

West: I mean, we've evaluated the government's fiscal, you know, projections, and 17-18, on their accounting basis, we agree that the government will likely be in a small surplus position of $200 million. They're forecasting $500 million. That's neither here nor there. But going forward, because of the loss of one-time revenues – and we list five of them in this report – those are reflected both in our projection and the government's projection – and just somewhat more moderate growth in tax revenues. That will be enough to (inaudible) you know, revert to a deficit going forward. So the – you know, the – you know, in 2016-17, the Public Accounts, the government did improve a little bit on what they were projecting, but most of that is not particularly dramatic actually, and so going forward we still think there's concerns. We still have concerns.

Q. Brule: It seems like to be a pattern here. I remember seeing a story we did recently in May and then last November as well, last year, where you predict the same thing so is it a deaf ear from the government?

West: I can't speak for the government, that's for sure. But, I mean, our projections have been quite consistent. We think on the government's accounting basis, that they will achieve a balanced budget, a small surplus in 2017-18. But we (inaudible) very consistent that because of – because of a number of factors, we think the deficit will re-emerge. And now, with this accounting debate, will become more significant.

Q. Smith Cross: Can you speak more to the long term concerns that you have?

West: So this is just over the next four years. It's a five-year projection, but really over the next four years to 2021-22, but it does, you know, transition into our long-term – our long-term forecast, which we – in our long-term report, which we released in October, we made the point that the government needs to run small surpluses. It's, you know, six-billion-dollar adjustments, six-and-a-half-billion-dollar adjustment to spending or revenues, to run a very small surplus, a moderate surplus going forward to allow them to achieve the 27 per cent target that they have identified for themselves for debt-to-GDP. And without a small surplus – balanced budgets are not enough, and certainly deficits are not enough either. But you need – you need to make those adjustments today. To the extent that the government delays making those adjustments today, the cost will become greater in the future and you're shifting the burden to futures, so younger people, and to future generations as opposed to dealing with it today.

Q. Smith Cross: Could you clarify what the difference in the deficit based on the accounting dispute, what that means for the province outside of what it says – if it says it's balanced its budget? What are the ramifications come from whether the deficit is as the government is recording or as the AG would like them to?

West: I mean, well it's – I mean, what – it's confusing for the public and for MPPs as to what the appropriate treatment is, so it would be nice to have one set of – one set of numbers. I think the ramifications is that debt will continue to rise and the government is borrowing. We make the point here that – which is cash, the government is out borrowing this money. So this current year, they're going to borrow $23 billion in the markets, and that's going to rise to $45 billion in the coming years, and in four years. $45 billion is driven by deficits, small – you know, moderate deficits, but also the Fair Hydro Plan, borrowing for the Fair Hydro Plan, and also borrowing for infrastructure. So I mean, just to provide clarity, we're, you know, hoping our report helps provide clarity that this is what will be occurring.

Q. Benzie: Do you think the Liberals are cooking the books? Is that – I mean, that's what the opposition parties contend. It sounds like there's something fishy going on.

West: I don't – obviously we're not going to use that kind of language, but it's pretty clear that we think that they are overly optimistic in their revenue projections, and we make that clear. So the difference between our forecast, which is still very optimistic for revenues and the economy going forward, and their forecast, is three billion dollars. So just a tenth or two tenths on economic growth, depending on the variable, leads to a three-billion-dollar gap.

Q. Benzie: I'm not talking about growth. I'm talking about using the pension assets, the – those two pension plans as assets. Is that an example of chicanery?

West: Certainly to the extent that the government has reflected the pension assets on their books, it may not be a cash effect, but they are – but there is an impact on debt, on net debt, and on the deficit, which are key metrics for credit rating agencies and others. So these are key metrics and we think they should be presented as the Auditor General has recommended.

Q. Benzie: Now we've been wondering why the credit rating agencies haven't downgraded Ontario since this has been going on for more than a year. The Auditor General raised this in 2016. Why do you think that is that Bay Street or the rating agencies believe the government more than they believe the watchdogs?

West: I think as this debate goes forward, I think the credit rating agencies may revisit their ratings.

Q. Brule: So you agree that all the money's been taken to fund the Fair Hydro Plan, actually public money and not – government is putting it under ratepayers instead of taxpayers.

West: So on average, over the next five years, they're going to borrow $2.8 billion a year to fund this financing of lower electricity costs. That is spending, according to the Auditor General's recommended approach, and that we reflected in our estimates, and that spending increases program spending, it increases the deficit by an equivalent amount.

Q. Smith Cross: When you (inaudible) figures for the government's borrowing, just again, is that just the government's portion of the borrowing for the Fair Hydro Plan, or does that – do those figures also include OPG's borrowing as part of the Fair Hydro Plan?

West: I think that's just the government's actually. I'm going to look to my pals over here. So that is just the government's borrowing.

Q. Brule: Just quickly, you mentioned something about the report about minimum wage going up, how's that going to affect the coffers?

West: So we've reflected (inaudible) the scheduled increases in minimum wage in 2018 and 2019 in these numbers. Labour income growth is quite strong, 4.3 per cent on average over the next four years. That reflects about a one-per-cent boost to labour income from these legislated increases. So certainly the minimum wage will increase labour income, but it also will increase consumer price index. CPI is running a little bit stronger than it would otherwise without the minimum wage impact. At the same time, we've incorporated the 50,000 jobs that we estimated in August or September for that will be lost as a result of a higher minimum wage. That's incorporated into our employment projections going forward. Even so, we're seeing strong employment growth for the province. So the 50,000 is really a very small number. We're seeing about 80,000 jobs on net being created each year over the next four years. So it's anyways, the bottom line is we have reflected minimum wage in –

Q. Brule: According to you, is that going to impact the revenues from corporate taxes?

West: So the minimum wage raises labour income. That will be reflected in slightly higher PIT revenues in our – the way the models are structured. I don't think there was a direct impact on corporate taxes, no, from minimum wage.

N.B.: Comments captured are not verbatim quotes

<u>Prepared by:</u>
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