

A Balanced Approach to Deficit Reduction

Fiscal Year 10/11

Robert Kavcic
Economist

March 23, 2010

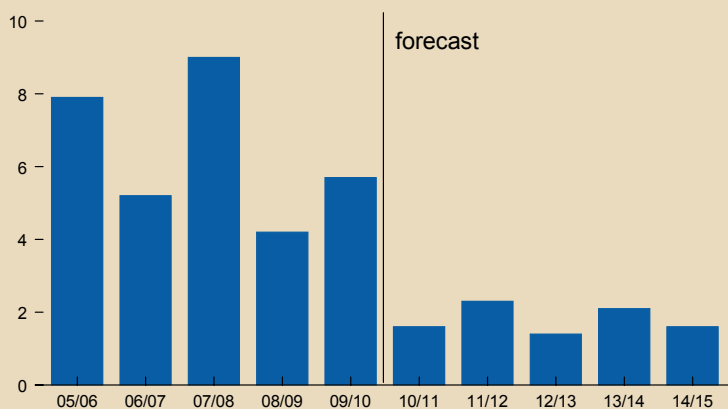
Manitoba's FY2010/11 budget takes a balanced approach to deficit reduction against a still-fragile economic backdrop, offering modest spending growth and some tax/user fee increases. **The Province is projecting a \$545 mln summary deficit in FY2010/11**, slightly improved from an estimated \$555 mln deficit in FY2009/10, with the latter unchanged from the Q3 update. The Province will lean on its Fiscal Stabilization Account for \$129 mln. Longer term, the Province is anticipating four years of deficits before returning to a \$185 mln surplus in FY2014/15. Starting at 1% of GDP, Manitoba's deficit will remain relatively small, and a moderation in spending growth combined with a looming economic recovery should allow the province to grow its way back into the black.

Fiscal Outlook (C\$ millions)

	estimate	— projection —	
	09/10	10/11	11/12
Total Revenue	12,502	12,720	13,119
Core Government	10,042	10,218	10,514
Other Entities	2,460	2,502	2,605
Total Expenditure	13,057	13,265	13,567
Core Government	10,644	10,755	11,037
Other Reporting	2,413	2,510	2,530
Summary Net Income	(555)	(545)	(448)

Source: Provincial forecasts

Total Spending (y/y % chng)



Source: Provincial forecasts

Total revenues are projected to rise 1.7% to \$12.7 bln in FY2010/11, with income tax receipts rising just 0.5%. This reflects the fact that the economic recovery is still in its early stages, which will limit the bounce-back in personal and corporate income taxes in the coming year. Meantime, some very modest tax changes will add \$8.6 mln to revenue, the largest being an increase in the tobacco tax. Most prior tax reduction initiatives will continue to roll out, with the biggest FY2010/11 impact coming from the business sector—e.g. the Mineral Exploration Tax Credit and elimination of Small Business Corporate Income Tax rate—but the reduction of the general corporate tax rate to 11% (from 12%) will be postponed. All told, tax changes (from this and prior budgets combined) will shave \$18.8 mln from revenue in FY2010/11. Federal transfers will total \$4.1 bln, 1.3% above the prior fiscal year.

Total spending is projected to rise 1.6% to \$13.3 bln in FY2010/11, led by a 5.6% jump in education and 4.8% increase in health care. This reflects a marked slowdown from the 6% annualized growth seen over the prior four years. While the Province will continue to spend on education and health, cuts elsewhere (e.g. negotiating a public-sector wage freeze) will allow overall spending growth to slow to 1.8% per year over the forecast horizon. This restraint would leave inflation-adjusted spending flat over the next five years, and represent a modest contraction of

about 0.7% per year on a real per-capita basis. The Province will invest \$1.8 bln in **infrastructure and capital renewal** in FY2010/11, with a continued focus on transportation, social housing and health care.

