

Manitoba: 2020–21 Budget

ROOM TO STIMULATE IN A HIGHLY UNCERTAIN ENVIRONMENT

SUMMARY

- Manitoba's budget (*Budget*) for fiscal year 2020–21 (FY21), was released yesterday following a weeklong legislative delay and significant escalation of the COVID-19 pandemic.
- A significantly weaker global economic outlook means that most of *Budget's* projections are now out of date; still, the plan provides some insight into Manitoba's potential policy responses.
- Recent outperformance on the fiscal balance has provided some near-term flexibility to respond to a further deterioration in the outlook.
- As the extent and impact of the crisis evolves, flexibility in its path to balance will likely be warranted.

OUR TAKE

The fruits of Manitoba's past efforts to rein in spending and manage debt levels are on display in this plan, and give the Province some firepower to address the forthcoming economic downturn. Its tax-supported debt levels were high and growing unsustainably as a result of running chronic structural deficits. The Government has made better-than-anticipated progress so far in adhering to its consolidation efforts against a proposed path that is gradual in the context of moderate economic activity. That has given it room to boost infrastructure spending, set aside funds for contingency, and provide tax relief.

However, a deteriorating outlook related to COVID-19 will clearly put the current path under pressure. Timing has precluded the Government from incorporating more significant downside from the pandemic into its fiscal plan. We expect a significant deterioration in economic activity across Canada in the near term that will result in significantly lower growth for provinces including Manitoba in 2020. This will have an impact on the government fiscal affairs in the near term relative to Budget that will no doubt require adjustments as the situation evolves

Nevertheless, measures in *Budget* will provide some support in the near term to varying degrees. The rainy day fund offers flexibility for a range of targeted policy levers to address public cost pressures or softer growth related to the virus. On the margin, payroll tax reductions should provide modest support in a weaker economic environment and complement federal measures. The new sales tax cut will also likely have only a minimal effect in the near term, as COVID-19-related reductions in consumer activity are more likely to be induced by fear than by cost. It may help to offset surge pricing for in-demand goods and services.

It should be noted that neither of the signature tax measures were designed as emergency values; rather, they are permanent adjustments that will erode revenues in the longer term. Otherwise, emergency funding and fiscal stimulus from Ottawa may help to alleviate downward pressure on economic growth and Provincial coffers, but the Government should be ready to step in again.

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Updated Fiscal Forecast

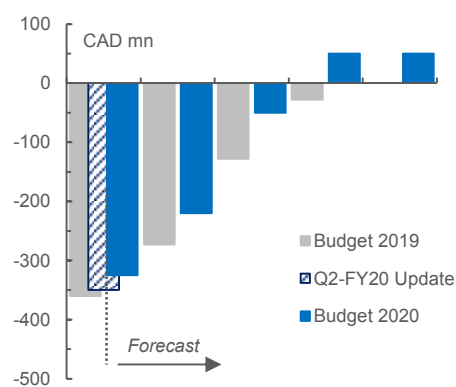
\$ millions except where noted

	FY20		FY21
	Q2	Bud.	Bud.
Own-Source Revenue	11,424	11,569	11,854
Gov. Enterprise Net Inc.	839	863	747
Federal Transfers	4,832	4,841	5,136
Total Revenue	17,095	17,273	17,737
Program Spending	16,352	16,575	16,956
Debt Servicing	1,043	1,023	1,001
Total Expenditure	17,395	17,598	17,957
Contingency for Writedown	50	—	—
In-Year Adjustment/Lapse	—	—	—
Budget Balance	-350	-325	-220
Net Debt	25,799	25,667	26,436
Memo Items, % of GDP			
Bud. Balance	-0.5	-0.4	-0.3
Own-Source Revenue	15.3	15.5	15.3
Program Spending	23.3	23.5	23.2
Net Debt	34.5	34.3	34.2
Debt Service / Revenue	6.1	5.9	5.6

Sources: Scotiabank Economics, Manitoba Finance.

Chart 1

Manitoba's Budget Balances



Sources: Scotiabank Economics, Manitoba Finance.

