

BUDGET ANALYSIS

Quebec: Budget 2019

A Budget with Promise for the Future



HIGHLIGHTS

- ▶ Quebec's new government inherited an excellent financial situation that has allowed it to introduce a number of new measures and still maintain a balanced budget for 2019–2020 and the following years.
- ▶ The total financial impact of the new budget measures will be \$16.2B to 2023–2024, with a significant emphasis on health, education, reducing Quebecers' tax burden and improving the long-term growth potential of the economy and the environment.
- ▶ The 2018–2019 fiscal year should wrap up with a surplus of \$2,500M, which will be allocated to the stabilization reserve. With the surpluses from the last few years, this reserve will reach \$9,674M by March 31st, 2019, providing excellent leeway to the provincial government to face unexpected developments, or even a sharp downturn in the economy, without compromising the budgetary balance.
- ▶ The balance of the Generations Fund may reach \$20.9B by March 31st, 2024.
- ▶ The gross debt-to-GDP ratio will dip slightly below the 45% mark in 2020–2021, reaching the objective set by the law five years earlier than planned.

The Legault Government Stays the Course

The new CAQ government inherited an excellent financial situation that has allowed it to introduce a number of new measures in its 2019 budget without compromising the budgetary balance. After a budget surplus assessed at \$2,500M for 2018–2019, the Minister of Finance, Eric Girard, is staying on course, and the balance should return to zero for subsequent years. A minor return to positive numbers is forecast for 2022–2023, with a surplus of \$100M, followed by another surplus of \$450M in 2023–2024. These surpluses will be allocated to the stabilization reserve. With the surpluses from the last few years, this reserve will reach \$9,674M by March 31st, 2019, providing excellent leeway to the provincial government to face unexpected economic or other developments.

This is great news because the risk of a downturn in the economic forecast has grown in recent months. The increase in interest rates is having a greater impact in many areas of domestic demand, including consumer spending, which is growing more slowly. Global uncertainties are also heightened,

which has led many central banks to show far greater caution recently in normalizing their monetary policy. Our economic forecasts for 2019 and 2020 are also a little lower than the assumptions used in the budget.

With regard to the Generations Fund, the new government is following the lead of its predecessors in dedicating certain revenues to it. From 2018–2019 to 2023–2024, the total amount allocated to the Generations Fund may reach \$18.1B. As announced in the fall, the government will, nevertheless, withdraw \$8B from the Generations Fund in 2018–2019, followed by another \$2B in 2019–2020. These funds will be assigned entirely to paying down the debt to reduce the increase in interest charges over the coming years. Ultimately, the balance of the Generations Fund should, nevertheless, reach just over \$20B by March 31st, 2024. In this regard, Quebec has clearly set itself apart from most of the other provinces, which do not have this kind of financial cushion.

In terms of the changes in fiscal revenues, the good economic conditions in 2018 fostered relatively rapid growth for the

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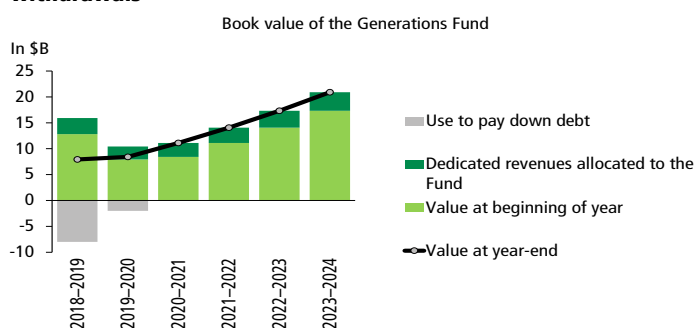
NOTE TO READERS: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively.

