Fiscal Policy and Tracking in a Post 2017 Budget Context

Office of the Budget
MINISTRY of FINANCE

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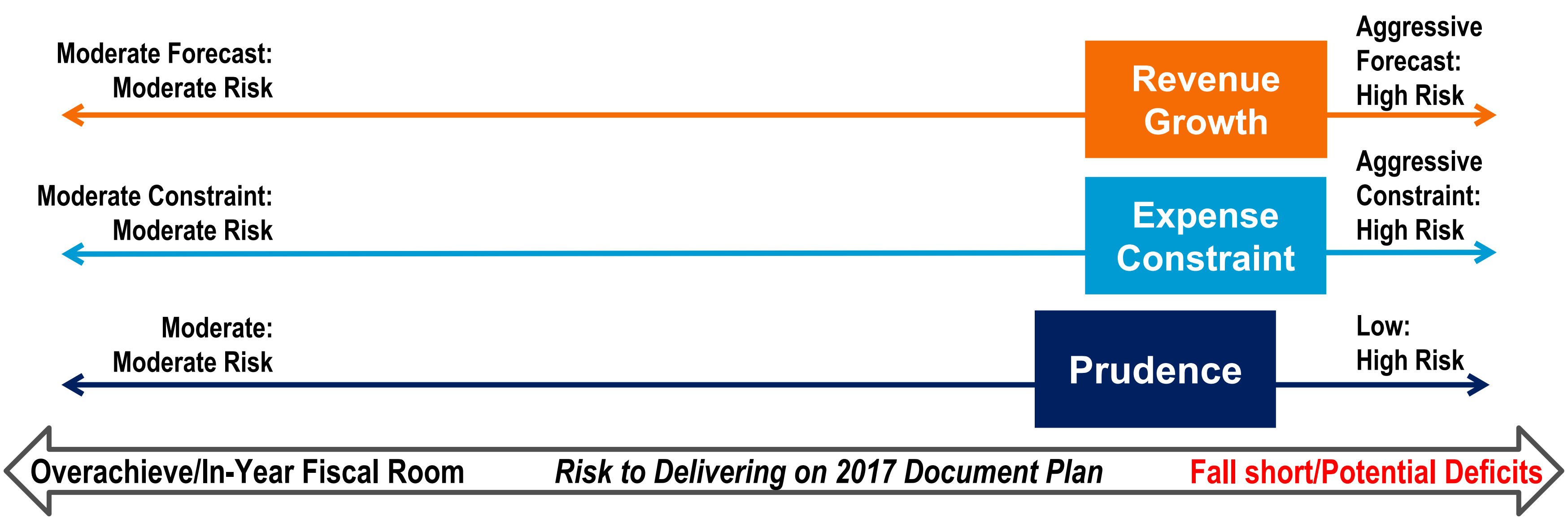
Purpose

- Provide a brief recap of the key variables that underpin the fiscal architecture of the 2017 Budget.
- Provide the overarching framework and objectives to guide fiscal tracking and decision making in 2017–18.

Current Fiscal Environment

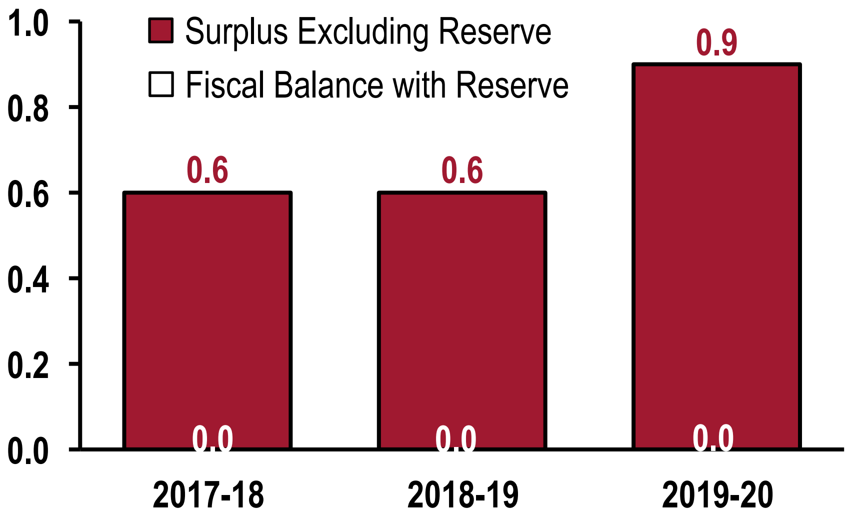
- While the 2017 Budget delivers on a balanced budget, the underlying fiscal architecture and assumptions are strained – making the plan vulnerable to risk.
  - Revenue forecast is aggressive and may not materialize
  - Expenditure management plan is robust and may fall short
  - Historically low levels of prudence are currently built into the plan
- It is also important to note that this fiscal architecture mix runs the risk of not being able to adjust to adverse events – providing limited room for error, reduced flexibility for unforeseen (or known downside risks) and potential further investments.



