FAO’s 2017 Fall Economic and Fiscal Outlook

ISSUE

On Monday Dec 11th, 2017 the Financial Accountability Office will release its ‘Fall Economic and Fiscal Outlook’ report. This note is a summary.

TOP MESSAGES

- I would like to thank the Financial Accountability Officer (FAO) for releasing his fall economic and fiscal outlook for Ontario. We value the FAO’s independent assessment and projections of the province’s fiscal plan.
- The government is committed to a responsible fiscal plan that provides the conditions for all Ontarians to thrive.
- As outlined in the 2017 Ontario Economic Outlook and Fiscal Review, the government is projecting a balanced budget for 2017–18 and continued balance in 2018–19 and 2019–20.
- The FAO report also projects a balanced budget for Ontario this year.
- The government has a strong track record of beating its fiscal targets. In fact, the Public Accounts of Ontario reported that the 2016–17 deficit was $1.0 billion, beating our annual deficit target again, for the eighth year in a row.
- The 2017 Ontario Economic Outlook and Fiscal Review builds on the government’s track record of fiscal management that has resulted in $29 billion in accumulated deficits being avoided over the past seven years, relative to the 2010 Budget forecast.
- We are also targeting a net debt-to-GDP ratio of 35 per cent by 2023–24 and reducing Ontario’s net debt-to-GDP ratio to its pre-recession level of 27 per cent, with current projections showing that this will be achieved by 2029–30.
- Since 2014, Ontario’s real GDP growth has strengthened, positioning Ontario as a growth leader, not only in Canada, but among G7 countries. In fact, over the 2014-17 period, Ontario’s real GDP growth is on pace to exceed that of all G7 countries.
- Private-sector economists are projecting continued growth for Ontario over the forecast horizon; the FAO’s real GDP projections are aligned with the 2017 Fall Economic Statement over the 2017 to 2020 period.
- This shows that our plan to make strategic investments in Ontario to grow the economy is working.
- A balanced budget is providing the Province the fiscal flexibility to invest more in health care, education, support for seniors and small businesses and other public services that matter most to Ontario families. A balanced budget also adds stability to Ontario’s finances and positions the government to better respond to demographic challenges and unexpected global economic shocks that the province will face over the next decade.
- We will continue moving forward on our fiscally responsible plan that creates fairness and opportunity for all Ontarians.

KEY POINTS

Economic Outlook

- The FAO has raised its forecast for Ontario economic growth in 2017 from its spring outlook report. However, despite this upward revision, the FAO forecast is at the bottom of the current range of the MOF survey of private sector forecasts for both real and nominal GDP growth in 2017.
- Beyond 2017, the FAO forecast anticipates growth to moderate as the housing market and consumer spending cool alongside gradually rising interest rates, in line with the FES forecast.
- Over the 2017 to 2020 period, the FAO's forecast for average annual real GDP growth of 2.2 per cent is the same as the 2017 FES outlook.
- However, for nominal GDP growth, the FAO's average annual forecast of 4.2 per cent over the 2017 to 2020 period is slower than the FES projection of 4.4 per cent growth. This difference is explained by a much lower FAO nominal GDP forecast in 2017 compared to the FES (4.7 per cent vs 5.3 per cent).
- The FAO forecast takes into account its estimate of the impact of the new minimum wage legislation, which is expected to boost wage growth over the forecast, but temper employment gains. Even with these employment impacts, the FAO predicts a modest decline in the unemployment rate.

Fiscal Outlook

- The FAO is projecting a budget deficit of $4.0 billion in 2017–18 using the **Auditor General's recommended accounting treatment for both the Fair Hydro Plan and the net pension assets of jointly sponsored pension plans.** In the absence of any fiscal policy changes the deficit grows steadily to $9.8 billion in 2021-22.
- Under the **government's accounting presentation (excluding the AG's recommendations)**, the FAO projects a small surplus for 2017–18 of $0.2 billion (excluding the reserve) and a return to deficits beyond 2017–18 driven by revenue factors - loss of temporary revenues combined with more moderate tax revenue growth.
- The FAO suggests that by not adopting the AG's recommended accounting presentation, the 2017 Budget and the 2017 FES have reduced transparency and clarity of Ontario's fiscal position and Ontario will continue to receive qualified opinions from the AG on its Pubic Accounts.

