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No Choice But to Lead

FILLING THE FEDERAL BUDGET VOID

Hugh Mackenzie

The economic context for Ontario's 2009–10 budget has been called the most challenging faced by an Ontario government in a generation. That is putting it mildly. While the headlines from the financial economy continue to pile bad news on top of bad news, the economy that provides a livelihood for most Ontarians is slipping rapidly backwards. Tens of thousands have lost their jobs; tens of thousands more job losses are almost certain to follow.

Public services in this province have only recently begun to recover from the damage caused by the Harris years, and are in far worse shape than they were at the time of the last recession in 1991. Thanks to irresponsible tax cuts in the late 1990s, Ontario's fiscal capacity is not strong going into this recession.

To make matters worse, the government appears until very recently to have been in denial over the severity of the situation facing this province. At a time when the employment numbers were telling us that the economy was in free-fall — since confirmed by the data on GDP growth for the 4th quarter of 2008 — the government was forecasting a deficit of only $500 million for 2008–9.

Finally, the long awaited federal response may have been a political success, but as an economic response to the recession it falls far short of the mark. It delivers economic stimulus that is too small — less than half the 2% recommended by the International Monetary Fund — focused too much on general tax cuts and subjected to too many conditions to be effective. It does virtually nothing to help individual Canadians adversely affected by the recession. And it is so driven my short-term political considerations and so unfocused that it does very little to position Canada's economy to thrive in the recovery.

That leaves Ontario with a clearly defined set of requirements for 2009–10. It must resist service cuts that will make the situation worse. It must ensure that the required matching funding is available to lever all of the federal infrastructure funding as quickly as possible. It must provide assistance to Ontario families devastated by the recession, beginning by accelerating the introduction of its poverty reduction strategy. It must make careful, strategic investments aimed at positioning Ontario for recovery in the future. Although the current state of the economy is a definite challenge, public services and transfer payment agencies, from healthcare to critical community services, are essential to our economic recovery. They provide essential supports to families affected by the recession. They also make up a significant share of the Ontario economy, making up one job in five and serving as the only stable bulwark against an even deeper downturn.

A difficult context

The rapidly changing context for Ontario's 2009–10 budget is making a normally challenging exercise even more difficult. Projections for economic growth that looked conservative when the Minister of Finance delivered his 2008 budget last March were already looking optimistic last fall, even before the full scope of the economic slowdown affecting every economy in the world became obvious. To make matters worse, it seems as if each passing day includes new indications that the slump may be deeper and longer than originally expected.

Complicating the situation further, there has been nothing short of a revolution in thinking across the world concerning the most appropriate public policy response to this severe and widespread recession. As recently as last fall, the place of safety in debate over fiscal policy was to repeat the anti-deficit mantra of the 1980s and 1990s. All four of Canada's political parties managed to get through the election campaign pledging repeatedly that under no circumstances would they permit a budgetary deficit to re-emerge.

While it is certainly not correct to say, as some have, that "we are all Keynesians now", a surprisingly broad spectrum of politicians, economists and business leaders is advocating precisely the kinds of fiscal policies that Keynes would have advocated in response to the recession.

The use of fiscal policy to stimulate the economy — with the inevitable increases in budgetary deficits that result — has moved in a few short months from anathema to received wisdom. Ideas about economic policy and the role of government in the economy that have dominated public discourse for nearly three decades have been discredited.

The 2009–10 federal budget that appears to have rescued Prime Minister Stephen Harper from his do-it-yourself political crisis both underlines that shift in political and economic thinking and creates an additional set of challenges. The underlining of the change is obvious. From his claim in November 2008 that his budget would be balanced this year and his pledge to do whatever had to be done to keep deficits from recurring, federal Finance Minister Jim Flaherty tabled a fiscal plan that included substantial deficits for the next two years and continuing smaller deficits for several years thereafter.

The new challenges for Ontario posed by the federal budget are less obvious, but are substantive in nature.

Federal budget 2009: Political success, economic failure

As much as the federal budget for 2009 is an evident political success — the Harper government will survive a budget confidence vote — it falls far short of what Canada, and Ontario, needs economically. The size of the stimulus is inadequate; the mechanisms chosen for the delivery of that stimulus are the wrong mechanisms; and perhaps most important, the stimulus package itself is so unfocused and incoherent it will leave us with far too little to show for the billions invested in it.

