EXECUTIVE SUMMARY

Ontario's Deficit Reduction Strategy Mirrors Previous, Unsuccessful Attempts

by Ben Eisen and Steve Lafleur

This study analyzes the first budget of the new Progressive Conservative government in Ontario, tabled in early April 2019, to assess the extent to which it reflects either a fundamental shift in fiscal policy from the policies of the Ford government's predecessors, or continuity with the fiscal policies of the McGuinty and Wynne governments.

Although the new budget does represent a policy change from the final years of the Wynne government, its fiscal policy approach is decidedly similar to that which prevailed under the McGuinty and Wynne governments in the period following the 2008/09 recession. Specifically, we compare Budget 2019 to the 2011 budget tabled by the government of Premier Dalton McGuinty and draw attention to key similarities.

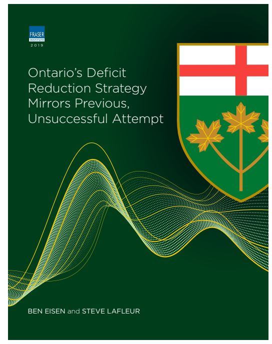
Despite large budget deficits, both the 2011 and 2019 budgets called for continued nominal spending growth with the hope that faster revenue growth would lead to gradual deficit reduction over time. Specifically, the 2019 budget forecasts spending growth averaging 1.0 percent annually whereas the 2011 McGuinty budget called for a spending growth rate of 1.4 percent.

Given similar spending trajectories and revenue outlooks, the two budgets also forecasted similar rates of gradual deficit reduction and therefore a lengthy period of deficit spending. The 2011 budget called for annual deficit reduction of $1.78 billion. And in fact, due to stronger than expected revenue growth, the McGuinty government did slightly better than expected and reduced the annual deficit reduction by $2.38 billion annually over a five-year period. By comparison, the Ford government's budget calls for deficit reduction at a nearly identical rate of $2.41 billion per year. As a result of this slow rate of deficit reduction and the large baseline deficit, both governments' fiscal plans called for slow, gradual returns to balance—7 years in the case of the 2011 budget and 5 years in the case of the 2019 budget.

Another point of similarity between the 2019 budget and those of the Ford government's predecessors is its reliance on elevated tax rates to finance government activities. The 2019 budget retained the province's general corporate income tax rate and its top marginal personal income tax rate, which it kept at 20.53 percent (including surtaxes). By following a similar gradualist approach to deficit reduction as Budget 2011, the Ford government may forgo an opportunity to increase Ontario's eroding tax competitiveness. Were it to eliminate the "temporary deficit-fighting high-income tax bracket" and follow through on a long-standing Liberal promise to reduce the general corporate income tax rate to 10 percent, those steps would help make Ontario a more at-

tractive place for workers and investment, and would come at a minor cost: 2 percent of government revenue if we assume no "behavioural effects." In other words, it assumes that the improved incentives to invest created by lower tax rates would not cause any additional economic activity. In the likely event that rate changes did lead to some additional economic activity, the budgetary impact of the rate reductions would be less than we estimated.

One important difference between the two budgets is that Budget 2019 projects less debt accumulation than the post-recession McGuinty and Wynn budgets, largely due to lower infrastructure spending. While Budget 2011 called for a 4.9 percentage point increase in the debt-to-GDP ratio over a three-year period, Budget 2019 plans to reduce the debt-to-GDP ratio by 1.6 percentage points by 2023/24. However, these reductions in capital spending are back-loaded, and might conflict with other initiatives, including the potential uploading of some assets and responsibilities of the Toronto Transit Commission and new subway extensions. While lower capital spending might help reduce the debt-to-GDP ratio, it is not yet clear whether that will projection come to pass.



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Canadian history is replete with examples of changes in government leading to substantial changes in fiscal policy direction. This analysis of the new Progressive Conservative government's first budget, however, suggests that this has not yet been the case in Ontario. Indeed, when it comes to the province's spending trajectory, approach to deficit reduction, and personal and corporate income tax policy, the new government has embraced strategies similar to those of its predecessors.

Premier Ford vs. Premier McGuinty: Cumulative Deficit Reduction (Budget and Actual) (in $ billions)