Budget Balance - FAO's Fiscal Outlook ($ Billions)	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
AG Presentation	-5.0	-2.4	-4.0	-7.1	-7.8	-9.0	-9.8
Government Presentation	-3.5	-1.0	0.2	-1.9	-1.9	-2.6	-3.7
2017 FES -- Excluding Reserve	-3.5	-1.0	0.5	0.5	0.8	N/A	N/A

Revenue Outlook

- The FAO is projecting average annual revenue growth of 3.2 per cent from 2016-17 to 2019-20 as compared with the government's projections of 4.0 per cent. The main drivers are:
  - The FAO projections for taxation revenues are $2.9 billion lower by 2019-20 than the projections in the 2017 FES due to lower projected growth in household spending, labour income and corporate profits.
  - In addition, the FAO continues to highlight a number of one-time 2017-18 revenues, including: increase to sales and rentals from sale of final tranche of H1, higher federal transfers for infrastructure (PTIF), a one-time boost from extra Cap and Trade auction. Taken together the FAO estimates that these amount to $4.5 billion in additional one-time revenues in 2017-18.

Expense Outlook

- From 2017–18 to 2019–20 the FAO's outlook adopts the government's 2017 FES projections for program spending, **adjusted to reflect the AG's recommended accounting presentation.**
  - Both the Fair Hydro Plan and net pension asset adjustment impact the expense side with a combined impact of approximately $4.2 billion in 2017-18.
- The FAO notes that in 2018-19 and 2019-20, increases in program spending will be restrained to an average of 2.4 percent, below the growth in underlying spending pressures. Beyond 2019–20 the FAO projects program spending will grow faster -- at an average annual rate of 4.2 per cent – due to population pressures.

Borrowing and Net Debt

- Using the **government's accounting presentation** net debt-to-GDP is expected to reach 38.5 per cent by 2019–20 and 38.7 per cent by 2021–22. This increases to 41.4 per cent by 2021–22 **under the AG's accounting presentation for jointly sponsored pension plans and the Fair Hydro Plan**.
  - The 2017 FES projected a net debt-to-GDP ratio of 37.0 per cent by 2019–20.