The size of the federal package — 1.3% of GDP using the federal government's own numbers, barely 1% using the numbers from the Parliamentary Budget Office — falls well short of the 2% of GDP recommended by the International Monetary Fund and even further short of the fiscal efforts of many OECD nations. The federal numbers get close to 2% of GDP by assuming that federal infrastructure spending will lever approximately $10 billion in additional municipal and provincial spending. That's an obvious challenge for Ontario, especially given the perilous state of local government finances.

The form in which the stimulus is delivered also poses challenges for Ontario.

A significant proportion of the federal government's stimulus package will be delivered in the form of broad-based tax cuts, a decision that will weaken the economic impact of the package as a whole. By reducing federal fiscal capacity, it will also extend the period of budget deficits at the national level. The official budget documents suggest that more than two-thirds of the total fiscal stimulus will come from the federal government with one-third from the provinces and municipalities. With about half of the claimed federal stimulus rendered ineffective by these choices, the actual federal share will likely be less than 50%.

The failure of the package to include Employment Insurance reform of any consequence is a double blow to Ontario. From an economic perspective, it will do nothing to address the disgracefully low coverage of the unemployed in Ontario under the current program. Across the province, only about 30% of the unemployed qualify for EI; in our major cities, coverage is closer to 20%. Despite a remarkably broad consensus that EI coverage is a critical problem in a recession, the changes announced in the federal budget will have little or no impact. That, in turn, will place increased pressure on Ontario's inadequate system of social assistance.

From a political perspective, the Ontario government is relying heavily on federal government participation for the success of its poverty reduction strategy. EI reform is a critical component of that strategy. So is affordable housing policy.

In the aggregate and on the surface, the federal budget's commitment to housing looks impressive. The total amount allocated for housing is claimed to be more than $9 billion over two years. But here, as in other parts of the budget, there are problems both with the size of the claimed stimulus and the way it is allocated. Of the $9 billion, $1.5 billion is actually provincial and municipal money that it is assumed will be levered by the federal funding.

Most important, fully one-third of the total is for the tax credit for home renovation, a measure that will provide substantial funding for people who can already afford to renovate and who would likely be doing so anyway. While the families that add decks to their cottages or replace hardwood floors in their homes will be pleased to get the money, from a housing policy perspective and from an economic stimulus perspective, it is money down the drain.

Unfortunately, Ontario isn't in much of a position to complain about the limitations of federal housing funding, since the track record of the McGuinty government matches the abysmal record of the Harris-Eves governments that preceded it. The failure of the federal government to respond to Ontario's actual housing needs, however, puts additional pressure on the McGuinty government to act.

The infrastructure spending package, touted as the core of the federal program, has its own set of problems. Despite repeated calls for fast, first-dollar funding for infrastructure programs, the federal government was unable to resist the temptation to make its program look bigger than it really is by requiring financial leverage. Most of the government's infrastructure investment requires cost sharing with provincial governments and, where relevant, with municipalities and provincial transfer payment agencies. Despite long-standing complaints about conditions on funding and extended approval processes, the federal government was unable to resist the temptation to exercise detailed control through a formal application and approval process and to require that funding flow through Build Canada, with its irrational and time-consuming preference for infrastructure delivery through public-private partnerships. Finally, in the face of calls for funding that frees recipient governments to invest in accordance with their own priorities, the federal government was unable to resist the temptation to meddle, imposing its own priorities on cost-shared investments.

For Ontario in particular, investments in public transit that the province considers to be of critical importance will likely not be funded while lower priority projects — renovation of hockey arenas, for example — will receive funding.

Ironically, despite the federal government's penchant for meddling when it comes to infrastructure spending, the biggest single problem with the infrastructure investment program is that it lacks any theme or coherent set of objectives. It is little more than a political grab bag.

Indeed, the infrastructure and housing packages resemble a typical U.S. Appropriations Bill after it has been through the House of Representatives and had countless pork barrel investments attached to it. There is no core strategy implicit in the laundry list of investments. It stands in sharp contrast to the focused and strategic approach being taken by the Obama administration in the United States.

If nothing is done to impose some order on the chaos of the federal program, we will come out of this recession having missed the opportunity to build a foundation for the future.

The contents of the federal budget will pose real policy and budgetary challenges for Ontario. So will other key issues overlooked in the budget.