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TABLE 1
Summary of transactions

IN \$M (EXCEPT IF INDICATED)	ACTUAL		PROJECTIONS				
	2017–2018	2018–2019	2019–2020	2020–2021	2021–2022	2022–2023	2023–2024
Own-source revenue	85,919	90,146	90,714	93,789	97,034	100,443	103,895
Variation (%)	3.9	4.9	0.6	3.4	3.5	3.5	3.4
Federal transfers	22,485	23,411	24,924	25,600	25,950	26,589	27,251
Variation (%)	11.4	4.1	6.5	2.7	1.4	2.5	2.5
Total budget revenues	108,404	113,557	115,638	119,389	122,984	127,032	131,146
Variation (%)	5.3	4.8	1.8	3.2	3.0	3.3	3.2
Program spending	-94,249	-99,052	-104,038	-107,467	-110,645	-113,911	-117,287
Variation (%)	5.9	5.1	5.0	3.3	3.0	3.0	3.0
Debt service	-9,240	-8,899	-8,996	-9,138	-9,292	-9,661	-9,727
Variation (%)	-3.0	-3.7	1.1	1.6	1.7	4.0	0.7
Contingency reserves	---	---	-100	-100	-100	-100	-100
Balance	4,915	5,606	2,504	2,684	2,947	3,360	4,032
Generations Fund	-2,293	-3,106	-2,504	-2,684	-2,947	-3,260	-3,582
Balance in the meaning of the Act	2,622	2,500	0	0	0	100	450
Gross debt	201,071	200,756	204,169	207,318	211,357	214,095	215,494
Variation (%)	-1.2	-0.2	1.7	1.5	1.9	1.3	0.7
In % of GDP	48.2	46.1	45.3	44.6	44.1	43.4	42.3
Debt representing combined deficits	114,644	111,538	109,034	106,350	103,403	100,143	96,561
Variation (%)	-2.3	-2.7	-2.2	-2.5	-2.8	-3.2	-3.6
In % of GDP	27.5	25.6	24.2	22.9	21.6	20.3	19.0

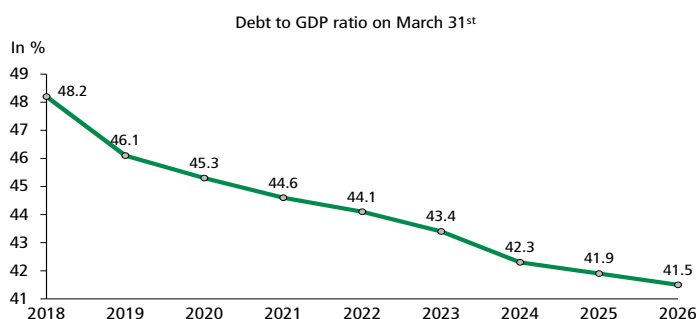
Source: Ministère des Finances du Québec

GRAPH 1
Value of the Generations Fund continues to climb despite withdrawals


Sources: Ministère des Finances du Québec and Desjardins, Economic Studies

2018–2019 fiscal year. However, the tax relief granted to individuals and businesses is expected to lead to some slowing in 2019–2020. The increase in revenues should then climb back to about 3% per year. As for budget spending, the many new measures in the 2019 budget will lead to a fairly quick increase in 2018–2019 and 2019–2020, as the government makes use of the financial leeway acquired through good economic performance and tight management of public finances. Still, the increase in spending is expected to match the increase in revenues by 2020–2021.

Finally, despite the balanced budget, the gross debt will continue to climb in the years ahead, largely due to infrastructure financing. Its growth rate will, nonetheless, remain lower than that of the economy, so the debt-to-GDP ratio will continue its downward trend, dipping in 2020–2021 slightly below the objective of 45% set out in the *Act to reduce the debt and establish the Generations Fund*, five years earlier than planned.

