RE: FAO Economic and Fiscal Outlook - May 31

From: "Bevan, Andrew (OPO)" <"/o=govon/ou=exchange administrative group (fydibohf23spdlt)/cn=recipients/cn=bevan, andrewf93">
To: "Forgione, Andrew (OPO)" <andrew.forgione@ontario.ca>, "MacKenzie, Rebecca (OPO)" <rebecca.mackenzie@ontario.ca>, "Killorn, Bill (OPO)" <bill.killorn@ontario.ca>, "McEachern, Gillian (OPO)" <gillian.mceachern@ontario.ca>
Cc: "McPhail, Blane (OPO)" <blane.mcphail@ontario.ca>
Date: Tue, 30 May 2017 17:59:09 -0400

Good, thanks

From: Forgione, Andrew (OPO)
Sent: May-30-17 5:55 PM
To: Bevan, Andrew (OPO); MacKenzie, Rebecca (OPO); Killorn, Bill (OPO); McEachern, Gillian (OPO)
Cc: McPhail, Blane (OPO)
Subject: RE: FAO Economic and Fiscal Outlook - May 31

Andrew – below is our draft messaging for tomorrow's avail, if the Premier is asked. Minister Sousa is currently viewing a draft statement, so once I receive it back from Finance I will share here as well.

General

- I appreciate the work of the Financial Accountability Officer.
- I'm pleased to see his economic forecasts are broadly in line with ours – showing strong economic momentum in 2017 and 2018, and confirming strong job gains.
- His analysis is also in line with major Canadian banks and financial institutions, who predict Ontario will continue to lead Canada in economic growth.
- Our unemployment rate is the lowest it has been in 16 years and has been below the national average for the last 2 years.
- We thank the FAO for his analysis and look forward to our continued work with his office.

Deficit

- This year, we were pleased to announce the first balanced budget in a decade, and we committed to having balanced budgets through to 2020.
- This allows us to invest in education, healthcare and infrastructure, while also being fiscally responsible.
- We have stated time and time again: we will be balancing the budget this year and in the years that follow, and we remain confident in our commitment.

On Auditor General & Pension Assets

- When we received advice from officials that varied from that of the Auditor General, we asked an independent expert panel to determine the accounting treatment of the pension assets.

- The Panel was composed of four highly qualified individuals:
  - **Tricia O'Malley** → former Chair of the Canadian Accounting Standards Board and member of the International.
  - **Murray Gold** → leading expert in jointly trusted pension and benefits plans across Canada on best practices, senior pension and benefits partner at Koskie Minsky LLP.
  - **Uros Karadzic** → partner at Ernst and Young (EY) as a pension actuary, and has extensive experience in accounting for benefit plan obligations.
  - **Paul Martin** → A comptroller with the Government of New Brunswick with significant experience in Public Accounting Standards.
- In February, the Panel released its independent advice and recommended that the net pension assets for two jointly sponsored plans be recognized in the province's financial statements.
- This aligns with the treatment originally included in the 2016 Budget plan, and is consistent with how accounting standards have been applied to these plans since 2001.

From: Bevan, Andrew (OPO)
Sent: May-30-17 8:27 AM
To: Forgione, Andrew (OPO); MacKenzie, Rebecca (OPO); Killorn, Bill (OPO); McEachern, Gillian (OPO)
Cc: McPhail, Blane (OPO)
Subject: RE: FAO Economic and Fiscal Outlook - May 31

- Thx. Shd give more detail about panel members here pls: When we received advice from officials that varied from that of the Auditor General, we asked an independent expert panel to determine the accounting treatment of the pension assets.

From: Forgione, Andrew (OPO)
Sent: May-30-17 8:23 AM
To: Bevan, Andrew (OPO); MacKenzie, Rebecca (OPO); Killorn, Bill (OPO); McEachern, Gillian (OPO)
Cc: McPhail, Blane (OPO)
Subject: FAO Economic and Fiscal Outlook - May 31
Importance: High

Hi – the FAO will be releasing his economic and fiscal outlook tomorrow at 9 AM.

Below is a brief summary as well as key messages. We are working with Sousa's office to draft up a strong statement in response to the report as it has some critical language about the deficit and debt (he takes the AG's accounting treatment in his projections).