ECONOMIC OUTLOOK

Manitoba's fiscal plan is based on an outlook firmly rooted in pre-COVID-19 conditions. Real GDP is expected to accelerate from 1.1% in 2019 to 1.5% in 2021. The Province suspects that the global industrial sector slowdown that dominated headlines last year had been bottoming out, and also anticipates that tax changes—notably reductions in the retail sales tax rate—will also support growth. The Government noted that Manitoba's diversified industrial base and geographical export profile have contributed to its historical resilience to economic downturns. A weaker Chinese expansion and potential supply chain disruptions vis-a-vis COVID-19 are listed as a downside risk to the global economy, though *Budget's* base case forecast assumes 5.8% real GDP gains in China this year.

The Province also provided some details of its plan to create 40,000 new jobs in the next four years. Measures in the plan include strategic infrastructure outlays of \$1.8 bn in FY21—more than the minimum mandated \$1 bn per year—energy efficient building retrofits, previously announced tax cuts, and further use of the Provincial Nominee Program to attract skilled immigrants.

BASELINE FISCAL PLAN DETAILS

Budget largely adheres to its plan to balance its books by FY23. The Province plans to gradually erode deficit spending in the next two years—with \$220 mn and \$50 mn deficits in FY21 and FY22 respectively—before posting a surplus of \$50 mn in FY23. That would be the first surplus position since FY08, and the government intends to maintain it thereafter (chart 1, p.1). Meanwhile, a smaller-than-previously anticipated deficit is forecast for FY20 at \$325 mn on \$17.6 bn in expenditures. The \$35 mn in savings relative to the prior plan largely stems from resilience in revenue performance. FY20–23 improvements in balances relative to forecasts in last year's *Public Accounts* amount to \$111 mn.

Budget modestly rebalances its revenue mix. The second reduction in the retail sales tax under the Government's renewed mandate will erode revenues with an estimated annual loss of \$243 mn in FY21. The payroll tax cut for small businesses announced days before *Budget* will reduce corporate receipts by a smaller \$2.2 mn in the upcoming fiscal year, as the new Green Levy replacing the federal carbon tax lifts receipts by \$218 mn. Overall own-source revenues are expected to grow by 2.5% in FY21, which is somewhat more modest than peers that have resisted tax cuts, but on balance, the composition shift is positive. It effectively replaces part of the consumption tax with a 'greener' version of a consumption tax, and lower labour taxes that should underpin employment at a time when the outlook is weakening.

Offsetting revenue measures should also be credit-positive. S&P had raised its outlook for Manitoba last October—from stable to positive—in light of its strengthened fiscal performance, indicating the potential for another notch-upgrade would be predicated on sustaining this positive fiscal momentum. Slowing economic growth will restrict the Government's flexibility in this regard.

Otherwise, expenditure restraint will continue to drive consolidation efforts. Following the 2.5% growth in total spending estimated for FY20, further restraint is projected with average annual growth around 1.6% during FY21–24 (chart 2). That level of restraint will likely be challenging, especially as a weakened growth outlook adds pressure on revenues and triggers automatic stabilizers.

