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Weaker hand-off, but new government charts path to balance by 2027-28

By Daren King, Warren Lovely & Taylor Schleich

Highlights

In its first official budget, a relatively fresh Manitoba government (elected in October 2023) tabled a fiscal plan that commits to addressing affordability pressures and 'rebuilding health care' while still forging a path to balance. One must first acknowledge that the fiscal year just ended was subject to a material restatement. Indeed, the deficit originally planned to be \$363 million (0.4% of GDP) jumped to nearly \$2 billion (2.2% of GDP) as spending and revenue both disappointed. However, the province expects to make serious progress on the deficit this year with healthy revenue gains (particularly via federal transfers) and better-controlled spending more than halving the shortfall (projected at \$796 million or 0.9% of GDP). Progress continues in the outer years of the fiscal plan, before an expected return to black ink in 2027-28. Despite the worse starting point, budgetary balance comes a year earlier than outlined in Budget 2023. Owing to the larger-than-planned deficit, Manitoba's net debt is estimated to end 2023-24 materially higher than projected in Budget 2023 (\$33.5 billion/37.5% of GDP vs. \$31.1 billion/34.6% of GDP). Ongoing budget shortfalls alongside tangible capital investments leaves net debt on an upward trajectory. Relative to GDP, debt levels will peak in 2025-26 before turning a bit lower thereafter. Debt servicing consumed a bit more than 10% of revenue in 2023-24 and while the debt service envelop will continue to grow, the relative 'interest bite' is projected to drop to 9.7% in 2024-25 (and holding around here thereafter). When it comes to long-term borrowing, Budget 2024 identifies a \$6.2 billion gross requirement for 2024-25, which is up a bit from the \$5.6 billion secured in 2023-24. Note that this reflects pre-funding six months of future cash needs, includes Crown requirements and is also boosted by sizeable maturities. New cash requirements (net of repayments) are a more modest \$2½ billion. Supply will moderate in future years with requirements of \$5.8 billion for 2025-26 and \$4.7 billion in 2026-27. Overall, Manitoba's fresh budget is consistent with what we're seeing across the provincial landscape. That is, in the face of slower growth and cost of living pressures, more red ink is being accumulated than previously expected. On the bright side, Manitoba's outsized 2023-24 deficit will quickly be brought under 1% of GDP and steadily chipped away at thereafter. Despite the much weaker starting point, a path to balance is still clearly telegraphed.

- **Economic outlook** – Thanks to its most diversified economy in the Confederation and historical population growth, Manitoba's economy remained resilient in 2023 despite restrictive monetary policy and high inflation. Indeed, it is estimated that real GDP in the province increased by 1.4% in 2023, above the 1.1% for Canada as a whole. More importantly for public finances, nominal GDP rose by 3.4% in 2023, a growth rate that is also above the 2.7% national average. Unlike the job market in some provinces which have not been able to fully absorb the strong demographic growth, Manitoba's job market is also standing out. Its unemployment rate was a mere 4.5% in February 2024, the lowest of all Canadian provinces and relatively stable compared with the 4.6% observed at the same time last year. As monetary policy, inflation and geopolitical issues cloud the outlook, economic growth in Manitoba is expected to slow in the coming year. Indeed, the Budget assumes real GDP growth of 0.6% in 2024 based on the average private sector forecast. Manitoba's real GDP is then expected to grow by 1.9% in 2025. When it comes to nominal GDP, the Budget assumes growth of 2.9% and 3.1% in 2024 and 2025, respectively. As for the labour market, job creation should start to lag population growth in 2024 due to a slower economy, with unemployment rate rising from 4.8% on average in 2023 to 5.7% in 2024 and 2025.
- **Outgoing fiscal year budget balance (2023-24)** – Like many provinces in Canada, Manitoba's budgetary position deteriorated over the course of the 2023-24 fiscal year. What was originally thought to be a small \$363 million (0.4% of GDP) deficit in last year's budget grew to \$1.6 billion (1.8% of GDP) in the Second Quarter Report and has since slid further to \$2.0 billion (2.2% of GDP) in today's Budget (Note this latest estimate reflects what was presented in last month's Third Quarter Report). What drove the additional red ink? It was a combination of both lower-than-planned revenue and higher-than-planned spending. On the revenue side, roughly two-thirds of the miss can be attributed to net income of Government Business Enterprises (specifically Manitoba Hydro) as inflows here are now expected to settle \$640 million (-54%) below Budget 2023 estimates. Specifically, low water conditions and lower net export revenues were to blame. Tax revenues also disappointed, landing \$406 million (-3.9%) below last year's guidance. On the expense side, pressure can almost entirely be traced to a single line item: Health, Seniors and Long-Term Care. Expenses in this department look to finish more than 9% above last year's estimate and in dollar terms, the \$702 million of additional outflows represents 95% of overall above-plan spending.
- **Medium-term fiscal outlook (2024-25 & beyond)** – After a significant fiscal restatement in what was a transition year for the province's legislature, the budgetary balance is set to improve markedly in 2024-25 even if a shortfall remains. Indeed, the deficit is expected to be more than halved this year—from \$2 billion in 2023-24 (2.2% of GDP) to \$796 million in 2024-25 (0.9% of GDP). The 2024-25 estimate also includes a \$100 million contingency which creates scope for a modest budgetary beat should it go unused. A smaller deficit is largely a function of higher revenues, as inflows are set to jump over 9% this year. The province sees tax receipts advancing at a healthy clip (+\$426 million or +4.3%) and it also sees net income from GBEs improving from last year (+\$276 million or +51%). However, the overall jump is predominantly a function of more federal transfer dollars (+\$1.2 billion or +16.7%). On the other