Education is missing in action. There is funding for bricks and mortar for universities, but nothing to support what goes on in those institutions, and nothing for the students who study in them. In short, nothing that addresses the twin problems of quality and affordability. The absence of any action on post-secondary education is particularly noteworthy in light of the fact that the Harper government had actually identified post-secondary education as an area of federal interest. With the Obama administration signaling that the United States has rediscovered post-secondary education as a public policy issue, a failure to invest at this point could compromise Canada's ability to compete with a highly educated workforce in the future.

And as expected, there is nothing in the budget for early childhood education, an omission that threatens to have a devastating impact on child care availability in major centres throughout Ontario.

While the government held back on any immediate cuts in funding for the non-profit sector in this budget, it fails to provide relief from the financial crisis facing this sector as charitable donations shrink with the economy and investment returns on endowment funds collapse at the same time as demand for services grows.

It is evident from the budget that the only help the Harper government is prepared to offer in the economic crisis is to banks.

Consistent with the government's general orientation, it proposes to address the economic consequences of the downturn for Canadian businesses through the tax system. There is no program specifically targeted to companies facing partial or complete shutdowns of activity in Canada.

Implications for Ontario's 2009 budget

Ontario must take the federal budget into account in formulating its own budget in three respects.

First, funding for programs either cancelled or allowed to expire by the federal government must be maintained through provincial initiative. This is both a short-term and a medium-term problem. In the short term, the end of federal funding will have immediate and direct negative effects. In the medium term, it is clear that at least for the foreseeable future federal funding is not going to come back. To put it bluntly, if the federal government cannot find money to maintain its child care funding in a budget in which it is committing $40 billion over two years, what are the chances of such funding reappearing in normal budget years?

Child care funding tops the list of candidates for provincial funding to backfill federal cuts. Thanks to the non-renewal of child care funding, Ontario has lost $63.5 million in federal funding. To avoid losing the 22,000 child care spaces at stake, Ontario would have to increase its funding by $100 million — $63.5 million to replace the lost federal funding and an additional $36.5 million to offset the impact of required income-tested subsidies.

The federal budget contained funding for physical infrastructure for universities, but nothing to support either the educational activities that would take place in those buildings or the students who would study in those facilities.

Tuition fees for post-secondary education in Ontario are slated to go up this coming September by 5%. At a time when the finances of both students and parents are strained, it is inappropriate to persist with plans to increase tuition fees. The fee increase should be suspended, and colleges and universities compensated through increased grants for the lost revenue.

Second, the federal budget requires matching funding nationally of $6.56 billion in 2009–10 and $5.12 billion in 2010–11. Assuming Ontario's share is determined on an equal per capita basis, Ontario's share of this matching obligation would be 38.9% of the total, or $2.55 billion in 2009–10 and $2 billion in 2010–11. Depending on how the infrastructure projects themselves are financed, a portion of these costs would be amortized rather than expensed as cash transfers and the annual budgetary impact in the next two years would be relatively limited.

Third, Ontario has no choice now but to deal directly with the implications of the federal government's failure to address the weaknesses in employment insurance funding. As the system currently stands, Ontario's social assistance system is not designed to be of any help to those most affected by recession. For laid off employees who either run out of EI or do not qualify in the first place, the choice before them is not a happy one. Ontario Works rules require that applicants exhaust their assets as a condition of eligibility. That means, in particular, that applicants will be required to use up their retirement savings before qualifying for social assistance. Once they are forced onto social assistance the rates will not enable families to keep their homes or cover their basic needs, never mind allow them to buy consumer goods and stimulate the economy. Even for those who qualify, EI and Ontario Works are not designed to help those who want to retrain for a new career.

What to look for in the Ontario 2009 budget

Ontario has a lot at stake in the government's choices in the next provincial budget. The right choices will: provide substantial additional stimulus to the economy when it is most needed; help Ontario individuals, families and businesses get through the recession; and leave behind a legacy of investments in infrastructure and in people to ensure a more prosperous and sustainable future.

There are hundreds of choices potentially available to the government as it formulates its budget.

Things to look for in Ontario's 2009 budget:

1. A provincial commitment to provide the full amount of matching funding expected by the federal government for Ontario's share of federal infrastructure funding.

While the federal budget contemplated tri-partite funding involving local governments and other agencies under provincial jurisdiction, it is not reasonable to expect municipalities and provincial transfer payment agencies to be able to find their share of this funding.

On a cash basis, this would require a contribution from Ontario of $2.55 billion. The budgetary cost would be much less because most of the additional costs can be amortized.

This will ensure Ontario is in a position to benefit fully from the federal economic stimulus package.

