PRESS RELEASE **For immediate publication**

THE QUEBEC GOVERNMENT IS SINKING FURTHER INTO DEBT

Montreal, March 11, 2015 – "In Quebec, the issue is not so much the size of the government's debt, although there is cause for concern, but the context in which it has taken on that level of debt," says Robert Gagné, Director of the HEC Montréal Centre for Productivity and Prosperity. In a study analyzing the Quebec government's debt, researchers have shown that recurring budget deficits are creating a major debt spiral, with a particularly negative impact on the province's public finances.

"Beyond the debate surrounding the concepts used to determine the size of the debt, it must be understood that the real problem is budget deficits. The Quebec government has been accumulating deficits since the early 1970s, and continuing to drive itself further into debt. The end result is that the 'good debt' taken on by the government, that is the debt contracted to finance its investments, is gradually being converted to finance consumption," explains Gagné, co-author of the study. This situation has become even more problematic since the *Balanced Budget Act* was weakened in 2008.

Size and impact of the debt

The study shows, not very surprisingly, that the Quebec government's debt is systematically higher than in the other Canadian provinces, regardless of how it is calculated. And when it is compared with the 31 OECD member countries, it can be seen that only nine countries have a higher debt. Without sounding the alarm, the fact remains that a good number of these countries – Greece, Italy, Portugal, Spain, Japan – are facing serious economic problems.

Moreover, the sizeable indebtedness of the Quebec government is a relatively recent phenomenon. In the early 70s, the province's gross debt represented only 10% of its GDP, whereas today it is estimated at over 50%. While part of this increase can be explained by accounting reforms, the analysis shows that the debt burden had practically quadrupled even before reforms altered the accounting treatment of the debt in the late 90s.

Consequently, the government's indebtedness remains a worrisome issue. Given its huge debt, the Quebec government devotes a considerable proportion of its budget every year to paying interest, and this cuts into the amounts it should normally devote to financing its missions.

The *Balanced Budget Act*: an essential tool

While the *Balanced Budget Act* was fully in force, it allowed the Quebec government to maintain a certain level of budgetary rigour. As a result, the debt burden shrank constantly during the 2000s, for the first time in over 30 years.

Unfortunately, in 2009 the government suspended those sections of the Act that prevented it from running budgetary deficits. All the debt indicators began rising again as soon as the government set aside this budgetary control mechanism. Since then, the government has run numerous deficits and its debt burden has risen once again. The current circumstances bear some resemblance to the situation that prevailed in the late 90s, which led to the adoption of the first version of the *Balanced Budget Act*.

A few recommendations

In light of this analysis, one thing is clear: "Reaching a balanced budget must remain a priority for the Quebec government," maintains Gagné. "Especially since this government plans to invest $90 billion in the province's infrastructure over the next several years, investments that will be largely financed through debt. In addition to accelerating the rate of growth of government debt, these investments will considerably increase the proportion of the budget that will have to go to paying down the debt and servicing it – meaning the interest paid on government debt. The pressure on public finances will continue to grow and it will become even more difficult to attain a balanced budget. So the Quebec government should implement an effective and well-considered strategy for maintaining a balanced budget over many years, and do so starting immediately. It will have to set clear goals and, most importantly, respect them."

"To prevent the problem of indebtedness from becoming even more serious, the Quebec government should bring the *Balanced Budget Act* back into force, with some amendments," recommends Gagné. "First of all, the Act should apply more strictly, by prohibiting the government from running budgetary deficits even if they are less than $1 billion. On the other hand, the Act should give the government greater flexibility in absorbing deficits incurred because of economic fluctuations. Remember that, as it stands, the Act obliges the government to pay down its deficits within five years at most. This means that the government has to show exceptional rigour at a time when it is emerging from a crisis, although the economic context is generally not suited to that approach. Lastly, to make sure that debt-reduction efforts are not sidestepped again in future, the government should never again be able to suspend part or all of the *Balanced Budget Act* without the support of a broad consensus, for instance by obtaining two-thirds of votes in the National Assembly."

For more information:

- Consult the report (in French), entitled *L'heure juste sur la dette du gouvernement du Québec*, by Jonathan Deslauriers, Robert Gagné and Jonathan Paré.
- Download the press release *in French*.

About the Centre for Productivity and Prosperity

The HEC Montréal Centre for Productivity and Prosperity, created in 2009, has a twofold mission. First of all, it is devoted to research on productivity and prosperity, mainly in Quebec and in Canada as a whole. The Centre then shares its research findings, making them widely accessible and, in the end, educating people about productivity and prosperity. For more information on the Centre, visit www.hec.ca/cpp**.**

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