side of income statement, spending is seen growing at a more controlled 2.8% (compared to last year). The envelope that contributed most to last year's higher-than-planned deficit—Health, Seniors and Long-Term Care—is budgeted to increase just 1% in 2024-25. Education is expected to be the largest fiscal pressure point, as spending in these departments is expected to advance \$419 million (+7.8%). Beyond 2024-25, progress on the deficit will continue albeit at a slower pace. The province is signalling a \$532 million deficit in 2025-26 (0.6% of GDP) and a \$266 million deficit in 2026-27 (0.3% of GDP). Compared to last year's budget, there is \$1.05 billion more red ink across these three years (i.e., 2024-25 to 2026-27). Importantly, in the outermost year of the province's fiscal plan (i.e., 2027-28), an ever-so-slight surplus of \$18 million has been pencilled in. Note that this is technically one fiscal year earlier than promised in Budget 2023. Over these outer years of the forecast horizon, the province has assumed revenues will rise at a pace of 3.5%/year and program expenses will grow by 2.1%/year. Just like in 2024-25, a \$100 million contingency has been layered into these outer years too.

- **New initiatives** – As is often the case with provincial budgets, the primary focus of the Manitoba budget is health. Indeed, the 2024 Budget plans to hire 1,000 new healthcare workers, including 100 doctors, 210 nurses, 90 paramedics and 600 health care aids. Of the \$309.5 million earmarked to recruit, retain, and train more health care workers, \$66.7 million is included to increase bed capacity and reduce ER wait times. The Budget also plans to provide better care for seniors with an investment of \$22.3 million. The second focus of the Budget is to reduce costs for families and includes a number of measures to this end. After starting on January 1st for a period of six months due to the Imperial Oil pipeline shutdown, the government has announced the extension of the 14-cents-per-litre tax cut on gas for an additional three months. For an average single-vehicle family, that might represent savings of \$187.50 over the entirety of the nine-month tax holiday. On housing, the Budget announced the creation of a new \$1,500 homeowners' affordability tax credit that will begin in 2025 and will replace the existing school tax rebate and education property tax credit. The government also increased the Renters Tax Credit to \$575. Among other measures, the Budget doubles the maximum Fertility Treatment Tax Credit, provides free access to prescription birth control, decreases by 5% auto insurance rates, creates a \$4,000 rebate for new electric vehicles, and a \$2,500 rebate for used one.
- **Debt burden & interest bite** – As per Manitoba's recently released Q3 report, summary net debt is estimated to end the 2023-24 fiscal year at \$33.5 billion or 37.5% of nominal GDP. That's a material deterioration vs. the Budget 2023 plan (\$31.1 billion and 34.6% respectively), reflecting the much larger-than-planned budget deficit. It means Manitoba's net debt load took a step up last fiscal year, net debt-to-GDP having been 35.0% in 2022-23. Looking ahead, ongoing budget shortfalls alongside tangible capital investments leaves net debt on an upward trajectory, in level terms and when scaled to nominal GDP. At \$35.4 billion, the projected level of net debt comes March 2025 would be equivalent to 38.5% of GDP, compared to a weighted provincial average we currently estimate at 32%. It's expected that the debt burden will peak in 2025-26 at 39.1% before turning a bit lower thereafter. The province's stated aim of returning to balance by 2027-28 would be consistent with a falling debt ratio, this key metric seen at 38.3% by 2027-28. (For reference, the pre-COVID average was a snick above 35% of GDP.) We'd note an accounting change in the treatment of debt servicing costs (and related revenue) that was implemented after Budget 2023. Controlling for the new framework (which adds in Manitoba Hydro), debt service amounted to \$2.17 billion in 2023-24, consuming a bit more than 10% of revenue. While the debt service envelop will continue to grow, the relative 'interest bite' is projected to recede to 9.7% in 2024-25, holding at or near that level over the balance of the fiscal plan. Following from the economic outlook summarized earlier, the budget assumes a 4.2% average term borrowing rate for 2024-25. It is estimated that a 1%-pt change in all interest rates is worth roughly \$50 million to the annual interest bill.
- **Long-term borrowing requirement** – In fiscal 2023-24, Manitoba tapped debt capital markets for a total of \$5.6 billion, a material portion of which (\$2.7 billion) reflected six months of pre-borrowing towards 2024-25. Three quarters of last fiscal year's completed funding was taken out of the domestic market, the remaining one quarter secured via a USD1 billion 10-year trade and EUR30 million private placement. Under an assumption that the province once again pre-funds six months of future cash needs, Budget 2024 identifies a \$6.2 billion gross borrowing requirement for 2024-25. This total requirement includes Crown needs and is also boosted by sizeable maturities. For context, new cash requirements (net of repayments) are roughly \$2½ billion. As per the budget, the \$6.2 billion gross need for 2024-25 is meant to be a relative peak, the mid-term financing outlook showing a gross requirement of \$5.8 billion for 2025-26 followed by \$4.7 billion in 2026-27. Hydro has no new cash requirements in the mid-term outlook, as capital needs for this Crown are to internally funded. Regarding Manitoba's debt management strategy, a 'well-established domestic program' remains a primary objective, 10s and 30s core tenors (supplemented, as we saw in 2023-24, by the occasional 5-year or ultra-long for diversification purposes). International markets have historically been considered when costs are competitive vis-à-vis domestic funding levels, with foreign currency trades helping to diversify the investor base. Any/all international debt is swapped back to CAD, leaving the province with no net FX exposure. As noted, the province maintains a six-month cash buffer. In January 2024, the province increased its authorized limit on promissory notes (to \$1.5 billion) in order to bolster available liquidity.
- **Current long-term credit ratings** – S&P: A+, Stable | Moody's: Aa2, Stable | DBRS: A(High), Stable
[Refer to our Provincial Ratings Snapshot for additional colour on specific credit rating drivers/considerations]