2. The creation of the office of the Ontario jobs commissioner with a budget and mandate to develop creative solutions for distressed businesses to bridge them through the recession.

Ontario's economy is too exposed to economic forces around the world to recover on its own. Workers who have been laid off are not going to be recalled to produce products for which there is no demand. At the same time, however, workers cannot be recalled to work at plants that no longer exist. The greatest long-term threat from the recession is plant closures that will undermine Ontario's ability to participate in an economic recovery when it takes place.

The function of the jobs commissioner would be to identify issues threatening business operations in Ontario and negotiate flexible arrangements to bridge those operations through the recession.

3. Enhanced funding for recession-sensitive provincial programs such as social assistance, and emergency transitional assistance for non-profit organizations involved in the delivery of public services.

Ontario should accelerate the provincial assumption of full responsibility for funding social assistance and provide enhanced funding to cover 100% of any increased costs for social assistance.

Non-profit organizations are being pressured by the recession from every angle. As the recession deepens, demand for services expands. But at the same time, income from donations tends to dry up and foundations are losing money in financial markets. This threatens many organizations with financial crisis precisely at the time when the community needs them the most.

4. Funding for a substantial first phase of a comprehensive poverty reduction strategy.

Ontario cannot afford to wait to begin work on a poverty reduction strategy. An emphasis on poverty reduction supports four key objectives at once. It moves forward on an important, long-standing public policy objective. It delivers immediate and effective economic stimulus. It fills part of the gap in recession relief left by the federal government's failure to reform the employment insurance system. And it delivers significant long-term economic and social benefits to the province.

This includes measures to increase social assistance benefits, relax punitive asset restrictions in social assistance, increase child benefits, take the first steps towards universally accessible child care, increase funding for students at risk in elementary and secondary schools and improve access to affordable housing.

5. Invest now to improve quality and expand participation in post-secondary education.

After 15 years of constrained provincial funding for education and rapidly increasing tuition fees, Ontario has become complacent about inadequacy. It ignores the warning signs about deteriorating quality as class sizes increase and program offerings are narrowed. And it congratulates itself on the fact that enrolment has not gone down as tuition has increased. Stable enrolment at a time when needs are expanding rapidly is not nearly good enough.

Ontario has no long-term goals for increasing participation in post-secondary education and no plans to get there. Ontario has no vision for the future of its post-secondary education system, and no plans to pay for the improvements that are needed. Ontario has driven undergraduate tuition fees to the highest levels in the country while allowing its own funding per student to drop to the lowest. It has sat by and watched as tuition fees for professional programs have soared beyond the reach of low-and moderate-income families and ignored the mounting evidence that participation in those programs is increasingly restricted to the economic elite.

There is no quick fix to the problems plaguing post-secondary education in Ontario. There are some obvious first steps, however. Tuition fees should be rolled back to their pre-recession levels and increased funding should be provided to colleges and universities to replace the lost revenue.

Ontario should ramp up funding for a quality improvement initiative to bring funding per student and faculty-student ratios up to the average in other provinces.

Ontario should provide the increased operating funding colleges and universities require to match federal funding for rehabilitation and repair of post-secondary facilities.

6. Invest in a greener energy future

The need to replace Ontario's greenhouse gas intensive coal-fired power stations and its aging nuclear facilities presents the opportunity of a generation to transform Ontario's energy production and consumption infrastructure and to create the green energy industries to support it.

Ontario needs significant public investments in publicly owned and operated generation from renewable sources — wind, sun, water, geothermal. The majority of this public investment should not be used to prolong the lives of the old technologies (as is now the plan) — all into repairing old nuke facilities or into generating energy from incinerating garbage or into complicated processes to "sequester" the noxious gases produced by burning coal and other fossil fuels. Unless public utilities play the major role in conservation and the development and use of renewable generation technologies, Ontario will squander its ability to direct the sector into a sustainable future.

In addition, Ontario should provide new first-dollar funding for improvements in public transit. It is clear that if we wait for federal funding to get going on broad-based plans like Metrolinx and Transit City, or if we wait until local governments are able to find the funding they need to match provincial dollars, we will be waiting forever. And we cannot afford to wait.

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CANADIAN CENTRE
for POLICY ALTERNATIVES
CENTRE CANADIEN
de POLITIQUES ALTERNATIVES

410-75 Albert Street, Ottawa, ON K1P 5E7
TEL 613-563-1341 FAX 613-233-1458
EMAIL ccpa@policyalternatives.ca

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