Recapping the 2017 Budget Fiscal Architecture

2017 Budget Fiscal Targets

Fiscal Balance
($ Billions)



Net Debt-to-GDP			
	2017-18	2018-19	2019-20
Outlook	37.5%	37.3%	37.2%
Targets	• 35% in 2023-24 • 27% in 2029-30		

Historically low reserve of $0.6 billion in 2017–18 and 2018–19, $0.9 billion in 2019–20.

Key Revenue Assumptions (2017–18 to 2019–20)

- The forecast assumes **revenue growth continues at a stronger pace than would normally be forecast given the economic outlook** and removes prudence from the nominal GDP forecast as well as assumes a modest slowing of the housing market.
- Assumes **High-Yield Tax assumptions** of $1.3 billion in 2017–18, $1.8 billion in 2018–19, and $2.2 billion in 2019–20, and zero PIT tax planning.
- Includes **Revenue Integrity Targets** of $0.1 billion in 2017–18, $0.2 billion in 2018–19, and $0.4 billion in 2019–20.
- Assumes no year-over-year decline in **Equalization Payments in 2018-19 (flat-lined at $1.4 billion)**.
- Potential impact of **IFRS Accounting** for OPG/H1 amounts to $0.5 billion in 2018–19 and 2019–20.

Key Expense Assumptions (2017–18 to 2019–20)

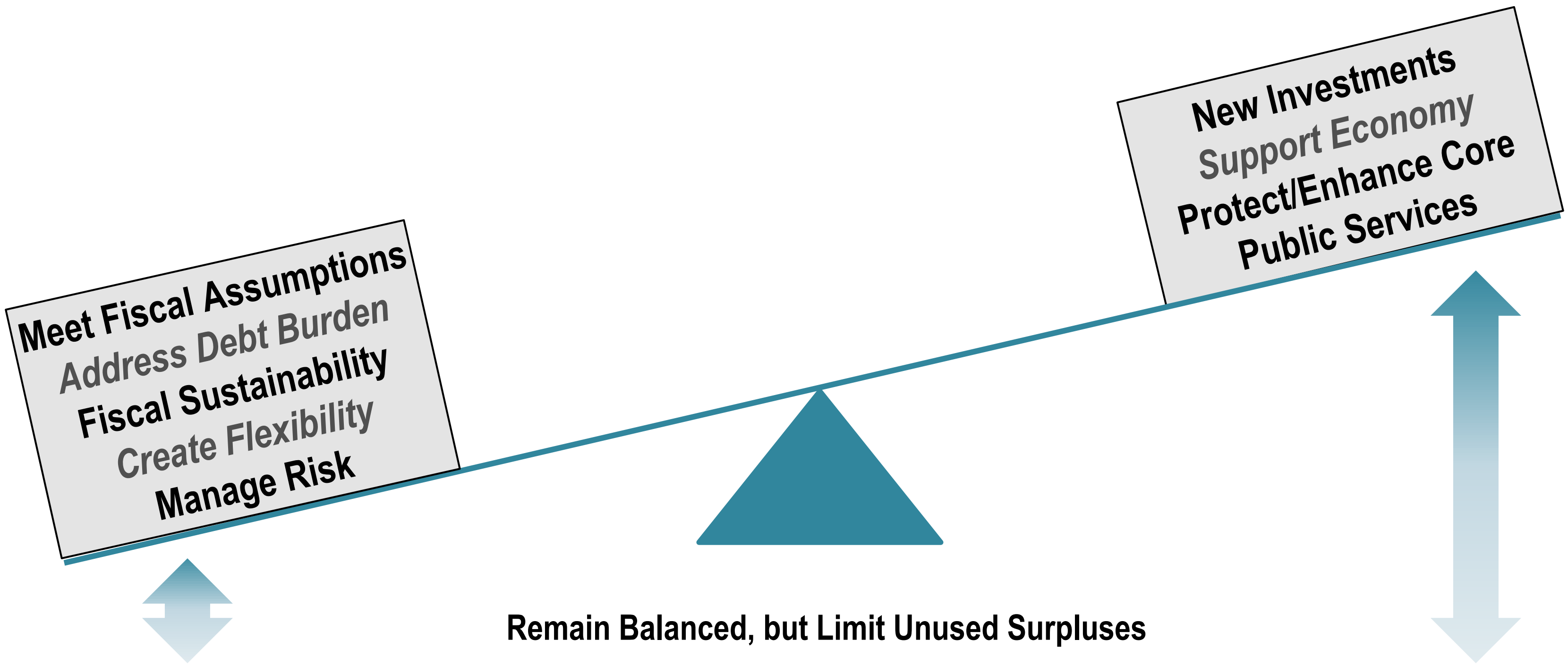
- **Net increase in program expense of $16.4 billion over three years** compared to the *2016 Budget* to invest in every sector and increase overall average spending growth from **1.9% to 2.9%** -- with a particular focus on **health and education.**
- However, overall program spending **remains constrained** – continues to decline as a share of GDP; overall growth slower than inflation+population.
- **Contingency Funds** at $0.6 billion in 2017–18; grows to $1.8 billion in 2019–20 (including set aside for MoFwd Outside the GTHA of $0.7B)
- **Year–end Savings** targets of $1.2 billion in 2017–18 and 2018–19, and $1.1 billion in 2019–20.
- **Program Review Savings** targets of $750 million in 2018–19 and 2019–20.
- Limited **Interest-on-Debt** prudence over the outlook.