GRAPH 2
Relative size of debt decreasing faster than expected


Sources: Ministère des Finances du Québec and Desjardins, Economic Studies

TABLE 2
Economic outlook

VARIATION IN % (EXCEPT IF INDICATED)	2018	2019f	2020f
Real GDP¹			
Ministère des Finances forecasts	2.3	1.8	1.5
Desjardins forecasts	2.3	1.7	1.3
Nominal GDP			
Ministère des Finances forecasts	4.3	3.5	3.2
Desjardins forecasts	4.5	3.6	2.8
GDP deflator¹			
Ministère des Finances forecasts	2.0	1.7	1.7
Desjardins forecasts	2.1	1.9	1.5
Housing starts (annual rate in thousands of units)			
Ministère des Finances forecasts	46.9	42.8	40.7
Desjardins forecasts	46.9	44.5	40.0
Consumer prices			
Ministère des Finances forecasts	1.7	1.4	2.0
Desjardins forecasts	1.7	1.6	1.8
Job creation (annual average in thousands)			
Ministère des Finances forecasts	38.9	38.8	27.1
Desjardins forecasts	38.9	35.0	20.0
Unemployment rate (annual average in %)			
Ministère des Finances forecasts	5.5	5.4	5.3
Desjardins forecasts	5.5	5.2	5.1
Treasury bills—3-month (annual average in %)			
Ministère des Finances forecasts	1.4	1.9	2.2
Desjardins forecasts	1.4	1.7	2.0
Federal bonds—10-year (annual average in %)			
Ministère des Finances forecasts	2.3	2.3	2.8
Desjardins forecasts	2.3	2.0	2.2
Exchange rate (annual average in US\$)			
Ministère des Finances forecasts	0.77	0.77	0.79
Desjardins forecasts	0.77	0.75	0.76

f: forecasts; ¹ Due to rounding, the sum of the real GDP and GDP deflator does not correspond exactly to nominal GDP.
Sources: Ministère des Finances du Québec and Desjardins, Economic Studies

The New Government Has Set Its Priorities

The 2019 budget includes several new measures as the Legault government lays down the first milestones in its electoral program. In total, the financial impact of the new budget measures will reach \$16.2B by 2023–2024. Significant new resources will be dedicated to health and education, rolling back some of the restrictions from recent years. Several measures have also been introduced to reduce the tax burden of Quebecers, along with measures to protect the environment and improve the long-term growth potential of the economy. This is a good initiative, considering the aging of the Quebec population, which will place serious constraints on the growth of the province's real GDP in the years ahead. Here is a summary of the main measures that caught our attention:

- ▶ Total additional spending of \$2.4B on education to 2023–2024:
 - A large portion of this sum will be dedicated to 250 new kindergarten classes for 4-year-olds, beginning in September 2019.
 - A number of other measures have also been proposed:
 - ✓ Adding an extra hour of extracurricular activities per day in secondary schools.
 - ✓ Enhancing support for student success and retention and adding special education classes.
 - ✓ Increasing support for teachers and the promotion of the profession.

TABLE 3
Financial impact of the measures in Budget 2019–2020

IN \$M	2018–2019	2019–2020	2020–2021	2021–2022	2022–2023	2023–2024	TOTAL
Putting money back in the pockets of Québécois	-5	-271	-419	-457	-473	-472	-2,097
Improving the quality of education and health services	-90	-1,031	-1,164	-1,429	-1,737	-1,865	-7,316
Increasing the potential of the economy	-357	-505	-679	-703	-738	-709	-3,690
Acting for the environment	-51	-395	-491	-138	-113	-88	-1,276
Supporting communities	-930	-105	-162	-191	-186	-164	-1,739
Other	---	-15	-22	-30	---	---	-67
TOTAL	-1,432	-2,322	-2,937	-2,948	-3,248	-3,298	-16,185

Note: Totals may not add due to rounding.

Source: Ministère des Finances du Québec

- ✓ Increasing funding for CEGEPs and regional universities.
- ✓ Financing cultural outings for students and enriching the content of school libraries.
- ✓ Fostering early detection of learning disabilities.
- ▶ A \$20.3B increase in investments for education and higher learning networks has also been announced. These investments will be used to renovate schools and to build new schools, maintain buildings and add learning spaces. 80% of all investments will be used to keep the existing infrastructure in good condition.
- ▶ A \$4.9B increase in spending on health to 2023–2024:
 - Measures have been introduced to improve services to seniors by improving home care and services, building seniors' homes, adding residential beds and spaces, improving informal caregivers' quality of life and increasing the personal expense allowance.
 - Improve direct services to the public:
 - ✓ Reinforce access to front-line services.
 - ✓ Establish winter clinics.
 - ✓ Ensure a stronger presence of specialized nurse practitioners within the network.
 - ✓ Enhance the Support Program for Community Organizations.
 - Improve certain initiatives for youth, including earlier screening for learning disabilities.
 - Increase the number of nurses, nursing assistants, patient-care attendants and other health and social service practitioners.
- ▶ The government is also planning additional investments of \$20.2B for the health and social services sector to build new infrastructure or improve existing facilities.
- ▶ A \$2.1B reduction in Québécois' tax burden to 2023–2024:
 - Complete elimination of the additional contribution for childcare (between \$0.70 and \$13.90 per day), rolled out gradually over four years. Beginning in 2019, the bottom bracket will be eliminated, affecting over 40,000 families. The second threshold will then be gradually raised and completely disappear in 2022, when families will no longer have to pay the additional contribution.
 - Budget 2019–2020 allows the government to take its first step toward standardizing tax rates and lowering school taxes, beginning on July 1st, 2019. To that end, the government will transfer \$200M to the school boards in 2019–2020 to compensate for the reduction in their school tax revenues. For the subsequent years, the government will determine the additional amounts required to gradually establish a single tax rate that should converge at \$0.10540 per \$100 of assessment.
 - The government is proposing investments of \$173.2M over five years to provide better support for low-income families who receive support for dependent children and assistance under certain government programs.

