Manitoba

2013-2014 Budget Analysis

Key Findings

- This budget reflects an effort to reduce the deficit while maintaining priority spending. However, it does not advance a strategic long-term vision needed for Manitoba to secure a prosperous future.
- Measures to increase education, skills and workforce participation could be meaningful if pursued aggressively and if protracted federal-provincial negotiations on skills training programs can be avoided.
- Despite tax increases, the province will remain in the red. As a result, the government will have to work hard to find ways to support strategic economic initiatives in the coming year.
- The budget produced mixed results on business tax competitiveness. Increasing the small business tax threshold is a positive step, but raising capital taxes on financial institutions is not.
- The government highlighted the need to find opportunities to reduce the cost of government and increase efficiency. Steps to review existing funding and streamline internal operations to lower costs are critical to achieve that goal.

The Canada West Foundation is dedicated to building a western Canada in which our children will thrive and prosper. Our focus on provincial and federal government budgets reflects that priority. We are primarily concerned with the ***long-term*** directions that governments are setting in their budgets and less preoccupied with year-to-year changes in spending or in fiscal balances.

Detailed Analysis

In its budget preview, the Canada West Foundation identified four steps the Manitoba government could take that would lead to a more prosperous future for all residents. Those steps were:

1) Action to address current and future labour shortages.
2) Tax reforms that remove impediments to growth.
3) A balance between near-term deficit elimination and critical investments in long-term economic competitiveness.
4) Steps to improve value for money in government service delivery.

1

Action to address labour and skills shortages

The budget recognizes the importance of education and skills training to future prosperity in Manitoba. However, it contains only modest steps to address skills training issues.

In spite of its budget challenges, the Manitoba government demonstrated that education remains a spending priority. Overall government spending on all levels of education rose by 4.5% in the 2013 budget. Included in that total was a 3% increase in support for operating expenditures at universities. University tuition increases were capped at the rate of inflation.

The budget also announced that *Manitoba's Strategy for Sustainable Employment and a Stronger Labour Market* will be launched this spring. The strategy will focus on ensuring that employers have access to workers with specific skills and abilities while also creating sustainable, meaningful jobs. The budget suggests that the strategy will place heavy emphasis on helping disadvantaged Manitobans, particularly those who face challenges finding and retaining work.

Manitoba's budget was the first to be released after the federal government announced its new approach to financing skills training. Instead of transferring money to the provinces and territories, the federal government will put the onus on businesses to identify their own labour needs and take action to address them. Federal money will be delivered to employers and require matching funding from the provinces and businesses.

This carries a risk for Manitoba. The province has recognized the importance of skills development and sustainable employment. However, the new federal initiative will require negotiation with the provinces and territories before it can be implemented. History suggests that these inter-governmental negotiations can easily get bogged down, creating the danger that Manitoba may slow efforts to vigorously pursue its own skills training agenda while the details of the federal program are ironed out. Manitoba needs to act now.

2

Tax reforms to improve business competitiveness

In its budget preview, the Canada West Foundation suggested two measures that would complement recent efforts to improve the competitiveness of Manitoba's business tax structure. These were: a phase-out of the Health and Post Secondary Education Tax Levy – a payroll tax on larger businesses; and, consideration of a harmonized sales tax to replace the PST. Neither of these measures were in the budget. In fact, the idea of an HST was explicitly rejected.

However, the budget did include a number of business tax initiatives, some of which will be beneficial to the provincial economy, while at least one will not. On the positive side, small businesses in the province will have additional room to grow before being subject to income tax. Currently, Manitoba is the only province where businesses with less than $400,000 in income pay no corporate taxes. Effective January 1st 2014, that threshold will be raised to $425,000. Budget 2013 also included a number of other tax initiatives including the extension of a series of tax credits aimed at specific industries; the extension of the small business venture capital tax credit; and an increase in the manufacturing investment tax credit to offset the effect of the increase in the PST.

The one negative measure was an increase in the corporation capital tax on financial institutions from 4% to 5%, effective immediately. A capital tax is a tax on a company's assets, such as its facilities, machinery and equipment and applies regardless of a firm's profitability. Such taxes are not economically efficient because they provide a disincentive for businesses to reinvest in expanding their operations. Manitoba eliminated its general corporation capital tax in 2011 (financial institutions and Crown corporations excepted) for that very reason. Raising the capital tax on financial institutions is a step in the opposite direction. The revenues generated from this tax could have been found elsewhere with a less negative impact on the Manitoba economy, especially considering the important role played by insurance companies and other financial institutions in the province.

3

Striking a balance between fiscal responsibility and long-term economic competitiveness

As signalled in late 2012, the Manitoba government has backed away from its commitment to balance the provincial budget by 2014/15. The province had initially made that pledge in 2010, but a combination of factors, including costs associated with the 2011 flood and slower-than-expected economic growth, threw the plan off course.

Rather than implement austerity measures and cut overall spending, the government chose to increase tax revenues (most notably by raising the PST from 7% to 8%) and limit spending growth in non-core programs to gradually return to budget balance. The province now plans to eliminate the deficit in 2016/17, two years later than initially forecast.

As stated in the budget, all revenue from the PST increase is intended to be spent on infrastructure through the newly-created *Manitoba Building and Renewal Plan*. The budget also emphasized that flood protection infrastructure would be a key component of that plan, although it contained few details on the matter.

There can be a benefit to allocating the proceeds from a specific tax increase to strategic infrastructure spending and flood protection. If transparently applied, it can offer predictable funding and increase accountability for spending. However, the PST rate hike does not appear to meet these criteria. For additional PST revenues to be earmarked for infrastructure, they must be clearly and demonstrably linked to an *increase* in infrastructure spending or a *specific* infrastructure project. Otherwise, the rate hike is little more than a general tax increase with a purely notional attachment to a certain type of spending that may or may not have taken place anyway.