Manitoba

\$000,000	Budget	Forecast	Budget	Projection		
	2023/24	2023/24	2024/25	2025/26	2026/27	2027/28

SUMMARY BUDGET

Revenue	22,377	21,476	23,337	24,127	24,992	25,866
Income taxes	5,532	5,239	5,588			
Other taxes	4,772	4,659	4,736			
Fees and other revenues	2,543	2,558	2,650			
Federal transfers	7,299	7,104	8,291			
Net income (loss), government business enterprises	1,181	542	818			
Sinking funds and other earnings	1,250	1,374	1,354			
Contingency	(200)	-	(100)	(100)	(100)	(100)

Expenditure	22,740	23,473	24,133	24,659	25,258	25,848
<i>of which Debt servicing</i>	<i>2,151</i>	<i>2,170</i>	<i>2,264</i>	<i>2,357</i>	<i>2,463</i>	<i>2,547</i>
Summary net income	(363)	(1,997)	(796)	(532)	(266)	18
Debt servicing as a % of revenues	9.6%	10.1%	9.7%	9.8%	9.9%	9.8%
Summary net income as a % of GDP	-0.4%	-2.2%	-0.9%	-0.6%	-0.3%	0.0%

SUMMARY NET DEBT

Beginning of year	29,415	30,263	33,514			
Summary net income	363	1,997	796			
Net investment in Tangible Capital Assets	1,279	1,254	1,111			
= Increase in net debt	1,642	3,251	1,907			
Summary net debt at the end of the fiscal year	31,057	33,514	35,421			
Summary net debt as a % of GDP	34.6%	37.5%	38.5%	39.1%	38.9%	38.3%

BORROWING REQUIREMENTS (\$ million)

Refinancing	3,472
New cash requirements	3,298
Less Repayments	779
Less Pre-borrowing	2,717
Plus Pre-funding	2,918
Total borrowing requirements	6,193
As of Manitoba Hydro	868

Source: Province of Manitoba, *Budget* documents

Economics and Strategy

Montreal Office

514-879-2529

Stéfane Marion

Chief Economist and Strategist
stefane.marion@nbc.ca

Kyle Dahms

Economist
kyle.dahms@nbc.ca

Alexandra Ducharme

Economist
alexandra.ducharme@nbc.ca

Matthieu Arseneau

Deputy Chief Economist
matthieu.arseneau@nbc.ca

Daren King, CFA

Economist
daren.king@nbc.ca

Angelo Katsoras

Geopolitical Analyst
angelo.katsoras@nbc.ca

Jocelyn Paquet

Economist
jocelyn.paquet@nbc.ca

Toronto Office

416-869-8598

Warren Lovely

Chief Rates and Public Sector Strategist
warren.lovely@nbc.ca

Taylor Schleich

Rates Strategist
taylor.schleich@nbc.ca

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