Comparison: 2017 Fall Economic Statement and the 2017 Fall FAO Fiscal Outlook

$ Billions	Actual		Outlook					Avg. Annual Growth		
	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	16-17 to 19-20	19-20 to 21-22	16-17 to 21-22
2017 Fall Economic Statement										
Taxation Revenue	91.8	94.3	99.9	105.1	110.0			5.2%		
Transfers from Gov't of Canada	23.1	24.5	26.2	26.0	25.4			1.2%		
Income from GBEs	4.9	5.6	5.1	5.9	6.2			3.7%		
Other Non-Tax Revenue	16.3	16.3	19.0	16.5	16.6			0.7%		
Total Revenue	136.1	140.7	150.1	153.6	158.2			4.0%		
Expense										
Program Expense	128.1	130.0	137.4	140.4	144.2			3.5%		
Adjustment for Pension Assets	-	-	-	-	-					
Adjustment for Fair Hydro Plan	-	-	-	-	-					
Interest on Debt	11.6	11.7	12.2	12.7	13.3			4.2%		
Total Expense	139.7	141.7	149.6	153.1	157.4			3.6%		
Surplus/(Deficit)	**(3.5)**	**(1.0)**	**0.5**	**0.5**	**0.8**					
Net Debt	295.4	301.6	311.7	323.0	335.6			3.6%		
Change - 2017 Fall Economic Statement to 2017 Fall FAO Fiscal Outlook										
Taxation Revenue	-	-	-1.2	-2.4	-2.9					
Transfers from Gov't of Canada	-	-	0.0	-0.5	-0.4					
Income from GBEs	-	-	0.0	0.0	0.0					
Other Non-Tax Revenue	-	-	0.4	0.0	0.0					
Total Revenue	-	-	(0.7)	(2.9)	(3.4)					
Expense										
Program Expense	-	-	-	-	-					
Adjustment for Pension Assets	1.5	1.5	2.3	2.6	2.9					
Adjustment for Fair Hydro Plan	-	-	1.9	2.7	2.9					
Interest on Debt	-	-	*(0.4)*	*(0.6)*	*(0.7)*					
Total Expense	*1.5*	*1.5*	*3.8*	*4.7*	*5.2*					
Surplus/(Deficit) AG Presentation	***(1.5)***	***(1.4)***	***(4.5)***	***(7.6)***	***(8.6)***					
Surplus/(Deficit) - Gov't Presentation (excl. Fair Hydro Pension Adj.)	***(0.0)***	***(0.0)***	***(0.3)***	***(2.4)***	***(2.7)***					
Net Debt	*11.0*	*12.5*	*17.5*	*24.7*	*32.4*					
2017 Fall FAO Fiscal Outlook										
Taxation Revenue	91.8	94.3	98.7	102.7	107.0	111.3	115.8	4.3%	4.0%	4.2%
Transfers from Gov't of Canada	23.1	24.5	26.2	25.5	25.0	25.8	26.6	0.7%	3.2%	1.7%
Income from GBEs	4.9	5.6	5.1	5.9	6.2	6.5	6.7	3.5%	4.0%	3.7%
Other Non-Tax Revenue	16.3	16.3	19.4	16.5	16.6	17.3	18.0	0.6%	4.1%	2.0%
Total Revenue	136.1	140.7	149.4	150.7	154.8	160.8	167.0	3.2%	3.9%	3.5%
Expense										
Program Expense	128.1	130.0	137.4	140.4	144.2	150.2	156.9	3.5%	4.3%	3.8%
Adjustment for Pension Assets	1.5	1.5	2.3	2.6	2.9	2.9	2.9			
Adjustment for Fair Hydro Plan	-	-	1.9	2.7	2.9	3.4	3.2			
Interest on Debt	11.6	11.7	11.8	12.1	12.6	13.2	13.8	2.5%	4.7%	3.4%
Total Expense	141.2	143.2	153.4	157.8	162.6	169.8	176.8	4.3%	4.3%	4.3%
Surplus/(Deficit) AG Presentation	**(5.0)**	**(2.4)**	**(4.0)**	**(7.1)**	**(7.8)**	**(9.0)**	**(9.8)**			
Surplus/(Deficit) - Gov't Presentation (excl. Fair Hydro Pension Adj.)	**(3.5)**	**(1.0)**	**0.2**	**(1.9)**	**(1.9)**	**(2.6)**	**(3.7)**			
Net Debt	306.4	314.1	329.2	347.7	368.0	386.8	404.4	5.4%	4.8%	5.2%

Note: All surplus/deficits exlcude the reserve. Numbers may not add due to rounding.

Economic Assumptions: FAO vs FES

Real GDP	**2017**	**2018**	**2019**	**2020**	**2017-20 average**
FAO - Fall 2017	2.8	2.1	2.0	1.9	2.2
FES 2017	2.8	2.1	2.0	2.0	2.2
Nominal GDP					
FAO - Fall 2017	4.7	4.1	4.1	4.1	4.2
FES 2017	5.3	4.1	4.1	4.2	4.4
Labour income					
FAO - Fall 2017	4.0	4.5	4.3	4.1	4.2
FES 2017	4.3	4.7	4.8	4.4	4.6
Corporate profits					
FAO - Fall 2017	11.7	2.2	3.7	4.4	5.5
FES 2017	16.1	2.9	2.8	3.7	6.4
Household consumption*					
FAO - Fall 2017	4.7	4.2	4.1	3.9	4.2
FES 2017	5.1	4.3	4.3	4.3	4.5

* Real household consumption plus CPI