
OBSERVATION

TD Economics



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WITH ONTARIO VOTES IN, THE BIG JOB BEGINS

Highlights

- The status quo situation largely prevails with yesterday's election outcome in Ontario.
- Recent downgrades to provincial economic growth forecasts are poised to carve away some budgetary revenues.
- If we add campaign promises to the mix and the procedural hurdles associated with a minority governance, the province's fiscal plan will be more challenged than ever before.

With all ballots now counted, Ontarians elected their third consecutive Liberal government. With the difficult job of winning re-election now complete, the government now faces the even tougher job of addressing its sizeable deficit and steeply rising debt burden in a challenging economic environment. Given this limited wiggle room, the campaign promises of the Liberal Party were relatively modest in scope. Still, the task will not be made any easier by diminishing growth prospects since the current government issued both its 2011 budget and election platform. What's more, the new government is in a minority position, which in turn, could exacerbate the challenge of slaying the deficit dragon.

Despite these uncertainties, there was little reaction in financial markets to the election results. Investors had been braced for a minority Liberal government based on opinion polls in recent weeks. In addition, there are many other distractions in financial markets at the moment. Due to its significant fiscal challenge, the spread between Ontario bond yields and those of the Canadian federal government have widened by about 20 basis points so far this year, to land at about 80 basis points.

Economic growth projections have fallen

In the March budget, the Ontario government stuck with its plan to eliminate its deficit (which stands at about \$16 billion this year) gradually by fiscal 2017-18. The Province's debt burden was not expected to peak until fiscal year 2014-15 at a record 41% of GDP. Above all, the elimination of the deficit during a moderate growth environment would require holding spending growth down at a minimal rate of about 1.5% per year over the period, which would represent the most prolonged period of fiscal restraint in the post-war period -- no easy feat.

Since March, the news facing the government's fiscal position has been mixed, but overall still tilted toward an even more difficult fiscal environment than budgeted last year. Notably, since the outbreak of global financial turmoil in August, private-sector forecasters have been busy downgrading their medium-term growth outlook for Ontario. We show our revised projections relative to those of the 2011 budget and Liberal Party platform on the next page. In 2012, TD Economics is expecting nominal GDP to come in about 2 percentage points lower than factored into both documents. Based on the simple rule of thumb that each percentage point of nominal GDP leads to a reduction in revenues of about \$750 million, the cumulative reduction in nominal GDP will amount to a fiscal hit on the order of about \$2 billion over the next few years.

On the flip side, some of this impact would be offset by a lower-than-anticipated interest rates and, thus, debt service costs. Moreover, the release of the 2010-11 Public Accounts revealed that spending came in some \$2.4 billion lower than had been projected. Some of that downward adjustment will almost certainly carry forward to future years.

New spending initiatives total \$1.5 billion annually

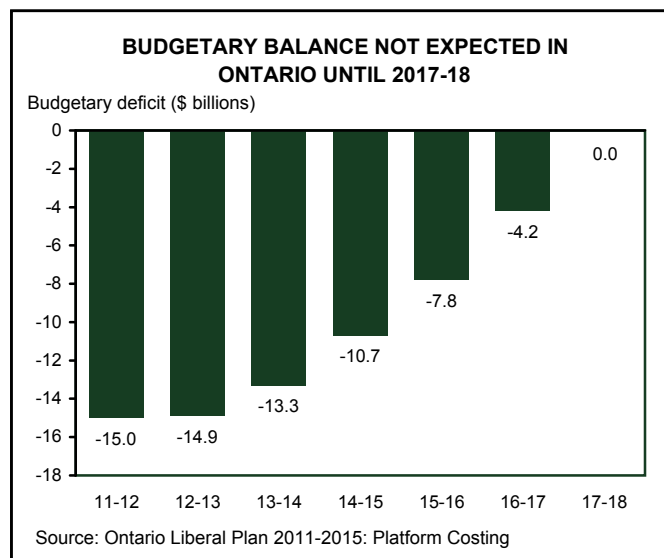
The government will also endeavour to make good on election promises. The Liberal platform includes spending promises amounting to about \$1.5 billion annually by the end of its four-year mandate. Key promises include:

- A 30% across-the-board postsecondary tuition grants for undergraduate studies;
- 60,000 new college and university spaces over five years; and
- Full-day kindergarten for all children by 2014; and
- \$35 billion, over three years, for infrastructure-related commitments.