Shifting Fiscal Policy for Balanced Budgets

Deficit Reduction Focus	Balanced Budgets Focus
Fiscal Targets: ▪ Declining year-over-year deficit ▪ In-year overachievement on deficit target	**Fiscal Targets**: ▪ No directionality; flat-lined around zero ▪ In-year underachievement potentially tolerable, but cannot be “structural” in nature
Revenue: ▪ Prudent in the face of recovering economy and unstable outlook ▪ Tax policy and other measures to strengthen growth	**Revenue**: ▪ Prudence is proportional to certainty of economic outlook and support for investments ▪ Policy and other measures to support growth, and to ensure integrity of base revenue
Expense: ▪ Constrained allocations supported by savings targets, compensation freezes, and ongoing transformation ▪ Limited and focused new investments	**Expense**: ▪ Allocations need to reflect cost and demand of current programs, while promoting modernization, transformation and a sustainable cost curve ▪ More room/ flexibility for new investment/ repurpose existing funding
Prudence: ▪ Larger contingency and reserve to help overachieve on fiscal target, and fund future investments /compensation pressures	**Prudence**: ▪ Contingency only there for unforeseen costs ▪ Reserve to be reduced proportional to forecast uncertainty, and/or create room for investment

Fiscal Planning Framework

- Given the government's new fiscal policy framework, the overall in-year tracking, decision-making and approach to the fiscal plan will also need to shift and adjust.
- As new information becomes available, and government plans and priorities continue to evolve and develop in the post-2017 Budget environment, the fiscal planning framework will need to remain anchored in a number of key principles – which may often be in competition or conflict with each other.



Integrating Information Flow and Fiscal Strategy

- The Province's fiscal position – at any point in time – is dependent upon:
  - Information on key drivers of revenue and expense (e.g. economic indicators, spending cost drivers, etc.);
  - Year-to-date flows or assessments of revenue and expense; and
  - Government decisions that impact revenue and/or expense (e.g. TB and Cabinet approvals, federal-provincial agreements, etc.).
- Ensuring evidence-based fiscal decision-making to support the balance of often conflicting priorities is highly dependent on these fiscal information flows, and balancing the relative uncertainty about the implications of that information on expected year-end fiscal positioning to inform spending or other fiscal decisions.
- While government decisions can provide more certainty in terms of impacts on the fiscal plan, information on the revenue forecast generally only becomes most certain towards the end of the fiscal year (December/January). Similarly, while ministries may estimate significant risks early on in the fiscal year, they have tended to be managed down as the year unfolds.
  - As a result, while fiscal information is available on a regular basis, deciding what impact it has on the overall fiscal position of the Province will involve trade-offs and balancing of risk.
  - This is particularly important in the context of the current fiscal year – 2017-18.