Chart 2

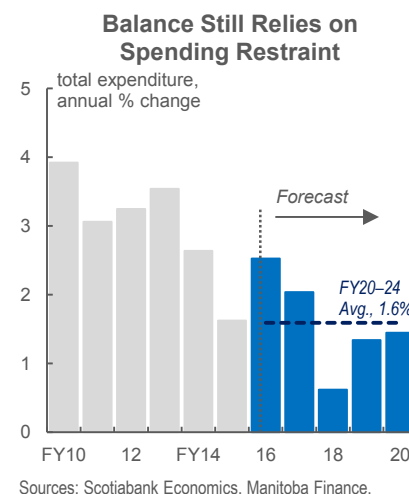


Chart 3

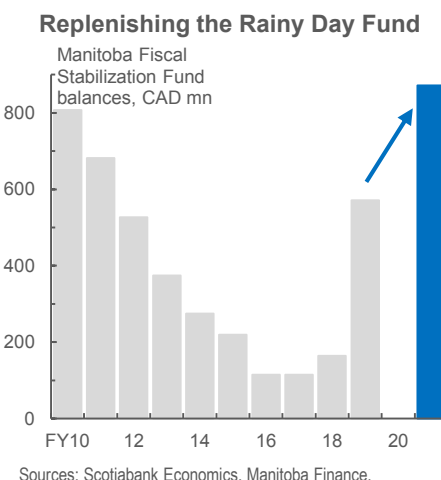
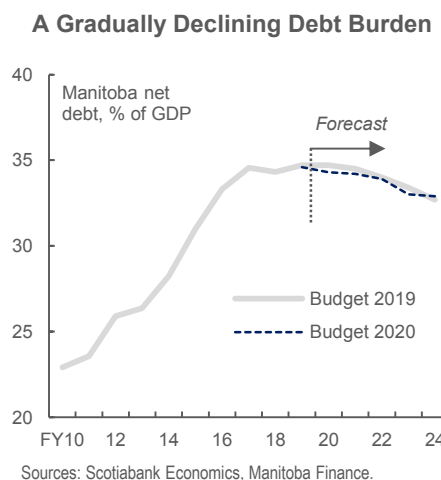


Chart 4



KEY POLICY MEASURES

Budget's signature policy measures were concentrated in tax relief, which the Government framed as part of its response to the adverse impacts of COVID-19 spread and containment efforts. A further 1 ppt reduction in the provincial sales tax rate to 6% takes effect July 1st, 2020. That builds on a similar cut last year and will be paid for predominantly by proceeds from the Province's carbon pricing scheme. The Government will also increase the minimum payroll thresholds for the existing Health and Post Secondary Education Tax Levy imposed on wages paid by employers. The move is expected to reduce the tax burden on 1,000 employers in Manitoba.

Alongside tax relief, Budget emphasized past efforts to increase the size of its rainy day fund, which is ready to be deployed should a severe economic downturn materialize. Deposits in the fund rose from about \$114 mn in FY16 to nearly \$600 mn by end-FY19. During FY20–21, the Government intends to deposit another \$300 mn (chart 3, p.2,) with the reserves expected to be fully funded by end-FY21. The Province also announced last week that it will allocate \$35 mn for personal protective supplies—such as gloves, face masks and shields—for health-care workers and patients.

DEBT AND BORROWING

Net debt is expected to rise by \$769 mn to reach \$26.4 bn in FY21. That figure is forecast to amount to 34.2% of nominal GDP, a 0.1 ppt decline from the projection for FY20. The Province is targeting further modest reductions in its debt burden throughout the forecast horizon, which it expects to culminate in a 32.9% net debt-to-GDP ratio in FY24—in line with last year's forecast (chart 4, p.2). For the moment, Manitoba's forecast debt burden puts it in the middle of the pack—outweighing those in BC, Alberta, Saskatchewan, and Prince Edward Island throughout the forecast window, and on track to creep ahead of Nova Scotia in FY23.

Also on this front, the Government noted that new standards on Asset Retirement Obligations will come into effect in 2021, with details to be announced in next year's fiscal plan. This will put upward pressure on Manitoba's debt-to-GDP ratio—as in other jurisdictions when similar rules are adopted—relative to the current baseline, but the Province intends to maintain a downward debt path.

FY21 borrowing requirements are expected to total \$5.6 bn. Of that amount, \$3.7 billion will be used for refinancing purposes. Net of projected repayments, new cash requirements are forecast at \$1.9 bn. As of Budget's release, pre-funding of \$476 mn had been completed for the coming fiscal year.

Manitoba's Borrowing Requirements						
(millions of dollars)						
	Refinancing	New Cash Req.'s	Est. Repmt.'s	Gross Borr. Req.'s	Pre-Funding	Borr. Req.'s
<u>Government Business Enterprises</u>						
MB Hydro-Electric Board	1,529	1,100	-	2,629	-	2,629
MB Liquor and Lotteries Corp.	60	60	48	72	-	72
Subtotal	1,589	1,160	48	2,701	-	2,701
<u>Other Borrowings</u>						
General Purpose Borrowings	1,442	92	-	1,534	96	631
Capital Investment Assets	355	732	318	769	280	288
Health Facilities	100	150	123	127	100	161
Other Crowns and Org.'s	110	442	276	276	-	190
Public School Divisions	-	160	17	143	-	657
Civil Service Superannuation Plan	100	-	-	100	-	-
Subtotal	2,107	1,576	734	2,949	476	2,473
Total Borrowing Requirements	3,696	2,736	782	5,650	476	5,174

Sources: Scotiabank Economics, Manitoba Finance.

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