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2017 QUEBEC ECONOMIC PLAN UPDATE

November 23, 2017

Investing the fiscal dividend in tax relief for Quebecers

- The Quebec government remains firmly on track to balance its budget this year and the next five years.
- The 2016-17 budget surplus of $2.4 billion was almost 10 times larger than projected.
- Quebecers will get more money in their pockets: personal income tax is cut and cheques to help with school supplies are on their way.
- Spending is boosted for health, education and the fight against poverty.
- Further material progress is made toward reducing the province's debt load.

On solid fiscal track

First off, as we suspected, Quebec's fiscal position last year turned out to be a lot stronger than the provincial government assumed when it prepared Budget 2017. The public accounts for 2016-17 published Tuesday showed a $2.4 billion surplus (*after* a $2.0 billion deposit into the Generations Funds). This was almost 10 times the $250 million surplus expected eights months ago. It also surpassed the $2.2 billion surplus recorded in 2015-16, which was the largest in the province's history (on a dollar-of-the-day basis). Years of tough budget medicine clearly turned things around in Quebec. Better yet for a government less than a year away from elections, the back-to-back bounties were structural in nature.

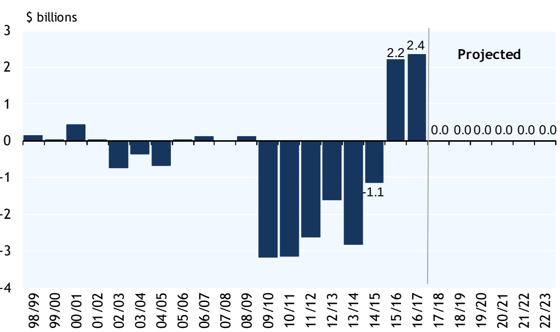
Room to give something back to Quebecers...

This created some room for Finance Minister Carlos Leitao to provide long-promised tax relief to Quebecers and to boost spending on priority items without abandoning his prudent approach to the province's finances. Indeed, in Tuesday's budget update Minister Leitao announced $11 billion in new 'investments' over six years. More than half of this amount ($6.3 billion) is dedicated to reducing the tax burden on individuals. The government is lowering the rate on the first personal income tax bracket from 16% to 15%, retroactive to January 1, 2017, and will send $100 cheques to families on July 1 every year to help cover the costs of school supplies. The government is allocating the remainder of the additional spending to the fight against poverty ($2.6 billion over six years), education and health ($1.1 billion), support for regional economies ($0.7 billion) and retirement income ($0.5 billion). The costs of these measures will total $1.3 billion in 2017-18 and ramp up to $1.8 billion by 2019-20. Such costs are well within the means of the government. Minister Leitao forecasts the budget to remain in balance over the entire six-year fiscal plan.

...without compromising the province's debt targets

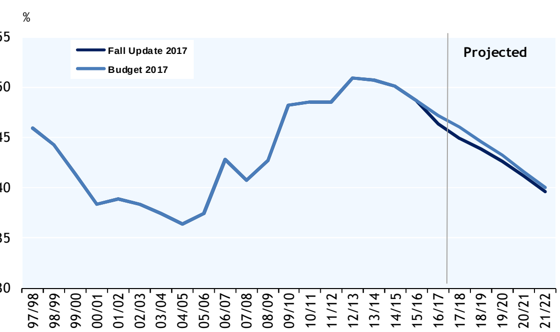
The other good news from the 2016-17 public accounts is that Quebec's net debt fell for a second-consecutive time last year by $3.3 billion to $182 billion as of March 31, 2017. The decline mainly reflected the $2.4 billion surplus be-

Quebec budget balance



Source: Ministère des Finances du Québec, RBC Economics Research

Net Debt as % of GDP



Source: Ministère des Finances du Québec, RBC Economics Research

Economic growth assumptions

	2016	2017	2018	2019	2020	2021
Real GDP growth (%)						
November 2017 Update	1.4	2.6	1.8	1.5	1.4	1.2
RBC	1.9	2.8	1.9	-	-	-
Nominal GDP growth (%)						
November 2017 Update	2.7	3.7	3.4	3.3	3.1	2.9
RBC	3.1	4.4	3.6	-	-	-