In summary, the Manitoba government chose to increase taxes to help address its budget balance problem rather than take drastic action on the expenditure side. This reflects the priorities articulated in the budget: families, social inclusion, poverty reduction and infrastructure. However, the budget does not contain a clear long-term economic vision. In light of its fiscal constraints, the government will have to work hard to find ways to advance a strategic agenda in the coming year.

4

Improving value for money in government service delivery

Budget 2013 reiterated the government's commitment to reducing costs and increasing the efficiency of public service delivery. The budget did not include any dramatic measures to that end, but built on measures taken in previous budgets and advanced plans set out in the November 2012 *Speech from the Throne*. Measures outlined in the budget include:

- → Integrating certain government operations;
- → Amalgamating regional offices of different government departments;
- → Containing administrative costs; and,
- → Reducing the size of the civil service by 600 people over three years.

The budget also noted that meeting government priorities and balancing the budget will require ongoing efforts to review existing funding and streamline internal operations. While there were no specific commitments or objectives identified in this budget, a concern for improving the efficiency of service delivery is important to ensure that Manitobans receive value for their tax dollars.

Manitoba Budget by the Numbers

Overview

The Manitoba government presented a cautious budget that will raise taxes and attempt to limit spending growth in order to gradually eliminate the provincial deficit by 2016/17. The budget projects a deficit of $518 million for the current fiscal year, a modest improvement over last year's estimated deficit of $583 million. However, the deficit last year came in significantly higher than forecast; the 2012 budget projected a fiscal shortfall of $460 million.

Revenues and Expenditures

The 2013 budget projects revenues to grow by 3.0% next year over 2012/13 levels. With relatively weak economic growth expected for the current year—the budget assumes GDP growth of 1.9% for 2013—the government is relying on tax increases to meet its revenue targets. As mentioned above, the most significant of these increases was a hike in the PST from 7% to 8%, effective July 1st. In addition, the province once again raised tobacco taxes, introduced a fuel tax for natural gas use in motor vehicles, and raised the cost of fishing licences.

Offsetting these revenue measures to some degree, the province raised the basic personal income tax exemption level by 2.8% (the inflation rate in the province last year was 1.6%). It also eliminated the PST on baby supplies and some other goods, introduced a tax credit on the construction of new rental housing and will eliminate school property taxes paid by seniors on their principal residences by 2015.

An additional challenge facing Manitoba on the revenue side is an anticipated drop in federal transfer payments in 2013/14. Federal transfers accounted for about one third of provincial revenues last year and the province expects those transfers to fall by 1.7% because of lower equalization payments and a reduction in funding for shared-cost programs.

Overall program spending is expected to rise by 3.1% in 2013/14. The government will increase health and education spending by 4.5% each. Those two expenditure lines account for more than two thirds of program spending in the province. The family services budget will also rise by 2.2%. All other government spending—about 25% total outlays—will be held flat. Debt-servicing costs will increase by $19 million this year as provincial government borrowing increases.

In the 2013 budget, the government announced $1.8 billion in capital investment. Of that total, $622 million will go to roads and highways, $578 million to health and education infrastructure and $333 million to housing. The budget does not include information on how this total compares to actual capital investment last year. (Consulting the previous budget reveals that the expected capital spending figure was $1.7 billion.)

Fiscal Information and Budget Projections → Manitoba
($millions)

	2008-2009	2009-2010	2010-2011	2011-2012	2012-2013e	2013-2014b
Tax Revenue	6,117	5,940	6,328	6,655	6,921	7,381
Non-Tax Revenue	6,648	6,725	6,912	7,200	6,843	6,801
Total Revenues	12,765	12,665	13,240	13,855	13,764	14,182
Program and Capital Expenditures	11,484	12,092	12,646	14,039	13,584	14,008
Interest on Debt	830	756	773	815	820	839
Total Expenditures	12,314	12,848	13,419	14,854	14,404	14,847
In-Year Adjustments/Lapse					-57	-150
2013 Spring Flood Contingency						30
Disaster Financial Assistance funds						-27
Net Income	**451**	**-183**	**-179**	**-999**	**-583**	**-518**
Summary Net Debt	**11,480**	**11,607**	**12,525**	**14,511**	**16,119**	**17,754**

Source: Canada West Foundation calculations using data from Manitoba Budget 2013.

Note: e= estimated, b=budgeted

Budget Reporting Issues and Concerns

Generally speaking, Manitoba budgets provide a very thorough documentation of the province's revenue and expenditure plans. There are, however, a few areas where the presentation and accuracy could be improved.

First, the province relies on unspecified in-year adjustments to improve its bottom line every year. These adjustments are never accounted for in subsequent budgets and obscure proper analysis.

Second, information on infrastructure and capital spending is not clearly laid out. The province stated that capital investments will total $1.8 billion in 2013/14 but this figure is not easily replicable using provincial revenue and expenditure estimates. Moreover, as mentioned above, no comparable figures are provided for actual spending in previous years.

Finally, Manitoba provides information on annual revenues and expenditures, as well as on net debt and borrowing requirements, but does not link the two. For example, in the current budget, the province has a projected deficit of $518 million, but net debt will increase by $1.6 billion. The province clearly lays out its pension liabilities and other borrowing requirements, but it would be useful to see a more direct link between the size of the deficit and the increase in debt.

This budget analysis was prepared by Canada West Foundation Senior Economist Michael Holden. The opinions expressed in this report are those of the author and are not necessarily those of the Canada West Foundation's Board of Directors, funders or advisors.

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