

BUDGET ANALYSIS

Quebec: Update on the Economic and Financial Situation Targeted Spending to Address Recent Concerns

HIGHLIGHTS

- ▶ Quebec's strong economic performance provides the Ministère des Finances with significant financial flexibility.
- ▶ The projected budget deficits are lower than the March budget projections.
- ▶ The government announces new initiatives totalling \$13B over five years.
- ▶ Gross debt growth should gradually slow as of 2021–2022.
- ▶ The gross debt-to-GDP ratio should decrease further by March 31, 2022.

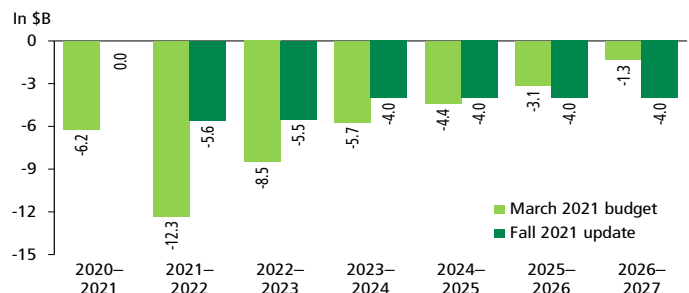
Budget Deficits Lower than Expected

Quebec's economic and financial situation has improved significantly since the March 25 budget. The vaccination campaign in the province has been running very well, meaning that many public health restrictions were able to be gradually lifted. Quebec's economic growth therefore greatly exceeded the Canadian average in the first half of 2021, making it possible for the province's real GDP to regain all the ground lost during the pandemic in the second quarter.

Quebec's strong economic performance notably resulted in faster budget revenue growth, providing the Quebec government with new financial flexibility to the tune of \$9.0B for 2021–2022, \$6.0B for 2022–2023 and \$5.9B for 2023–2024. It would have been easy for the government to use all of this flexibility to fund new budget initiatives. Instead, the Ministère des Finances is proposing to divide it wisely between implementing new initiatives and reducing budget deficits for future years.

The budgetary balance within the meaning of the Act for 2020–2021 therefore shifts from a \$6.2B deficit to a balanced budget, with the accounting use of the stabilization reserve. For 2021–2022, the forecast deficit is reduced by \$6.7B, that is, -\$5.6B instead of -\$12.3B (graph 1). The favourable variance is \$3.0B for 2022–2023 and \$1.7B for 2023–2024. Despite this more positive picture, the Quebec government predicts that a

GRAPH 1
Significant improvement in the budgetary balance as defined in the Act



Source: Ministère des Finances du Québec

structural deficit of around \$4B will remain as of 2023–2024. The Ministère des Finances is nevertheless confident that this deficit can be eliminated by 2027–2028.

Under these circumstances, the increase in gross debt should gradually slow starting in 2021–2022. Combined with relatively fast economic growth in the province, this should further decrease the gross debt-to-GDP ratio by March 31, 2022. Therefore, the share of budget revenue dedicated to servicing debt (that is, interest payments) should continue to decline slightly in the coming years (graph 2 on page 2).

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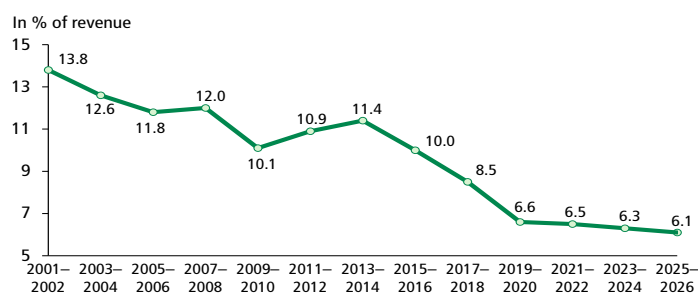
NOTE TO READERS: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively.