Potential Fiscal Building Blocks for 2017-18

- In order to balance the government's fiscal policy and other objectives for the upcoming fiscal year, there are a number of building blocks that can help provide a framework for fiscal planning moving forward.

Fiscal Policy Principle #1: Avoid Deficits But Limit Surpluses

- Landing as close as possible to balanced budgets leaves little flexibility for a significant surplus or deficit by year-end. As such, landing as close to balance as possible needs to be supported by both ***management strategies*** (i.e. in-year expenditure management, program review, and revenue integrity) as well as investment **prioritization plans** for allocating surpluses/fiscal flexibility.
- The approach to maintain balance in 2017–18 will differ from those in the out years.

2017–18 (plan year)

- Fiscal plan projects a surplus of $600 million should all revenue and expense assumptions hold.
  - A rigorous in-year management strategy is under development to help meet underlying fiscal assumptions. The Contingency Fund will not be available for new initiatives.
  - Similarly, an investment prioritization plan, including a list of items to allocate any surplus funds in-year may be required to support the strategic use of those funds (e.g., help address pressures or use in-year flexibility to pull-forward out-year commitments).
  - Consideration could also be given to year-end use of surplus allocation (e.g. 2008 Investing in Ontario Act).

Potential Fiscal Building Blocks for Out Years

2018–19 and beyond (out years)

- Projections for out years become more concrete as PRRT wraps up and planning commences for the 2018 Document process.
- Managing the fiscal architecture for the out years remains more flexible and there is more time to plan for and make adjustments – this can be done through the setting of ministry preliminary allocations in the Fall 2017.
    - At that time, any surplus funds can be set as fiscal room for 2018 Document initiatives; or alternatively, expenditure management strategies can be applied to help ensure targets are met.

Fiscal Policy Principle #2: Support Other Fiscal Anchors

- In addition to maintaining balance, the government has set an interim net debt-to-GDP ratio target of 35 per cent by 2023–24 and 27 per cent by 2029–30. Reporting and monitoring progress on this target will be required.

Potential Fiscal Building Blocks cont'd

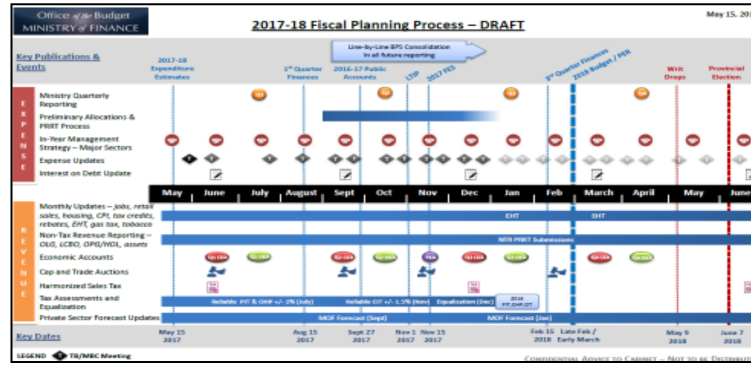
Fiscal Policy Principle #3: Transparent and Credible Fiscal Plan

- The Auditor General is expected to continue to criticize the government over its accounting treatment of net pension assets and potentially other issues.
- In addition, the 2018 Budget will also be a Pre-Election Report, which will be reviewed for reasonableness by the Auditor.
- The FAO is also expected to continue to scrutinize the province's plan to maintain balance, suggesting instead, that the province will remain in deficit over the outlook.
- Accounting changes will take effect after the release of the 2016–17 Public Accounts, reflecting the revenues and expenses of BPS organizations on a line by line basis. Though the change will be fiscally neutral, it may impact growth rates and make year-over-year comparisons more challenging.

Tools to Guide Fiscal Policy Decision-Making

1. *Gantt Chart*

- Used to educate decision-makers about the key sources of fiscal information inputs, the timing of information flows, major milestones in reporting, and other key events that will be important from a fiscal planning perspective.



2. *Fiscal Tracker*

- Placemat will be used to prepare regular updates on the fiscal plan, including:
    - a) Revenue Updates
    - b) Key Expense Approvals
    - c) Economic Indicators
    - d) Status of Key Fiscal Targets
    - e) Status of Capital Projects
    - f) Status of Federal Agreements
    - g) Status of Ontario's Borrowing Program
    - h) Key Risks to the Fiscal Plan