The election promises are relatively modest by traditional standards. Still, the government will still need to find the fiscal room.

Minority governance adds a wrinkle

The next challenge relates to the government’s minority status. The Premier and his Cabinet will need to develop a strategy to get legislative approval for the government’s fiscal plan. This process is inherently more complicated in a



minority setting. This scenario will also mean that political calculations will play a much more important role as these economic and fiscal policy decisions are made. For your information, we have provided detailed campaign promises of the three parties in the appendix.

Bottom line

Now that the election is over, the government will need to continue along the path of reining in its deficit. If anything, this challenge has got more difficult since the budget was brought down in the Spring. An important milestone ahead of the next budget will be the release of the Drummond Commission report, which will recommend ways to improve the efficiency of public service delivery in Ontario.

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| ONTARIO ECONOMIC PLANNING ASSUMPTIONS | | | | |
|---------------------------------------|------------------------|------|------|------|
| | Annual, percent change | | | |
| | 2011 | 2012 | 2013 | 2014 |
| Real GDP Growth | | | | |
| 2011 Budget | 2.4 | 2.7 | 2.7 | 2.6 |
| 2011 Liberal Platform | 2.4 | 2.7 | 2.7 | 2.6 |
| TD Economics [^] | 2.3 | 2.1 | 2.7 | 2.5 |
| Nominal GDP Growth | | | | |
| 2011 Budget | 4.6 | 5.1 | 4.8 | 4.6 |
| 2011 Liberal Platform | 5.5 | 4.7 | 4.9 | 4.6 |
| TD Economics [^] | 4.9 | 3.2 | 4.3 | 4.4 |

Notes: [^]As at September 2011.
 Sources: Ontario Ministry of Finance; 2011 Liberal Platform; TD Economics.

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| PROVINCIAL PARTIES' STANCE ON MAJOR ISSUES | | | |
|--|---|--|---|
| | Liberals | Progressive Conservatives (PCs) | New Democratic Party (NDP) |
| Fiscal Plan | <ul style="list-style-type: none"> Return to a balanced budget by 2017-18. Commission on the Reform of Ontario's Public Services already in place will recommend ways to improve fiscal sustainability. | <ul style="list-style-type: none"> Return to a balanced budget by 2017-18. Health and education spending to be protected. Cabinet will be 20% smaller than at present. Civil servant cuts are also proposed, although no target is specified. Reduce the number of agencies, boards and commissions. Create <i>Truth in Government Act</i> to mandate sharing of information, contracts, grants, travel costs and expenses. | <ul style="list-style-type: none"> Return to a balanced budget by 2017-18. Conduct an expenditure management review to find savings within the current fiscal framework. |
| Business Initiatives | <ul style="list-style-type: none"> Continue with previously announced cuts to corporate and small business tax rates. | <ul style="list-style-type: none"> Plan to introduce a Small Business Bill of Rights which will include red tape reduction, greater ability to bid on government contracts and choice over mandatory smart meter energy pricing. Reduce basic corporate income tax rate from 11.5% to 10% by 2013. | <ul style="list-style-type: none"> Hold the line on previously announced cuts to corporate income tax rates. Create a 10% tax credit for companies that invest in buildings, machinery and equipment. Create a training tax credit for companies. Reduce the small business tax rate to 4%. |
| Personal and Payroll Taxes | <ul style="list-style-type: none"> Create Healthy Home Renovation Tax Credit worth up to \$1,500 for seniors. Give seniors the option to defer property tax increases until they sell their house. Double the Children's Activity Tax Credit from \$50 to \$100 per child. No changes proposed. | <ul style="list-style-type: none"> Let families reduce their personal taxable income through income sharing of up to \$50,000. Lower personal income taxes by 5% on the first \$75,000 of taxable income. Double the Caregiver Tax Credit for those who care for an elderly or critically ill family member. | <ul style="list-style-type: none"> No changes proposed. |
| Harmonized Sales Tax (HST) | <ul style="list-style-type: none"> No changes proposed. | <ul style="list-style-type: none"> Remove HST from home hydro bills and home heating. | <ul style="list-style-type: none"> Remove HST off of daily essentials (e.g., electricity, home heating). Remove HST from gasoline by one percentage point per year. |
| Wage and Social benefits | <ul style="list-style-type: none"> Plan to create a new Family Caregiver Leave program which will give up to eight weeks of job-protected time away from work. | <ul style="list-style-type: none"> Allow Ontario Works and Ontario Disability Support Program recipients who work part-time keep more benefits. Require social assistance recipients to be residents of Ontario for one year before collecting benefits. | <ul style="list-style-type: none"> Increase minimum wage to \$11 in 2011 and index it thereafter to cost of living changes. Reduce clawback of social assistance benefits for people with disabilities returning to the workforce. Ensure Ontario Works rates keep up with inflation. |
| Postsecondary Education | <ul style="list-style-type: none"> Establish 30% postsecondary tuition grant for undergraduate studies. Freeze annual student debt limit at \$7,300. Fund 60,000 new college and university spaces over five years. Increase postsecondary education funding by \$700 million over four years. | <ul style="list-style-type: none"> Eliminate Ontario Trillium Scholarships for international PhD students. Create up to 60,000 new college and university spaces. Create 200,000 new apprenticeship spaces over four years and have colleges carry a greater share of the responsibility for matching apprentices and employers. Encourage partnerships between government, the private sector and postsecondary institutions in Northern Ontario. | <ul style="list-style-type: none"> Freeze tuition for college, undergraduate and graduate students for four years. Eliminate provincial interest on Ontario student loans. Forgive student debt of new doctors who practice in under-served communities. |
| Other Education Initiatives | <ul style="list-style-type: none"> Expand full-day kindergarten to everyone by 2014. | <ul style="list-style-type: none"> Increase spending by \$2 billion at the end of the government's first term. Implement full-day kindergarten for all schools by 2014. | <ul style="list-style-type: none"> No policies proposed. |