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TABLE 1
Budgetary situation

IN \$B (EXCEPT IF INDICATED)	ACTUAL	PROJECTIONS				
	2020–2021	2021–2022	2022–2023	2023–2024	2024–2025	2025–2026
Own-source revenue	91.9	101.6	104.9	108.2	112.3	116.1
Variation (%)	0.1	10.6	3.2	3.2	3.8	3.4
Federal transfers	30.7	29.5	28.5	29.9	29.4	30.2
Variation (%)	21.8	-4.1	-3.2	4.8	-1.6	2.6
Total budget revenues	122.6	131.1	133.4	138.1	141.7	146.3
Variation (%)	4.8	6.9	1.8	3.6	2.6	3.2
Program spending	-105.7	-118.1	-123.4	-127.2	-131.2	-136.4
Variation (%)	-1.4	11.8	4.5	3.1	3.1	4.0
Debt service	-7.7	-8.6	-8.8	-8.7	-9.0	-9.0
Variation (%)	0.2	11.4	3.3	-1.2	2.9	-0.2
Support and recovery measures	-13.0	-7.6	-1.0	-0.1	0.0	---
Change in accounting respecting transfer payments	-0.5	-0.4	-1.2	-1.3	-0.8	0.0
Provision for economic risks	---	---	-1.3	-1.0	-0.5	-0.5
Balance	-4.2	-3.6	-2.3	-0.1	0.2	0.4
Generations Fund	-3.3	-3.3	-3.3	-3.9	-4.3	-4.4
Balance before stabilization reserve	-7.5	-6.8	-5.5	-4.0	-4.0	-4.0
Accounting changes	-3.2	---	---	---	---	---
Use of the stabilization reserve	10.8	1.2	---	---	---	---
Balance in the meaning of the Act	0.0	-5.6	-5.5	-4.0	-4.0	-4.0
Gross debt	210.1	220.4	230.9	237.3	242.6	248.3
Variation (%)	5.7	4.9	4.7	2.8	2.2	2.4
In % of GDP	46.8	44.3	43.3	43.4	42.9	42.5
Debt representing combined deficits	108.7	112.3	114.6	114.7	114.5	114.1
Variation (%)	0.9	3.3	2.0	0.1	-0.2	-0.3
In % of GDP	24.2	22.6	21.5	21.0	20.3	19.5

Source: Ministère des Finances du Québec

GRAPH 2
Debt service will continue to decline slightly over the next few years


Source: Ministère des Finances du Québec

Additional Forward-Looking Measures

In the midst of the pandemic, the Quebec government focused all of its attention on managing the public health crisis and making every effort to reduce the adverse effects on households and businesses. However, the situation is normalizing more and more, and many post-pandemic problems are emerging. For

example, significant imbalances are noted between the supply and demand of many goods and services, putting upward pressure on prices. Labour shortages, already very much an issue in Quebec before the pandemic, have also become a major concern again.

Most of the initiatives introduced today by the Quebec government address these new concerns. Compared to the 2021 budget, the Ministère des Finances has announced additional initiatives totalling \$13B over five years. They can be summarized as follows:

- ▶ The effects of accelerating inflation have been felt in 2021, particularly by lower-income families, for whom rises in the price of food and housing can prove especially constraining. The government wants to help Quebecers, particularly low-income households, to better deal with inflation through a range of initiatives totalling \$2.1B, such as:
 - Implementing an extraordinary cost of living allowance, that is, \$400 for a couple and \$275 for an individual living alone. To get this benefit, a household must have

TABLE 2
Economic outlook

VARIATION IN % (EXCEPT IF INDICATED)	2020	2021f	2022f
Real GDP			
Ministère des Finances forecasts	-5.5	6.5	3.3
Desjardins forecasts	-5.5	6.5	2.5
Nominal GDP			
Ministère des Finances forecasts	-2.4	10.8	7.2
Desjardins forecasts	-2.4	10.4	6.1
Consumer prices			
Ministère des Finances forecasts	0.8	3.4	2.9
Desjardins forecasts	0.8	3.8	3.2
Job creation (annual average in thousands)			
Ministère des Finances forecasts	-208.5	167.3	107.5
Desjardins forecasts	-208.5	170.0	130.0
Unemployment rate (annual average in %)			
Ministère des Finances forecasts	8.9	6.3	5.7
Desjardins forecasts	8.9	6.3	4.9
Treasury bills—3-month (annual average in %)			
Ministère des Finances forecasts	0.4	0.1	0.4
Desjardins forecasts	0.4	0.1	0.6
Federal bonds—10-year (annual average in %)			
Ministère des Finances forecasts	0.7	1.3	1.7
Desjardins forecasts	0.7	1.5	2.2
Exchange rate (annual average in US\$)			
Ministère des Finances forecasts	0.75	0.80	0.79
Desjardins forecasts	0.75	0.80	0.81