Source: Ministère des Finances du Québec, RBC Economics Research

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ing 'saved' and allocated to the province's stabilization reserve. As a share of GDP, net debt came in at 46.3% at the end of March 2017 or 0.9 percentage points lower than projected in Budget 2017. This was a gift that will keep on giving over the remainder of the fiscal plan because it lowered the entire trajectory of the net debt-to-GDP ratio even though future budget balances remain unchanged. The government now projects the ratio to fall to 44.9% in March 2018 and drift further down to 39.6% by the end of the fiscal plan in 2022. The slight improvement in the trajectory bodes well for the province to meet its longer-term debt targets.

Right-sizing the stabilization reserve

The government will use more than half of its $4.6 billion stabilization reserve over the coming years to fund its various measures. This is a right-sizing operation. The government judges that a lower amount of $1.8 billion would be sufficient to cope with the effects of a moderate economic downturn. The reserve was re-instituted on the back of the surprise $2.2 billion surplus in 2015-16. The $2.4 billion surplus in 2016-17 more than doubled the amount last year. By law, the Quebec government must allocate any unexpected surplus to the stabilization reserve. The government indicated that it will reduce the reserve every year until it reaches $1.8 billion by the end of 2020-21.

This year's financing program is increased

The Quebec government now expects its financing program to total $14.8 billion in 2017-18 or $3.5 billion more than expected in Budget 2017. The increase primarily reflects $4.5 billion in pre-financing for next year. The government indicated that 48% of its borrowing to date was done in foreign markets. The financing program is projected to rise to $20.3 billion in 2018-19.

Good news overall but focus on debt should remain a priority

There are plenty of good vibes coming out of Quebec these days. The provincial economy accounts for many of them. And the 2017 Quebec Economic Plan Update and the 2016-17 public accounts just provided quite a few more. The turnaround in Quebec's fiscal situation over the past few years has been quite impressive for sure. It was accomplished through a lot of hard work and sacrifices. So it makes sense to reward Quebecers (arguably the most heavily taxed in North America) with some tax relief. Especially so when it's done in a way that can be afforded. Still, the government is years away from completing its mission to fully restore its fiscal flexibility. The weight of Quebec's debt remains one of the higher ones among the provinces. As long as this is the case, the Quebec government has to make it a priority to keep that weight on a downward track.

Quebec's consolidated fiscal plan

($ millions)	Actual	Forecast					
	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
General Fund - total budgetary revenues	78,148	79,953	81,880	85,217	87,690	90,655	93,342
Own-source revenue	54,831	55,570	57,694	59,656	61,407	63,400	65,488
Government enterprises	4,735	4,122	3,863	3,995	4,151	4,300	4,236
Federal transfers	18,582	20,261	20,323	21,566	22,132	22,955	23,618
General Fund - total budgetary expenditures	76,919	80,078	83,004	85,398	87,732	90,008	92,613
Program spending	69,376	72,591	75,579	77,951	80,266	82,669	85,153
Interest on public debt	7,543	7,487	7,425	7,447	7,466	7,339	7,460
Net results of consolidated entities	3,133	2,425	2,529	2,561	3,263	3,460	3,796
Contingency reserve	-	100	100	100	100	200	200
Surplus/(Deficit)	4,362	2,200	1,305	2,280	3,121	3,907	4,325
Payments to the Generations Fund	(2,001)	(2,450)	(2,712)	(3,031)	(3,465)	(3,907)	(4,325)
Use of the stabalization reserve	-	250	1,407	751	344	-	-
Budgetary balance for the purposes of the Balanced Budget Act	2,361	-	-	-	-	-	-

Source: Quebec Ministry of Finance, RBC Economics Research

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