Total borrowing requirements are expected to be \$3.4 bln in FY2010/11, with \$1.3 bln reflecting refinancing. Net debt will rise \$1.7 bln to \$14 bln, lifting the net debt-to-GDP ratio 2.4 ppts to 26.8%—that's higher than its neighbours to the west, but still comfortably below Ontario and Quebec.

Manitoba's diverse economy has quietly weathered the recession relatively well.

Real GDP likely contracted a modest 0.3% in 2009, representing the shallowest downturn in Canada. Manitoba is also well-positioned for the emerging recovery, with the economy expected to advance 3.0% this year and a further 3.1% in 2011 (the Province is forecasting achievable growth of 2.5% and 3.0%). While nonresidential construction growth will moderate, ongoing large-scale investments (e.g. Manitoba Hydro) will continue to provide economic support over the medium term. Meantime, manufacturing and trade have already begun to turn up, and should return to solid growth as the global economic recovery takes root, while the agriculture and mining sectors provide good long-term growth potential. Population growth has also picked up in recent years, and is now running ahead of the national rate for the first time since the early-1980s. This is a marked shift that should continue to drive growth in retail sales and housing demand.

The bottom line: Manitoba's well-diversified economy and solid recovery prospects, combined with some spending discipline, should allow the Province to grow its way out of what is a relatively small deficit.

The information, opinions, estimates, projections and other materials contained herein are provided as of the date hereof and are subject to change without notice. Some of the information, opinions, estimates, projections and other materials contained herein have been obtained from numerous sources and Bank of Montreal ("BMO") and its affiliates make every effort to ensure that the contents thereof have been compiled or derived from sources believed to be reliable and to contain information and opinions which are accurate and complete. However, neither BMO nor its affiliates have independently verified or make any representation or warranty, express or implied, in respect thereof, take no responsibility for any errors and omissions which may be contained herein or accept any liability whatsoever for any loss arising from any use of or reliance on the information, opinions, estimates, projections and other materials contained herein whether relied upon by the recipient or user or any other third party (including, without limitation, any customer of the recipient or user). Information may be available to BMO and/or its affiliates that is not reflected herein. The information, opinions, estimates, projections and other materials contained herein are not to be construed as an offer to sell, a solicitation for or an offer to buy, any products or services referenced herein (including, without limitation, any commodities, securities or other financial instruments), nor shall such information, opinions, estimates, projections and other materials be considered as investment advice or as a recommendation to enter into any transaction. Additional information is available by contacting BMO or its relevant affiliate directly. BMO and/or its affiliates may make a market or deal as principal in the products (including, without limitation, any commodities, securities or other financial instruments) referenced herein. BMO, its affiliates, and/or their respective shareholders, directors, officers and/or employees may from time to time have long or short positions in any such products (including, without limitation, commodities, securities or other financial instruments). BMO Nesbitt Burns Inc. and/or BMO Capital Markets Corp., subsidiaries of BMO, may act as financial advisor and/or underwriter for certain of the corporations mentioned herein and may receive remuneration for same. "BMO Capital Markets" is a trade name used by the Bank of Montreal Investment Banking Group, which includes the wholesale/institutional arms of Bank of Montreal, BMO Nesbitt Burns Inc., BMO Nesbitt Burns Ltée/Ltd., BMO Capital Markets Corp. and Harris N.A., and BMO Capital Markets Limited. TO U.S. RESIDENTS: BMO Capital Markets Corp. and/or BMO Nesbitt Burns Securities Ltd., affiliates of BMO NB, furnish this report to U.S. residents and accept responsibility for the contents herein, except to the extent that it refers to securities of Bank of Montreal. Any U.S. person wishing to effect transactions in any security discussed herein should do so through BMO Capital Markets Corp. and/or BMO Nesbitt Burns Securities Ltd. TO U.K. RESIDENTS: The contents hereof are not directed at investors located in the U.K., other than persons described in Part VI of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001.

™ - "BMO (M-bar roundel symbol) Capital Markets" is a trade-mark of Bank of Montreal, used under licence. © Copyright Bank of Montreal.