f: forecasts

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

received the refundable solidarity tax credit for July 2021 to June 2022.

- Enhancing the senior assistance amount for seniors aged 70 or over (the maximum assistance amount in 2021 will be \$400 for a senior living alone and \$800 for a senior couple).
 - Implementing an affordable housing construction assistance program.
 - Helping low-income households pay their rent.
- ▶ In its update, the government is including additional measures totalling over \$3.4B by 2025–2026 in order to:
- Combat the labour shortage by supporting training and requalification for workers and attracting new talent.
 - Accelerate the growth in business productivity by supporting private investment and the implementation of the first innovation zones and innovative projects in Quebec.
- Support the recovery of Quebec’s cultural sector.
- ▶ The government is proposing initiatives totalling \$2.4B to support families through measures aimed in particular at:
- Enhancing the refundable tax credit for childcare expenses to reduce the costs paid by families with children attending a non-subsidized childcare service and to make the net rate more comparable to the cost of a subsidized service.
 - Completing the educational childcare services network by creating 37,000 subsidized spaces by March 2025, consolidating home-based childcare services and improving access to the network.
- ▶ Support totalling \$742M is proposed for communities to:
- Increase crime prevention efforts.
 - Combat gun violence, racism and domestic violence.
 - Support households with special housing needs.

- Develop local road transportation.
 - Encourage sports, recreation and leisure activities.
- Measures totalling \$4.4B to strengthen the health care system:
- Reduce the surgery waiting list so surgeries can resume at a more sustained pace.
 - Introduce measures aimed at improving working conditions and attracting staff to health care institutions, as provided for in the attraction and retention program for nursing and cardiorespiratory personnel.

Great Uncertainty Remains

Despite the positive evolution of the pandemic, Quebec's economy is facing many challenges. The measures announced today by the Quebec government will undoubtedly help the province overcome the obstacles that will emerge over the next few years. That said, the economic effectiveness of each of the new measures is not yet certain, and only time will tell their true impact. For example, implementing the extraordinary cost of living allowance might have unexpected effects. The aim of the measure is very commendable, as it will offset the loss of purchasing power that less well-off households have experienced as a result of the spike in prices. However, that could drive demand further and thus continue to put upward pressure on prices. Clearly, the solution is not simple. That said, the price surge is a global phenomenon and is largely a reflection

of the imbalances stemming from the pandemic. Yet, most forecasters expect a gradual reduction in inflationary pressures in the coming months, which should eventually bring relief to Quebec households.

As for the labour shortage, one of the greatest challenges facing Quebec's economy, the government is certainly not skimping, particularly in terms of training. Awarding incentive scholarships to increase post-secondary graduation in priority disciplines is a significant measure, as Quebec has long grappled with a shortage of highly skilled labour. We will have to see the details of these initiatives to fully assess their effectiveness. For example, what if a graduate leaves the country? What impact will there be on disciplines not targeted by these programs?

Beyond that, training is just one of the many solutions to be introduced to address the labour shortage. The retention of older workers, the immigration of workers with sought-after skills, better integration of newcomers and automation are all other levers that will have to be used to reduce the shortage of workers. The budget update revealed new commitments for some of these levers, but it is clear that much remains to be done before the labour shortage can be overcome.

The 2022 spring budget will be the next opportunity to take stock. Until then, the uncertainties brought about by the pandemic will likely have eased further. The Quebec government might gain more financial flexibility as a result, which will notably enable it to tackle the \$4.0B structural deficit and fine-tune its plan to return to a balanced budget.