ECONOMIC RESEARCH AND STRATEGY

LAURENTIAN BANK SECURITIES

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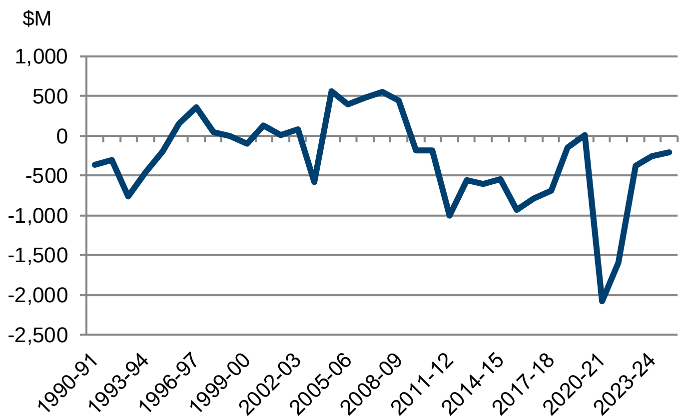
Manitoba Budget 2021– large short-term fiscal hit but no structural deficit

The impact of the pandemic on Manitoba's financial situation is meaningful. The $2.1B deficit registered in FY 2020-21 (2.9% of GDP) is expected to shrink to a $1.6B shortfall in FY 2021-22 (2.1% of GDP) according to Budget 2021 released yesterday (chart 1).

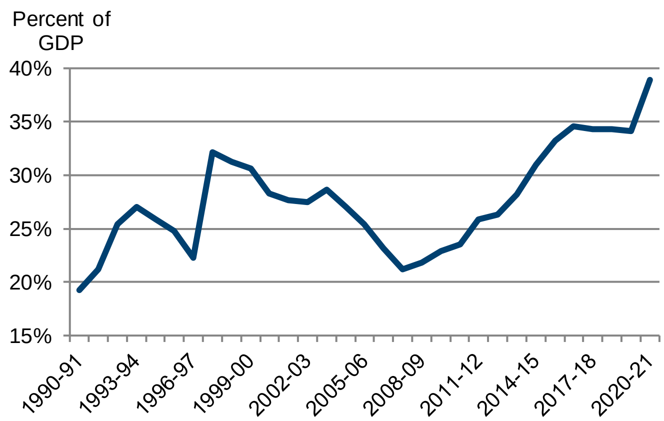
Without surprise, protecting people remains the top priority of this budget. The COVID-19 response will cost $1.2B in FY 2021-22 (health care delivery, vaccination and equipment, mental health, etc.), down from $2.0B last year and allowing total spending to edge down by 0.6% from a year ago, to $19.4B. The City of Winnipeg will receive $225M in funding from the Province for a second consecutive year.

Chart 1: Manitoba Budgetary Balance



Source: Manitoba Government, GoC Fiscal Reference Tables and LBS Econ. Res. and Strategy calculations.

Chart 2: Manitoba Net Debt



Source: Manitoba Government, GoC Fiscal Reference Tables and LBS Econ. Res. and Strategy calculations.

Total revenues are projected at $17.8B, a modest 2.1% increase in revenues relative to a year ago, essentially reflecting three factors. First, federal transfers are poised to fall by $227M, to $5.6B in FY 2021-22 as one-time extraordinary transfers from Ottawa fade out. Second, the modest expectation of a 4.1% real GDP rebound in 2021 underpins an improvement in revenues based on vaccination restoring confidence. Moreover, strong prices for agricultural products, growth in food manufacturing and a dynamic residential construction activity particularly stand out as positive economic pillars. So far, the third pandemic wave, driven by new variants, has hit Manitoba to a lesser extent than other regions across the country. The number of new cases stood at around 60 per day in early April. Thus, unlike Ontario, Quebec and Alberta, the number of active cases per capita in Manitoba haven't rose to a point where lockdown measures need to be reintroduced.

Third, the government sticks to its strategy of lowering taxes despite the pandemic. The budget offers plenty of targeted financial relief to individuals and businesses. The most important single measure is the phase-out of the Education Property Taxes, shaving $192M from the province's revenue. More precisely, residential and farmland owners will benefit from a significant 50% reduction in the education tax rate over two years; 10% for commercial owners. Other tax changes have a smaller impact on public finances. For instance, the removal of the 7% PST rate on selected personal services such as haircuts and manicures will save individuals an estimated $8M annually. Also, drivers will benefit from a reduction in motor vehicle registration fees for a second consecutive year. On the digital front, the province will apply the 7% PST rate to online platforms for digital streaming (Netflix), e-commerce purchases (Amazon) and online accommodation services (Airbnb). Taxing the digital economy has become imperative from a tax fairness standpoint and also promotes long term fiscal sustainability: the nontangible economy grows faster than the traditional tangible economy.

No structural deficit post-COVID and a new debt limit

One striking difference between Manitoba and many other provinces relates to the medium-term outlook. The Province does not deem its deficit structural: "The pandemic deficit of 2020/21, 2021/22 and possibly later years are not considered structural". Indeed, the smaller $374M, $254M and $209M shortfalls over the next 3 years ending in FY 2024-25 should be interpreted as a positive anchor by investors and credit agencies (chart 1). Accordingly, the net debt to GDP will likely peak at around 40% in FY 2021-22, up from 34% prior to the pandemic (chart 2). At these levels, debt ratios remain manageable. In other words, Manitoba is unlikely to resort to major tax hikes, large spending cuts or solely relying on increased long-term funding from the federal government to balance its books. In addition, Budget 2021 announced the introduction of a formal debt limit, or a cap on the annual capacity to borrow. That limit will be adjusted each budget, with some flexibility around adverse events such as recessions, but will decrease every year once the government balances its budget.

Partial use of the rainy day fund last year, lower requirements this year

Finally, the Province borrowed a record high $7.7B last year. To alleviate additional funding costs, the province withdrew $215M from its $800M rainy fund. As at March 31st, 2021, the remaining balance was estimated at $585M, providing continuous cushion against potential adverse market events in 2021. For FY 2021-22, borrowing requirements estimated at $4.9B reflect $2.7B in refinancing activities, $3.0B in new cash requirements, including funding the deficit and the capital plan, less $0.7B in pre-financing conducted in FY 2020-21. Manitoba Hydro, which makes up 43% of the Province's total outstanding debt, will receive $1.3B from the province's gross borrowings.

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