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|--|--|--|--|
| | Liberals | Progressive Conservatives (PCs) | New Democratic Party (NDP) |
| Public Transit and Infrastructure | <ul style="list-style-type: none"> Expand transit service by delivering full-day, two-way GO train service on all corridors. Provide money-back guarantee to customers who experience a 15-minute arrival delay. Spend \$35 billion over the next three years on the infrastructure, of which \$600 million is dedicated to postsecondary projects. | <ul style="list-style-type: none"> Increase dedicated number of revenue from the provincial gas tax to transit, roads and other infrastructure projects. Spend \$35 billion over the three years on infrastructure. | <ul style="list-style-type: none"> Share cost of operating transit equally with municipalities in exchange for a commitment to freeze transit fares at current levels for four years. |
| Healthcare | <ul style="list-style-type: none"> Create Council on Childhood Obesity whose goal will be a 20% reduction of the childhood obesity rate within five years. Provide Health Care Coordinator to facilitate care between specialists and family doctors for seniors hospitalized within the previous year. Create "Active Aging Strategy" to develop policies which reflect the needs of an ageing populace. | <ul style="list-style-type: none"> Increase annual investments in healthcare by \$6 billion at the end of the first term. Introduce rigorous system of patient satisfaction and outcome measures. Establish wait time guarantees for emergency room visits. Add 5,000 new long-term care beds. Increase investments in home care. Increase residency placements for medical students from Ontario who are trained outside of Canada. | <ul style="list-style-type: none"> Cut emergency room wait times by half. Give Ombudsman oversight of hospital and health spending. Eliminate Local Health Integration Networks (LHINs) and replace them with local decision-making. Eliminate fees for ambulance service. Fund an additional one million hours of home care, over four years. Conduct a comprehensive review of home care policy with a goal of creating a new publicly owned and accountable home care system that reduces management and administration costs by 20%. Fund 50 new family healthcare clinics that will provide round-the-clock healthcare services to an additional 250,000 people by 2015. |
| Electricity and Energy | <ul style="list-style-type: none"> Replace coal plants with the use of clean energy measures. Accelerate plan to have 5% of all new cars electric by 2020, while investing \$80 million in charging stations and necessary infrastructure. | <ul style="list-style-type: none"> Remove Debt Retirement Charge from home hydro bills. End mandatory time-of-use pricing and unplug mandatory smart meters. Close Ontario Power Authority. End feed-in tariff program. Establish a Consumer Advocate at the Ontario Energy Board to help independently set hydro rates. Close coal powered plants by 2014. | <ul style="list-style-type: none"> Consolidate Ontario's electricity agencies. Have Ontario Energy Board set a gas price ceiling every week. Expand support for energy saving home retrofits. Hold the line on new nuclear plants until further investigation and analysis is done. |