Bill is bringing a copy of the report to snr staff.

Report Summary: FAO Economic and Fiscal Update

Fiscal Position

- The primary conclusion is that the FAO is projecting **continued Ontario budget deficits** over the next 5 years.
- Under the government's accounting presentation, the FAO projects that a balanced budget is within the government's reach in 2017-18. Beyond 2017-18, the deficit is projected to deteriorate steadily due to rising expenses and moderate revenue growth. On this basis, staying in balance after 2017-18 will likely require additional fiscal policy measures.
- This presentation of Ontario's fiscal position would be expected to receive a qualified opinion from the Auditor General when published in the Province's 2016-17 Public Accounts.
- The FAO also takes the Auditor General's accounting treatment of the pension assets, so projects significant deficits over the entire fiscal outlook.
- Positive Quote:
    - "The FAO projects that a balanced budget is within the government's reach in 2017-18". P. 1

Economic Growth

- The FAO's economic outlook expects the recent strength of the Ontario economy to continue into 2017. The FAO is forecasting solid growth in real GDP of 2.4 per cent in 2017, moderating to an average annual pace of 2.0 per cent over the following four years. The FAO's economic forecast is broadly in-line with that presented in the government's 2017 Budget.
- However, there are significant risks that could result in weaker than expected economic growth for Ontario. In particular, the policy direction of the new U.S. administration remains uncertain. This could hamper business investment and Ontario's economic prospects.
- Domestically, Ontario's surging housing market continues to be the largest risk for the economy. A sharp correction in housing prices could reverberate beyond the housing market and lead to broader, economy-wide impacts
- Positive Quotes:
    - "The FAO's economic outlook expects the recent strength of the Ontario economy to continue into 2017" p. 2
    - Supported by the strong economic momentum in 2016 and continued improvement in economic indicators in the first quarter of 2017, the FAO is projecting real GDP to rise by 2.4 per cent in 2017 and 2.1 per cent in 2018.
        - Nominal GDP – the broadest measure of the tax base – increased by a robust 4.6 per cent in 2016. The FAO is projecting nominal GDP to increase by 4.1 per cent in 2017 and 4.2 per cent in 2018, reflecting solid gains in labour income and corporate profits

- o “Ontario experienced relatively strong employment growth of 1.1 per cent in 2016 (+76,400 net new jobs), the majority of which were full-time, private sector jobs.” P. 11
- o There was robust job growth in both goods and service producing industries. The construction industry in particular, posted the highest job growth (+3.4 per cent), followed by healthcare (+3.2 per cent).
- o The strength in Ontario’s labour market continued into 2017 with an increase of 99,600 jobs on a year-over-year basis during the first quarter. For the year, the consistent with the outlook for solid economic growth. P. 11
- o The net operating surplus of corporations (largely corporate profits) also increased by a robust 9.2 per cent in 2016 following an equally strong gain of 9.1 per cent in 2015.

Revenue

- Given Ontario’s recent economic strength relative to the rest of Canada, the Province’s Equalization entitlement declined $0.8 billion to $1.4 billion in 2017-18. The FAO is projecting a further drop to $0.6 billion in 2018-19.
- FAO expects revenue will increases by 3.3% per year on average over the outlook.
- The FAO also discusses one-time increases to revenue and lists federal infrastructure transfers, increased sales and rentals revenue as well as asset sales as well as cap and trade proceeds.

Expenses

- The expense outlook includes significant new spending across all sectors, including a new children and youth Pharmacare program, higher operating funding for hospitals, 24,000 new child care spaces.

Debt

- As a result, the FAO projects Ontario’s net debt to increase by $76 billion over the next five years to approximately $392 billion by 2021-22 based on the FAO’s application of the AG’s recommended accounting presentation.
- Based on the AG’s recommended accounting presentation, the FAO expects Ontario’s net debt-to-GDP ratio will edge higher to 40.3 per cent by 2021-22, reflecting the projected increase in net debt and the FAO’s forecast for nominal GDP growth. In contrast, based on the accounting presentation adopted by the government, the FAO projects that net debt-to-GDP will fall slightly from 38.6 per cent in 2015-16 to 37.5 per cent by 2021-22.
- In the 2017 Budget, the Province set an interim net debt-to-GDP target of 35 per cent by 2023-24 and committed to lowering the ratio to 27 per cent by 2029-30. The FAO’s net debt-to-GDP projections under both accounting presentations, suggest that additional fiscal measures would be required for the government to achieve its interim target of 35 per cent by 2023-24.

