Ontario Fall Update Affirms Guidance of Balanced Budgets Ahead

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CIBC Capital Markets
Macro Strategy

Ontario Fall Update Affirms Guidance of Balanced Budgets Ahead
November 14, 2017

Credit Implications: Neutral

Credit Ratings: DBRS AA (low), Moody's Aa2, S&P A+, Fitch AA-, All Outlooks Stable

Ontario's fall fiscal update reaffirmed guidance on balanced budgets ahead, after taking into account a provision for a $500mln forecast reserve in both 2017/18 and 2018/19, which increases to $800mln in 2019/20. The flat budget projection is unchanged from the spring budget, but the forecast reserves have been trimmed by $100mln in each year.

Highlights:

- Ontario's Ministry of Finance is forecasting real GDP growth of 2.8% in 2017, much higher than the 2017 Budget assumption of 2.3%.
- Total revenue in 2017/18 is projected to be $150.1bln, up $8.4bln from the budget estimate. The revenue projection thereafter is also higher than budget.
- Total expense in 2017/18 is projected to be $149.6bln, up $8.5bln from the budget estimate. The expense projection thereafter is also higher than budget.
- Combining the reduction in the forecast reserve with higher revenue and expense projections, the final deficit projection nets out to $0 throughout the forecast horizon to 2019/20.
- Ontario's long-term borrowing requirements in the current fiscal year will decline by $600mln to $25.8bln, due mainly to higher pre-borrowing from fiscal 2016/17. Projected borrowings in fiscal 2018/19 and 2019/20 are expected to step-up to $32.2bln and $37.8bln, respectively, unchanged from Budget 2017.
- The net debt-to-GDP ratio is projected to be 37.3% in 2017/18, down from the 37.5% forecast in the 2017 Budget.
- The Province intends to fulfil its commitment to increase the minimum wage to $15 per hour on January 1, 2019, as well as lower the small business tax rate by 1% to 3.5% on January 1, 2018.

Notwithstanding the return to balance after a decade of deficits, we highlight that future audited financial results will be subject to a qualified opinion due to the accounting of the Province's pension plans, as well as the Ontario Fair Hydro Plan.*

We also highlight that Ontario has a formidable capital program that will require debt funding. As presented in the 2017 Budget, Ontario's capital program is projected to total $190bln over a 13-year period that started in 2014/15. Funding for the program will factor in the implications of both the Federal and Provincial climate change plans, Federal funding and infrastructure needs. The latter will need to take into account renewal, replacement and growth. The particulars of all these aforementioned factors continue to evolve. For example, earlier this year, the Federal government announced that it will fund 43% of the Province's $4.4bln upgrades to the GO Transit Regional Express Rail. The Province had previously committed to funding 100%.

The Hydro One privatization strategy, which is largely concluded, has been a means to fund part of Ontario's capital program. For more information on the Hydro One privatization, please see our note "Ontario Sells Final Stake in Hydro One" Click Here

Overall, we consider today's announcement to be neutral ahead of next year's election that is scheduled for June 7, 2018. Post the election, however, we believe that should the Province continue on its current path of balanced budgets and achieve meaningful debt reduction, its improving fiscal performance will be rewarded by S&P. The rating agency downgraded the Province to A+ from AA- in 2015 on concerns about its high and rising debt burden. In Ontario's spring budget, the government announced an interim debt target of 35% (debt/GDP) by 2023/24, with the ultimate goal of bringing the debt ratio back to its pre-recession level of 27% by 2029/30. The debt ratio is currently around 37%.

S&P Ratings Scorecard: Province of Ontario	
Date	Jun-15-2017
Rating	A+
Outlook	Stable
Institutional Framework	Very predictable and well-balanced
Economy	Very strong
Financial Management	Strong
Budgetary Flexibility	Average
Budgetary Performance	Weak
Liquidity	Adequate
Debt Burden	Very high
Contingent Liabilities	Low

Source: S&P

*For more information on the pension and fair hydro plan issues, please see our research note "Expert advisory panel agrees with Ontario in pension accounting issue" Click Here as well as our note on "Auditor General Opines on Ontario Fair Hydro Plan" Click Here .

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