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Praying for rain:
The McGuinty strategy for fiscal recovery

By Hugh Mackenzie

Rather than confront the fiscal issues facing Ontario directly, the McGuinty Government has clearly decided on avoidance as the best strategy, hoping that increased Federal Government transfers and economic growth will take care of the problem.

Rather than address the fundamental revenue issue – the fact that tax cuts have left Ontario's revenue base far below what would be required to finance Ontario's public services needs, the government has decided to shift its attention to Ottawa, with its $23 billion campaign, hope for higher economic growth in the future, and ignore all but the most pressing public services needs.

At least as far as the bottom line is concerned, so far it seems to be working. Higher than expected corporate tax revenue and increased federal government transfers – an additional $1.2 billion each – generated substantially increased revenue, compared with the government's projections at budget time.

That's a turn-around of $2.4 billion. The budget also overestimated public debt interest by $700 million. These two items, by themselves, created a $3.1 billion swing in the budget balance. This swing was so substantial that in order to prevent the deficit for 2004-5 from dropping below its new $2.8 billion target for 2005-6, it had to shift $350 million in new spending for colleges and universities from the 2005-6 fiscal year back to 2004-5.

On the operating spending side of the budget for 2005-6, the government is committing additional funding for health ($1.8 billion), elementary and secondary education ($800 million), postsecondary education ($500 million) and child care ($300 million). Virtually everything else in the operating budget is either being flat-lined or cut.

In particular, there is no increase in social assistance benefits planned for this year. The only increase will be the pass-through of changes in the federal Child Tax Benefit previously announced. There will be no new Ontario money for social assistance. That means that after just one year of an increase, Ontarians in the greatest need have been pushed right back to the Harris-Eves era of inadequate, frozen and eroding benefits. When inflation is taken into account, the lowest-income Ontarians will be worse off this year than they were in the last year of the Harris-Eves era.

That is a disgrace.

In addition, the Ministry of Environment's budget has been virtually flat-lined. That means no new investments to strengthen Ontario's capacity to regulate for the improvement in environmental quality. That means no new investments towards Kyoto targets.

On the capital side, the government talks about supporting $30 billion in capital investment over five years. But there's no more detail in the budget than there was in Minister Caplan's speech to the Empire Club earlier this week. And if the Minister is correct in saying that Ontario faces a capital spending backlog of $100 billion, even the budget's vague plan addresses only 30% of the problem.

On top of that, the government remains vague about the role of P3s – or to use the new buzz word of Alternative Financing and Procurement. And the government has still not explained how it can make economic sense for Ontario to pay someone else to borrow money at a higher rate than Ontario's borrowing rate, rather than borrowing the money itself.

P3s or AFPs are simply too expensive. To take the Brampton hospital P3 as an example, for the cost of financing a $550 million P3 hospital, Ontario could have financed $725 million if it had borrowed the money directly. That's capital money that has disappeared into higher borrowing rates and profits for the P3 operator.

Looking at the 4-year forecast of the fiscal position of the government, the government has clearly abandoned its claim that it can reduce health care spending as it reforms the system. Forecast spending for 2007-8 has increased from $32.9 billion to $35.9 billion. That's good news for the health care system, although it likely has more to do with the government's promise to invest the Health Premium and increased federal health transfers into the health care system rather than any conscious change in plans.

Overall, the government's deficit elimination schedule has been set backwards by a full year, with the deficit projected to disappear by 2008-9 rather than 2007-8 as forecast last year.

While the 4-year projection still contains some flexibility – for example, it continues to overestimate public debt interest payments, and includes a very conservative estimate of corporate tax revenue – ultimately the government has decided to put its program spending and deficit reduction eggs into the federal transfers and economic growth basket.

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