Risks to the Fiscal Plan

- A sharp correction in the housing market could present a significant risk for both the broader economy and for the Province’s fiscal plan.
- A decline in house prices and housing market activity would directly reduce Land Transfer Tax and HST revenues. In addition, the broader economic impacts would lower personal and corporate income tax revenues.
- In the 2017 Budget, the government significantly reduced the prudence built into its program spending projection compared to the 2016 Budget, leaving less fiscal flexibility for the government to respond to unexpected events.

- In addition, the FAO projects that interest on debt payments as a share of both program spending and revenue will increase significantly, exposing the government to added fiscal risk should interest rates rise faster than expected.
- The FAO also includes a background on the Accounting Treatment of Jointly Sponsored Pension plans in Ontario where he outlines the government's position compared to the AG's.

Key Messages

Balancing the Budget

- **We have stated time and time again, we will be balancing the budget this year and in the years that follow**
- **A balanced budget means that the government will no longer need to borrow to pay for its ongoing operating costs.**
- **The result: more money to invest in health care, education and other public services that matter to the people of Ontario.**
- **We know that a strong economy, together with a balanced budget is positioning Ontario for long-term fiscal sustainability.**
- **The benefits of a balanced budget and strengthening economy are already giving the government the fiscal flexibility to do more to help Ontarians.**

Debt

- When the global economic recession hit we made a deliberate choice to invest in our economy while protecting vital public services like health care and education.
- We also set out a realistic and responsible approach to return to balance by 17-18, and in the coming weeks, our government will deliver on its commitment to balance the budget.
- This approach has enabled us to balance while making the largest infrastructure investment in Ontario's history – $190 billion over 13 years.
- We are building schools, hospitals and transit, creating jobs and strengthening our communities.
- These are smart investments. For every dollar invested in infrastructure today, real GDP can increase by nearly $6 in the long term.
- We also know that when we invest in infrastructure, private sector investment increases, businesses are more productive, and real wages rise.

Economy

- Outpaced Canada's and all other G7 countries for the last 3 years.
- 689,400 net new jobs since the recession
  - Majority are in the private sector and in above wage industries; about 95% are full-time
  - Unemployment rate is 5.8 % -lowest it has been in 16 years
- Below the national unemployment rate (6.5%) for over 2 years in a row.
- Canadians are moving to Ontario at the fastest rate in 29 years.

Accounting Treatment of Pension Assets

- When we received advice from officials that varied from that of the Auditor General, we asked an independent expert panel to determine the accounting treatment of the pension assets.
- The Panel released its independent advice and recommended that the net pension assets for two jointly sponsored be recognized in the province's financial statements.
- This aligns with the treatment originally included in the 2016 Budget plan, and is consistent with how accounting standards have been applied to these plans since 2001.

Asset Optimization

- Let's be clear. Ontario has restored balance through targeted, measured and fiscally responsible decisions to manage program spending and foster job creation and economic growth.
- We have said, time and time again, by law, net proceeds will be dedicated to the Trillium Trust to help fund infrastructure projects that will help create jobs and strengthen the province's economy.
- By broadening ownership of Hydro One, we have exceeded our target of $9 billion, supporting investments in transit and infrastructure in communities across the province.
- Ontario will be able to invest in vital public infrastructure renewal without corresponding increase in debt, deficit or cuts to other programs or services.
- For the people of Ontario, this means investments in transit include Moving Ontario Forward's GO Transit Regional Express Rail, the Hurontario LRT as well as road and bridge upgrades in rural and northern communities through the Ontario Community Infrastructure Fund.
- This is part of our plan to invest more than $190 billion in public infrastructure over 13 years, for priority projects like roads, bridges, public transit, hospitals and schools.