- ▶ Over the next few years, the increase in the potential of Quebec's economy will largely depend on its ability to take advantage of the current labour pool, attract new skilled workers, particularly in advanced fields, and stimulate investment and business growth. The government intends to increase the employment rate in the current labour pool, increase the pool of available workers, improve productivity and promote business growth. To increase the potential of Quebec's economy, Budget 2019–2020 provides for initiatives totalling nearly \$3.7B.
 - Furthermore, to encourage workers to extend their career, the government is proposing an increase in the tax incentive already offered to experienced workers. Budget 2019–2020 offers two changes that will be effective this year. The age of eligibility for the tax credit will be lowered from 61 to 60, and the ceiling on excess work income eligible for the tax credit will be raised to \$10,000 for workers aged 60 to 64. To target lower-income workers, this tax credit will be reducible based on employment income starting at \$34,610, so workers will no longer receive tax assistance if their income exceeds \$64,610.
 - \$130M in initiatives to support business investment and growth.
 - To increase the amounts made available to Investissement Québec, Budget 2019-2020 provides for a \$1B increase in its capital stock, taking it from \$4B to \$5B. This enhancement will allow Investissement Québec to use its own equity to increase its transactions with businesses, particularly loans and equity investments.
 - Implementation of a \$1B envelope to assist with the development of strategic businesses in Quebec and create a team whose mandate will be to develop business intelligence in the field of head office protection.
 - To boost innovation and create the jobs of tomorrow, the government is offering an envelope of \$709M to invest in innovative projects and speed up the adoption of artificial intelligence.
 - Budget 2019–2020 provides over \$715M to enhance the tax holiday for large, regional investment projects, improve regional infrastructure, stimulate tourism in Quebec and support the development of the bio-food sector.
- ▶ The Ministère des Finances is providing \$1,276M over six years to improve the government's environmental efforts. It will also extend the Drive Green program, which offers a discount on the purchase of electric vehicles and charging stations.

An Enviable Situation for the Short Term... but with Major Challenges Ahead

The budgetary restraint in recent years, combined with the strong performance of Quebec's economy, has put the new Legault government in an excellent position to draw up its first budget. In the coming years, the \$9.7B stabilization reserve should allow the Ministère des Finances to maintain a balanced budget, even if Quebec's economy were to go through a more difficult period.

As the government has said, Quebec will have to be able to overcome major challenges in the longer term, as the aging population and anemic productivity gains will lead to weaker economic growth. This will inevitably lead to slower growth in budgetary revenues when needs will be high, especially in terms of health and social services. Clearly, budgetary restraint will be required for many years. Quebec is still the second-most debt-ridden province in the country, despite the improvement in its financial situation. Under these conditions, the development of a detailed budget plan for a period of 10 to 25 years would be very useful.

And finally, although Budget 2019–2020 still did not open the door to creating the position of parliamentary budget officer, François Legault has seemed in favour of such an initiative in the past. As is the case in the federal government, Ontario and many other jurisdictions around the world, a parliamentary budget officer would provide non-partisan tracking of the public finances in Quebec and improve transparency in the development of budget parameters, especially with analyses in forecasts.